

TOLL BROTHERS INC  
Form 10-Q  
March 10, 2014

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q  
(Mark One)

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

For the quarterly period ended January 31, 2014

or

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-09186

TOLL BROTHERS, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of  
incorporation or organization)

23-2416878

(I.R.S. Employer  
Identification No.)

250 Gibraltar Road, Horsham, Pennsylvania

(Address of principal executive offices)

(215) 938-8000

(Registrant's telephone number, including area code)

19044

(Zip Code)

Not applicable

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T

(§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐ (Do not check if 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 ☒

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

At March 3, 2014, there were approximately 177,693,000 shares of Common Stock, \$.01 par value, outstanding.

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#### STATEMENT ON FORWARD-LOOKING INFORMATION

Certain information included in this report or in other materials we have filed or will file with the SEC (as well as information included in oral statements or other written statements made or to be made by us) contains or may contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. You can identify these statements by the fact that they do not relate to matters of strictly historical or factual nature and generally discuss or relate to estimates or other expectations regarding future events. They contain words such as “anticipate,” “estimate,” “expect,” “project,” “intend,” “plan,” “believe,” “may,” “can,” “could,” “might,” “should” and other words or phrases of similar meaning in connection with any discussion of future operating or financial performance. Such statements may include, but are not limited to, information related to: anticipated operating results; home deliveries; financial resources and condition; changes in revenues; changes in profitability; changes in margins; changes in accounting treatment; cost of revenues; selling, general and administrative expenses; interest expense; inventory write-downs; unrecognized tax benefits; anticipated tax refunds; sales paces and prices; effects of home buyer cancellations; growth and expansion; joint ventures in which we are involved; anticipated results from our investments in unconsolidated entities; the ability to acquire land and pursue real estate opportunities; the ability to gain approvals and open new communities; the ability to sell homes and properties; the ability to deliver homes from backlog; the ability to secure materials and subcontractors; the ability to produce the liquidity and capital necessary to expand and take advantage of opportunities; legal proceedings and claims; the anticipated benefits to be realized from the consummation of the Shapell acquisition; and post-closing asset sales.

From time to time, forward-looking statements also are included in other periodic reports on Forms 10-Q and 8-K, in press releases, in presentations, on our website and in other materials released to the public. Any or all of the forward-looking statements included in this report and in any other reports or public statements made by us are not guarantees of future performance and may turn out to be inaccurate. This can occur as a result of incorrect assumptions or as a consequence of known or unknown risks and uncertainties. Many factors mentioned in this report or in other reports or public statements made by us, such as government regulation and the competitive environment, will be important in determining our future performance. Consequently, actual results may differ materially from those that might be anticipated from our forward-looking statements.

Forward-looking statements speak only as of the date they are made. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise.

For a more detailed discussion of these factors, see the information under the captions “Risk Factors” and “Management's Discussion and Analysis of Financial Condition and Results of Operations” in our most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission and in this report.

When this report uses the words “we,” “us,” “our,” and the “Company,” they refer to Toll Brothers, Inc. and its subsidiaries, unless the context otherwise requires. References herein to “fiscal 2013,” “fiscal 2012,” “fiscal 2011,” “fiscal 2010,” “fiscal 2009,” and “fiscal 2008” refer to our fiscal years ending October 31, 2013, October 31, 2012, October 31, 2011, October 31, 2010, October 31, 2009, and October 31, 2008, respectively. References herein to “fiscal 2014” refer to our fiscal year ending October 31, 2014.

## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## TOLL BROTHERS, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(Amounts in thousands)

|  | January 31,<br>2014<br>(unaudited) | October 31,<br>2013 |
|--|------------------------------------|---------------------|
| <b>ASSETS</b>  |                                    |                     |
| Cash and cash equivalents  | \$1,190,489                        | \$772,972           |
| Marketable securities  | 13,017                             | 52,508              |
| Restricted cash  | 32,175                             | 32,036              |
| Inventory  | 5,235,647                          | 4,650,412           |
| Property, construction and office equipment, net   | 131,190                            | 131,320             |
| Receivables, prepaid expenses and other assets   | 240,034                            | 229,295             |
| Mortgage loans held for sale   | 58,131                             | 113,517             |
| Customer deposits held in escrow   | 45,834                             | 46,888              |
| Investments in and advances to unconsolidated entities   | 430,615                            | 403,133             |
| Investments in distressed loans  | 19,253                             | 36,374              |
| Investments in foreclosed real estate  | 79,267                             | 72,972              |
| Deferred tax assets, net of valuation allowances   | 284,603                            | 286,032             |
|  | <b>\$7,760,255</b>                 | <b>\$6,827,459</b>  |
| <b>LIABILITIES AND EQUITY</b>  |                                    |                     |
| <b>Liabilities</b>   |                                    |                     |
| Loans payable  | \$158,606                          | \$107,222           |
| Senior notes   | 2,921,851                          | 2,321,442           |
| Mortgage company warehouse loan  | 51,470                             | 75,000              |
| Customer deposits  | 218,747                            | 212,669             |
| Accounts payable   | 166,286                            | 167,787             |
| Accrued expenses   | 516,097                            | 522,987             |
| Income taxes payable   | 99,825                             | 81,188              |
| Total liabilities  | 4,132,882                          | 3,488,295           |
| <b>Equity</b>  |                                    |                     |
| Stockholders' equity   |                                    |                     |
| Preferred stock, none issued   |                                    |                     |
| Common stock, 177,553 and 169,353 shares issued at January 31, 2014 and October 31, 2013, respectively | 1,776                              | 1,694               |
| Additional paid-in capital   | 683,965                            | 441,677             |
| Retained earnings  | 2,937,583                          | 2,892,003           |
| Treasury stock, at cost — 2 and 0 shares at January 31, 2014 and October 31, 2013, respectively        | (81)                               | ) —                 |
| Accumulated other comprehensive loss   | (2,124)                            | ) (2,387 )          |
| Total stockholders' equity   | 3,621,119                          | 3,332,987           |
| Noncontrolling interest  | 6,254                              | 6,177               |
| Total equity   | 3,627,373                          | 3,339,164           |
|  | <b>\$7,760,255</b>                 | <b>\$6,827,459</b>  |

See accompanying notes



TOLL BROTHERS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in thousands, except per share data)

(Unaudited)

|                                     | Three months ended January 31, |           |
|-------------------------------------|--------------------------------|-----------|
|                                     | 2014                           | 2013      |
| Revenues                            | \$643,681                      | \$424,601 |
| Cost of revenues                    | 514,032                        | 345,937   |
| Selling, general and administrative | 97,870                         | 78,047    |
|                                     | 611,902                        | 423,984   |
| Income from operations              | 31,779                         | 617       |
| Other:                              |                                |           |
| Income from unconsolidated entities | 22,915                         | 3,083     |
| Other income - net                  | 16,541                         | 4,626     |
| Income before income taxes          | 71,235                         | 8,326     |
| Income tax provision                | 25,655                         | 3,894     |
| Net income                          | \$45,580                       | \$4,432   |
| Income per share:                   |                                |           |
| Basic                               | \$0.26                         | \$0.03    |
| Diluted                             | \$0.25                         | \$0.03    |
| Weighted-average number of shares:  |                                |           |
| Basic                               | 176,474                        | 169,064   |
| Diluted                             | 184,888                        | 171,903   |
| See accompanying notes              |                                |           |

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Amounts in thousands)

(Unaudited)

|   | Three months ended January 31, |         |
|---|--------------------------------|---------|
|   | 2014                           | 2013    |
| Net income  | \$45,580                       | \$4,432 |
| Other comprehensive income (loss), net of tax:          |                                |         |
| Change in pension liability                             | 53                             | (173 )  |
| Change in fair value of available-for-sale securities   | (31 )                          | 96      |
| Unrealized income on derivative held by equity investee | 241                            | 93      |
| Other comprehensive income                              | 263                            | 16      |
| Total comprehensive income                              | \$45,843                       | \$4,448 |
| See accompanying notes                                  |                                |         |

TOLL BROTHERS, INC.  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Amounts in thousands)  
(Unaudited)

|   | Three months ended January 31, |             |
|---|--------------------------------|-------------|
|   | 2014                           | 2013        |
| Cash flow used in operating activities:                                       |                                |             |
| Net income  | \$45,580                       | \$4,432     |
| Adjustments to reconcile net income to net cash used in operating activities: |                                |             |
| Depreciation and amortization   | 5,289                          | 6,525       |
| Stock-based compensation  | 7,669                          | 5,684       |
| Excess tax benefits from stock-based compensation                             | (789)                          | )           |
| Income from unconsolidated entities   | (22,915)                       | ) (3,083)   |
| Distributions of earnings from unconsolidated entities                        | 22,143                         | 2,413       |
| Income from distressed loans and foreclosed real estate                       | (6,619)                        | ) (3,011)   |
| Deferred tax provision  | 1,711                          | 2,306       |
| Deferred tax valuation allowances   | (448)                          | ) (216)     |
| Inventory impairments and write-offs  | 1,982                          | 709         |
| Change in fair value of mortgage loans receivable and derivative instruments  | 605                            | 554         |
| Gain on marketable securities   | (21)                           | )           |
| Changes in operating assets and liabilities                                   |                                |             |
| Increase in inventory   | (363,914)                      | ) (378,715) |
| Origination of mortgage loans   | (146,354)                      | ) (141,148) |
| Sale of mortgage loans  | 200,830                        | 176,830     |
| (Increase) decrease in restricted cash  | (139)                          | ) 13,519    |
| Increase in receivables, prepaid expenses and other assets                    | (7,274)                        | ) (8,256)   |
| Increase in customer deposits   | 7,132                          | 12,059      |
| (Decrease) increase in accounts payable and accrued expenses                  | (14,282)                       | ) 1,302     |
| Increase in income taxes payable  | 19,426                         | 2,274       |
| Net cash used in operating activities   | (250,388)                      | ) (305,822) |
| Cash flow (used in) provided by investing activities:                         |                                |             |
| Purchase of property and equipment — net                                      | (2,853)                        | ) (5,391)   |
| Purchase of marketable securities   |                                | ) (26,019)  |
| Sale and redemption of marketable securities                                  | 39,243                         | 38,775      |
| Investments in and advances to unconsolidated entities                        | (60,408)                       | ) (7,614)   |
| Return of investments in unconsolidated entities                              | 32,429                         | 17,311      |
| Investments in distressed loans and foreclosed real estate                    | (191)                          | ) (16,252)  |
| Return of investments in distressed loans and foreclosed real estate          | 17,574                         | 3,015       |
| Deposit - acquisition of a business   | (161,000)                      | )           |
| Net cash (used in) provided by investing activities                           | (135,206)                      | ) 3,825     |
| Cash flow provided by (used in) financing activities:                         |                                |             |
| Proceeds from issuance of senior notes  | 600,000                        |             |
| Debt issuance costs for senior notes  | (4,700)                        | )           |
| Proceeds from loans payable   | 275,334                        | 244,830     |
| Principal payments of loans payable   | (307,195)                      | ) (299,862) |
| Redemption of senior subordinated notes                                       |                                | ) (59,068)  |
| Net proceeds from issuance of common stock                                    | 220,357                        |             |
| Proceeds from stock-based benefit plans                                       | 18,529                         | 6,108       |



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|  |             |           |   |
|--|-------------|-----------|---|
| Excess tax benefits from stock-based compensation    | 789         |           |   |
| Receipts related to noncontrolling interest          | 81          |           |   |
| Purchase of treasury stock                           | (84         | ) (79     | ) |
| Net cash provided by (used in) financing activities  | 803,111     | (108,071  | ) |
| Net increase (decrease) in cash and cash equivalents | 417,517     | (410,068  | ) |
| Cash and cash equivalents, beginning of period       | 772,972     | 778,824   |   |
| Cash and cash equivalents, end of period             | \$1,190,489 | \$368,756 |   |
| See accompanying notes                               |             |           |   |

TOLL BROTHERS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Significant Accounting Policies

Basis of Presentation

The accompanying condensed consolidated financial statements include the accounts of Toll Brothers, Inc. (the "Company"), a Delaware corporation, and those majority-owned subsidiaries it controls. All significant intercompany accounts and transactions have been eliminated. Investments in 50% or less owned partnerships and affiliates are accounted for using the equity method unless it is determined that the Company has effective control of the entity, in which case the entity would be consolidated.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with the rules and regulations of the Securities and Exchange Commission ("SEC") for interim financial information. The October 31, 2013 balance sheet amounts and disclosures included herein have been derived from the Company's October 31, 2013 audited financial statements. Since the accompanying condensed consolidated financial statements do not include all the information and footnotes required by U.S. generally accepted accounting principles ("GAAP") for complete financial statements, the Company suggests that they be read in conjunction with the consolidated financial statements and notes thereto included in its Annual Report on Form 10-K for the fiscal year ended October 31, 2013. In the opinion of management, the accompanying unaudited condensed consolidated financial statements include all adjustments, which are of a normal recurring nature, necessary to present fairly the Company's financial position as of January 31, 2014, the results of its operations for the three-month periods ended January 31, 2014 and 2013, and its cash flows for the three-month periods ended January 31, 2014 and 2013. The results of operations for such interim periods are not necessarily indicative of the results to be expected for the full year.

Subsequent Events

Acquisition of Shapell Industries, Inc.

On February 4, 2014, the Company completed its previously announced acquisition of Shapell Industries, Inc. ("Shapell") pursuant to the Purchase and Sale Agreement (the "Purchase Agreement"), dated November 6, 2013, with Shapell Investment Properties, Inc. ("SIPI"). Pursuant to the Purchase Agreement, the Company acquired, for cash, all of the equity interests in Shapell from SIPI for an aggregate purchase price of approximately \$1.60 billion (the "Acquisition"). The Company acquired the single-family residential real property development business of Shapell, including a portfolio of approximately 4,950 home sites in California, some of which the Company expects to sell to other builders. As of the acquisition date, Shapell's home building operation had 11 active selling communities in Northern California and Southern California, within which it is focused on a select number of premium markets. In addition, the Company acquired approximately \$120.0 million of cash. As part of the acquisition, the Company assumed contracts to deliver approximately 126 homes with an aggregate value of approximately \$105.3 million. At January 31, 2014, the Company had deposited with an escrow agent \$161.0 million of the purchase price. This deposit is included in "Inventory" on the Company's Condensed Consolidated Balance Sheet at January 31, 2014.

The purchase price is subject to post-closing adjustment in accordance with the terms of the Purchase Agreement. The Company financed the Acquisition with a combination of \$370 million of borrowings under its \$1.035 billion unsecured revolving credit facility, \$485 million from the term loan facility described below, as well as with \$830 million in proceeds from debt and equity financings completed in November 2013.

Senior Unsecured Term Loan

On February 3, 2014, the Company entered into a 5-year senior, \$485 million, unsecured term loan facility (the "Term Loan Facility") with ten banks. The full amount of the Term Loan Facility was borrowed by the Company on February 3, 2014. The Company may select interest rates for the Term Loan Facility equal to (i) the London interbank offered rate ("LIBOR") plus an applicable margin, (ii) the base rate (which is defined as the greatest of (a) SunTrust Bank's prime rate, (b) the federal funds effective rate plus 0.5% and (c) one-month LIBOR plus 1%) plus an applicable margin or (iii) the federal funds / Euro rate (which is defined as the greater of (a) the sum of the federal funds effective rate plus an applicable margin plus 0.25% and (b) one-month LIBOR), with the applicable margin, in each case, based on the Company's leverage ratio. The initial interest rate on the Term Loan will be 1.72% per annum.



The Company and substantially all of its 100% owned home building subsidiaries are guarantors under the Term Loan Facility. The Term Loan Facility contains substantially the same financial covenants as the Company's five-year, unsecured revolving credit facility ("Credit Facility"). The Term Loan Facility will mature, and amounts owing under it will become due and payable, on February 3, 2019.

#### 364-Day Senior Unsecured Revolving Credit Facility

On February 4, 2014, the Company entered into a 364-day senior unsecured revolving credit facility (the "364-Day Facility") with five banks. The 364-Day Facility provides for an unsecured revolving credit facility to be made available to the Company, from time to time after February 4, 2014 and prior to February 3, 2015, in the amount of \$500 million. The Company intends for this facility to remain undrawn and its existence is to provide the Company additional liquidity should unforeseen circumstances arise. The Company may select interest rates for the 364-Day Facility equal to (i) LIBOR plus an applicable margin, (ii) the base rate (which is defined as the greatest of (a) Citibank's prime rate, (b) the federal funds effective rate plus 0.5% and (c) one-month LIBOR plus 1%) plus an applicable margin or (iii) the federal funds / Euro rate (which is defined as the greater of (a) the sum of the federal funds effective rate plus an applicable margin plus 0.25% and (b) one-month LIBOR), with the applicable margin, in each case, based on the Company's leverage ratio. The Company is obligated to pay an undrawn commitment fee. The Company and substantially all of its 100% owned home building subsidiaries are guarantors under the 364-Day Facility. The 364-Day Facility contains substantially the same financial covenants as the Company's Credit Facility. The 364-Day Facility will terminate, and amounts owing under the 364-Day Facility will become due and payable, on February 3, 2015.

## 2. Inventory

Inventory at January 31, 2014 and October 31, 2013 consisted of the following (amounts in thousands):

|  | January 31,<br>2014 | October 31,<br>2013 |
|--|---------------------|---------------------|
| Land controlled for future communities | \$254,549           | \$99,802            |
| Land owned for future communities      | 1,491,205           | 1,287,630           |
| Operating communities                  | 3,489,893           | 3,262,980           |
|  | \$5,235,647         | \$4,650,412         |

Operating communities include communities offering homes for sale, communities that have sold all available home sites but have not completed delivery of the homes, communities that were previously offering homes for sale but are temporarily closed due to business conditions or non-availability of improved home sites and that are expected to reopen within twelve months of the end of the fiscal period being reported on, and communities preparing to open for sale. The carrying value attributable to operating communities includes the cost of homes under construction, land and land development costs, the carrying cost of home sites in current and future phases of these communities, and the carrying cost of model homes.

Communities that were previously offering homes for sale but are temporarily closed due to business conditions that do not have any remaining backlog and are not expected to reopen within twelve months of the end of the fiscal period being reported on have been classified as land owned for future communities. Backlog consists of homes under contract but not yet delivered to the Company's home buyers ("backlog").

Information regarding the classification, number and carrying value of these temporarily closed communities, as of the date indicated, is provided in the table below.

|                                    | January 31,<br>2014 | October 31,<br>2013 |
|------------------------------------|---------------------|---------------------|
| Land owned for future communities: |                     |                     |
| Number of communities              | 22                  | 25                  |
| Carrying value (in thousands)      | \$141,356           | \$153,498           |
| Operating communities:             |                     |                     |
| Number of communities              | 15                  | 15                  |
| Carrying value (in thousands)      | \$91,984            | \$88,534            |



The amounts the Company provided for inventory impairment charges and the expensing of costs that it believed not to be recoverable, for the periods indicated, are shown in the table below (amounts in thousands).

|  | Three months ended January 31, |       |
|--|--------------------------------|-------|
|  | 2014                           | 2013  |
| Land controlled for future communities | \$682                          | \$9   |
| Operating communities                  | 1,300                          | 700   |
|  | \$1,982                        | \$709 |

See Note 13, "Fair Value Disclosures," for information regarding the number of operating communities that the Company tested for potential impairment, the number of operating communities in which it recognized impairment charges, the amount of impairment charges recognized, and the fair values of those communities, net of impairment charges.

See Note 15, "Commitments and Contingencies," for information regarding land purchase commitments.

At January 31, 2014, the Company evaluated its land purchase contracts to determine if any of the selling entities were variable interest entities ("VIEs") and, if they were, whether the Company was the primary beneficiary of any of them. Under these land purchase contracts, the Company does not possess legal title to the land and its risk is generally limited to deposits paid to the sellers and the creditors of the sellers generally have no recourse against the Company. At January 31, 2014, the Company determined that 86 land purchase contracts, with an aggregate purchase price of \$865.2 million, on which it had made aggregate deposits totaling \$47.6 million, were VIEs, and that it was not the primary beneficiary of any VIE related to its land purchase contracts.

Interest incurred, capitalized and expensed, for the periods indicated, was as follows (amounts in thousands):

|  | Three months ended January 31, |           |
|--|--------------------------------|-----------|
|  | 2014                           | 2013      |
| Interest capitalized, beginning of period  | \$343,077                      | \$330,581 |
| Interest incurred  | 39,944                         | 31,748    |
| Interest expensed to cost of revenues  | (25,440)                       | (19,974)  |
| Write-off against other income   | (317)                          | (88)      |
| Interest capitalized on investments in unconsolidated entities                                     | (2,457)                        | (1,363)   |
| Previously capitalized interest on investments in unconsolidated entities transferred to inventory | 1,811                          |           |
| Interest capitalized, end of period  | \$356,618                      | \$340,904 |

Inventory impairment charges are recognized against all inventory costs of a community, such as land, land improvements, cost of home construction and capitalized interest. The amounts included in the table directly above reflect the gross amount of capitalized interest without allocation of any impairment charges recognized. The Company estimates that, had inventory impairment charges been allocated on a pro-rata basis to the individual components of inventory, capitalized interest at January 31, 2014 and 2013 would have been reduced by approximately \$37.1 million and \$46.2 million, respectively.

### 3. Investments in and Advances to Unconsolidated Entities

The Company has investments in and advances to various unconsolidated entities. These entities include land development joint ventures, home building joint ventures, rental apartment joint ventures, Toll Brothers Realty Trust and Trust II, and a structured asset joint venture. At January 31, 2014, the Company had investments in and advances to these unconsolidated entities of \$430.6 million and was committed to invest or advance up to an additional \$76.9 million to these entities if they require additional funding. The Company's investments in these entities are accounted for using the equity method of accounting. At January 31, 2014, the Company had purchase commitments to acquire 115 home sites for approximately \$12.6 million. In addition, the Company expects to purchase approximately 3,800 additional home sites from several joint ventures in which it has interests. The purchase price of these home sites will be determined at a future date.

More specific information regarding the Company's investments in, advances to and future commitments to these entities is provided below.



## Land Development Joint Ventures

The Company has investments in and advances to a number of joint ventures with unrelated parties to develop land ("Land Development Joint Ventures"). Some of these Land Development Joint Ventures develop land for the sole use of the venture participants, including the Company, and others develop land for sale to the joint venture participants and to unrelated builders. The Company recognizes its share of earnings from the sale of home sites and other land by the Land Development Joint Ventures to other builders. With regard to home sites the Company purchases from the Land Development Joint Ventures, the Company adjusts its cost basis in those home sites by its share of the earnings/losses of the joint venture on the home sites the Company purchases. At January 31, 2014, the Company had approximately \$157.3 million invested in or advanced to the Land Development Joint Ventures and a funding commitment of \$26.0 million to three of the Land Development Joint Ventures which would be funded if additional investment in the ventures is required. At January 31, 2014, two of these joint ventures had aggregate loan commitments of \$105.0 million and outstanding borrowings against these commitments of \$73.2 million. At January 31, 2014, the Company had a purchase commitment to acquire 115 home sites from one of these Land Development Joint Ventures for an aggregate purchase price of \$12.6 million. In addition, the Company expects to purchase approximately 3,800 additional lots from several joint ventures in which it has interests. The purchase price of the lots will be determined at a future date.

In the first quarter of fiscal 2014, the Company entered into a joint venture with an unrelated party to develop a parcel of land in Texas. The joint venture expects to develop a master planned community consisting of up to 6,500 home sites and retail and commercial property. The Company has a 50% interest in this joint venture. Prior to the formation of the joint venture, the Company had entered into a land purchase agreement to acquire the land for approximately \$79.3 million. The Company contributed its rights under the purchase agreement to the joint venture and was reimbursed by the Company's joint venture partner for 50% of the costs the Company incurred prior to the formation of the joint venture. At January 31, 2014, the Company had an investment of \$40.6 million in this joint venture. The joint venture expects to obtain outside financing of approximately \$40.0 million to help fund the development of the property.

In the fourth quarter of fiscal 2013, the Company entered into a joint venture with an unrelated party to develop a parcel of land in Maryland. The property consists of 945 acres which the joint venture expects to develop into approximately 1,300 home sites. The Company has a 50% interest in this joint venture. The current plan is to develop the property and sell approximately 50% of the home sites to each of the members of the joint venture. The Company contributed \$11.8 million of cash to the joint venture. At January 31, 2014, the Company had an investment of \$11.9 million in this joint venture.

In the second quarter of fiscal 2013, the Company entered into a joint venture with an unrelated party to develop a parcel of land in Texas as a master planned community consisting of approximately 2,900 lots. The Company has a 50% interest in this joint venture. The joint venture expects to develop the property in multiple phases and sell groups of lots to the members of the joint venture and to other home builders. The Company contributed \$15.5 million of cash to the joint venture. The joint venture entered into a \$25.0 million line of credit with a bank, secured by a deed of trust on the property which can be expanded up to \$40.0 million under certain conditions. At January 31, 2014, the joint venture had \$24.8 million of borrowings under this line of credit. At January 31, 2014, the Company had an investment of \$20.3 million in this joint venture and was committed to make additional contributions to this joint venture of up to \$12.5 million.

The Company has a 50% interest in a joint venture that owns and is developing a master planned community in Orange County, California, consisting of over 2,000 home sites. At January 31, 2014, the joint venture owned approximately 1,200 home sites. At January 31, 2014, the Company had an investment of \$78.2 million in this joint venture and was committed to make additional contributions to this joint venture of up to \$10.0 million of additional funds to this joint venture, if needed. The joint venture has an \$80.0 million credit facility from a bank to fund the development of the property. At January 31, 2014, the venture had \$48.4 million borrowed under the facility.

## Home Building Joint Ventures



At January 31, 2014, the Company had an aggregate of \$175.9 million of investments in and advances to various joint ventures with unrelated parties to develop approximately 640 luxury for-sale homes. At January 31, 2014, the Company had \$27.6 million of funding commitments to two of these joint ventures.

Rental Apartment Joint Ventures

At January 31, 2014, the Company had an aggregate of \$74.8 million of investments in and advances to several joint ventures with unrelated parties to develop luxury for-rent residential apartments ("Rental Apartment Joint Ventures"), commercial space, and a hotel. At January 31, 2014, the Company had \$23.3 million of funding commitments to these joint ventures. At January 31, 2014, four of these joint ventures had aggregate loan commitments of \$319.8 million and outstanding borrowings against these commitments of \$16.6 million.

In the first quarter of 2014, two of the Company's Rental Apartment Joint Ventures entered into \$126.0 million of construction loan agreements to finance construction of multi-family residential apartments in suburban Philadelphia and northern New Jersey. At January 31, 2014, these ventures had no borrowings under the new facilities.

In the fourth quarter of fiscal 2013, the Company entered into a joint venture with an unrelated party to develop a 287-unit luxury for-rent residential apartment building in the Capitol Riverfront of Washington, D.C. on land that the Company owned and conveyed to the joint venture. The Company has a 50% interest in this joint venture. As part of the Company's initial capital contribution, it contributed land and improvements with a fair value of \$27.1 million to the joint venture and subsequently received a cash distribution of \$12.5 million to align the capital accounts of each of the members of the joint venture. The joint venture entered into a \$54.0 million construction loan agreement with a bank to finance the development of this project. At January 31, 2014, the joint venture had no borrowings under the construction loan agreement. At January 31, 2014, the Company had an investment of \$14.6 million in this joint venture.

In the second quarter of fiscal 2013, the Company entered into a joint venture with an unrelated party to develop a luxury, 38-story for-rent residential apartment building and retail space in Jersey City, New Jersey on land that the Company owned and conveyed to the joint venture. The Company has a 50% interest in this joint venture. As part of the Company's initial capital contribution, it contributed land and improvements with a fair value of \$28.8 million to the joint venture and subsequently received distributions of \$10.2 million and a \$1.2 million payment by the joint venture on our behalf to align the capital accounts of each of the members of the joint venture. The joint venture entered into a \$120.0 million construction loan agreement with a bank to finance the development of this project. At January 31, 2014, the joint venture had no borrowings under the construction loan agreement. At January 31, 2014, the Company had an investment of \$25.5 million in this joint venture and was committed to make additional contributions to this joint venture of up to \$4.9 million.

#### Toll Brothers Realty Trust and Trust II

In fiscal 2005, the Company, together with the Pennsylvania State Employees Retirement System ("PASERS"), formed Toll Brothers Realty Trust II ("Trust II") to invest in commercial real estate opportunities. Trust II is owned 50% by the Company and 50% by an affiliate of PASERS. In December 2013, Trust II sold substantially all of its assets to an unrelated party. As a result of this sale, the Company realized income of approximately \$23.5 million in the first quarter of fiscal 2014 representing its share of the gain on the sale which is included in "Income from unconsolidated entities" on the Company's Condensed Consolidated Statement of Operations. In December 2013, the Company received a \$20.0 million cash distribution from Trust II. At January 31, 2014, the Company had an investment of \$6.4 million in Trust II. In addition, in the first quarter of fiscal 2014, the Company recognized the \$2.9 million previously deferred gains on the Company's initial sales of the properties to Trust II; this gain is included in "Other income - net" on the Company's Condensed Consolidated Statement of Operations.

In 1998, prior to the formation of Trust II, the Company formed Toll Brothers Realty Trust ("Trust") to invest in commercial real estate opportunities. The Trust is effectively owned one-third by the Company; one-third by Robert I. Toll, Bruce E. Toll (and members of his family), Douglas C. Yearley, Jr. and former members of the Company's senior management; and one-third by an affiliate of PASERS. As of January 31, 2014, the Company had a negative investment in the Trust of \$0.9 million resulting primarily from a loss recognized by the Trust in the fourth quarter of fiscal 2013. The Company provides development, finance and management services to the Trust and recognized fees under the terms of various agreements in the amounts of \$0.6 million in each of the three-month periods ended January 31, 2014 and 2013.

#### Structured Asset Joint Venture

The Company, through Gibraltar Capital and Asset Management LLC ("Gibraltar"), is a 20% participant with two unrelated parties that purchased a 40% interest in an entity that owns and controls a portfolio of loans and real estate ("Structured Asset Joint Venture"). At January 31, 2014, the Company had an investment of \$22.6 million in this Structured Asset Joint Venture.

#### Guarantees

The unconsolidated entities in which the Company has investments generally finance their activities with a combination of partner equity and debt financing. In some instances, the Company and its partners have guaranteed

debt of certain unconsolidated entities which may include any or all of the following: (i) project completion including any cost overruns, in whole or in part, (ii) repayment guarantees, generally covering a percentage of the outstanding loan, (iii) indemnification of the lender as to environmental matters affecting the unconsolidated entity, (iv) a hazardous material indemnity that holds the lender harmless against any obligations for which the lender may incur liability resulting from the threat or presence of any hazardous or toxic substances at or near the property covered by a loan, and (v) indemnification of the lender from “bad boy acts” of the unconsolidated entity.

In some instances, the guarantees provided in connection with loans to an unconsolidated entity are joint and several. In these situations, the Company generally has a reimbursement agreement with its partner that provides that neither party is responsible for more than its proportionate share of the guarantee; however, if a joint venture partner does not have adequate financial resources to meet its obligations under the reimbursement agreement, the Company may be liable for more than its proportionate share.

The Company believes that, as of January 31, 2014, in the event it becomes legally obligated to perform under a guarantee of the obligation of an unconsolidated entity due to a triggering event, the collateral should be sufficient to repay a significant portion of the obligation. If it is not, the Company and its partners would need to contribute additional capital to the venture. At January 31, 2014, the unconsolidated entities that have guarantees related to debt had loan commitments aggregating \$424.8 million and had borrowed an aggregate of \$89.8 million. The term of these guarantees generally range from 22 months to 48 months. The Company estimates that the maximum potential exposure under these guarantees, if the full amount of the loan commitments were borrowed, would be \$424.8 million before any reimbursement from the Company's partners. Based on the amounts borrowed at January 31, 2014, the Company's maximum potential exposure under these guarantees is estimated to be approximately \$89.8 million before any reimbursement from the Company's partners.

In addition, the Company has guaranteed approximately \$11.5 million of ground lease payments and insurance deductibles for three joint ventures.

As of January 31, 2014, the estimated aggregate fair value of the guarantees was approximately \$2.0 million. The Company has not made payments under any of the guarantees, nor has it been called upon to do so.

#### Variable Interest Entities

At January 31, 2014, the Company determined that three of its joint ventures were VIEs under the guidance within FASB Accounting Standards Codification ("ASC") 810, "Consolidation." The Company has, however, concluded that it was not the primary beneficiary of the VIEs because the power to direct the activities of these VIEs that most significantly impact their performance was shared by the Company and the VIEs' other members. Business plans, budgets and other major decisions are required to be unanimously approved by all members. Management and other fees earned by the Company are nominal and believed to be at market rates and there is no significant economic disproportionality between the Company and other members.

The information presented below regarding the investments, commitments and guarantees in unconsolidated entities deemed to be VIEs is also included in the information provided above. At January 31, 2014 and October 31, 2013, the Company's investments in its unconsolidated joint ventures deemed to be VIEs, which are included in "Investments in and advances to unconsolidated entities" in the accompanying Condensed Consolidated Balance Sheets, totaled \$27.1 million and \$22.9 million, respectively. At January 31, 2014, the maximum exposure of loss to the Company's investments in unconsolidated joint ventures that are VIEs is limited to its investment in the unconsolidated VIEs, except with regard to \$37.7 million of additional commitments to the VIEs and \$9.5 million of guarantees under ground lease agreements. At October 31, 2013, the maximum exposure to loss of the Company's investments in unconsolidated joint ventures that are VIEs is limited to its investment in the unconsolidated VIEs, except with regard to a \$41.7 million additional commitment to fund the joint ventures and a \$9.6 million guaranty of ground lease payments.

#### Joint Venture Condensed Financial Information

The condensed balance sheets, as of the dates indicated, and the condensed statements of operations and comprehensive income for the periods indicated, for the unconsolidated entities in which the Company has an investment, aggregated by type of business, are included below (in thousands). The column titled "Rental Property Joint Ventures" includes the Rental Apartment Joint Ventures and Toll Brothers Realty Trust and Trust II described above.

## Condensed Balance Sheets:

|  | January 31, 2014                         |                                       |                                      |   |             |
|--|--|---------------------------------------|--------------------------------------|---|-------------|
|  | Land<br>Development<br>Joint<br>Ventures | Home<br>Building<br>Joint<br>Ventures | Rental<br>Property Joint<br>Ventures | Structured<br>Asset<br>Joint<br>Venture | Total       |
| Cash and cash equivalents                                  | \$29,003                                 | \$24,860                              | \$32,191                             | \$25,835                                | \$111,889   |
| Inventory  | 448,357                                  | 381,163                               | 395                                  |   | 829,915     |
| Non-performing loan portfolio                              |  |                                       |                                      | 97,801                                  | 97,801      |
| Rental properties  |  |                                       | 126,237                              |   | 126,237     |
| Rental properties under<br>development                     |  |                                       | 152,190                              |   | 152,190     |
| Real estate owned ("REO")                                  |  |                                       |                                      | 190,217                                 | 190,217     |
| Other assets (1)   | 10,330                                   | 68,288                                | 13,412                               | 155,925                                 | 247,955     |
| Total assets   | \$487,690                                | \$474,311                             | \$324,425                            | \$469,778                               | \$1,756,204 |
| Debt (1)   | \$139,801                                | \$10,927                              | \$195,642                            | \$155,900                               | \$502,270   |
| Other liabilities  | 25,310                                   | 23,784                                | 18,489                               | 1,380                                   | 68,963      |
| Members' equity  | 322,579                                  | 439,600                               | 110,294                              | 124,999                                 | 997,472     |
| Noncontrolling interest                                    |  |                                       |                                      | 187,499                                 | 187,499     |
| Total liabilities and equity                               | \$487,690                                | \$474,311                             | \$324,425                            | \$469,778                               | \$1,756,204 |
| Company's net investment in<br>unconsolidated entities (2) | \$157,293                                | \$175,904                             | \$74,843                             | \$22,575                                | \$430,615   |

  

|  | October 31, 2013                         |                                       |                                      |   |             |
|--|--|---------------------------------------|--------------------------------------|---|-------------|
|  | Land<br>Development<br>Joint<br>Ventures | Home<br>Building<br>Joint<br>Ventures | Rental<br>Property Joint<br>Ventures | Structured<br>Asset<br>Joint<br>Venture | Total       |
| Cash and cash equivalents                                  | \$30,826                                 | \$31,164                              | \$35,014                             | \$40,097                                | \$137,101   |
| Inventory  | 350,150                                  | 338,814                               | 4,998                                |   | 693,962     |
| Non-performing loan portfolio                              |  |                                       |                                      | 107,411                                 | 107,411     |
| Rental properties  |  |                                       | 164,325                              |   | 164,325     |
| Rental properties under<br>development                     |  |                                       | 133,081                              |   | 133,081     |
| Real estate owned ("REO")                                  |  |                                       |                                      | 202,259                                 | 202,259     |
| Other assets (1)   | 12,700                                   | 70,180                                | 18,526                               | 155,921                                 | 257,327     |
| Total assets   | \$393,676                                | \$440,158                             | \$355,944                            | \$505,688                               | \$1,695,466 |
| Debt (1)   | \$135,200                                | \$11,977                              | \$235,226                            | \$155,900                               | \$538,303   |
| Other liabilities  | 21,015                                   | 19,636                                | 9,461                                | 379                                     | 50,491      |
| Members' equity  | 237,461                                  | 408,545                               | 111,257                              | 139,764                                 | 897,027     |
| Noncontrolling interest                                    |  |                                       |                                      | 209,645                                 | 209,645     |
| Total liabilities and equity                               | \$393,676                                | \$440,158                             | \$355,944                            | \$505,688                               | \$1,695,466 |
| Company's net investment in<br>unconsolidated entities (2) | \$142,448                                | \$166,271                             | \$68,711                             | \$25,703                                | \$403,133   |

Included in other assets of the Structured Asset Joint Venture at January 31, 2014 and October 31, 2013 is \$155.9 (1) million of restricted cash held in a defeasance account which will be used to repay debt of the Structured Asset Joint Venture.

(2)

Differences between the Company's net investment in unconsolidated entities and its underlying equity in the net assets of the entities is primarily a result of the acquisition price of an investment in a land development joint venture in fiscal 2012 which was in excess of the Company's pro-rata share of the underlying equity, impairments related to the Company's investments in unconsolidated entities, a loan made to one of the entities by the Company, interest capitalized on the Company's investment, and distributions from entities in excess of the carrying amount of the Company's net investment.

## Condensed Statements of Operations and Comprehensive Income:

|  | For the three months ended January 31, 2014 |                                       |                                      |   |            |   |
|--|---|---------------------------------------|--------------------------------------|---|------------|---|
|  | Land<br>Development<br>Joint<br>Ventures    | Home<br>Building<br>Joint<br>Ventures | Rental<br>Property Joint<br>Ventures | Structured<br>Asset<br>Joint<br>Venture | Total      |   |
| Revenues   | \$1,544                                     | \$11,581                              | \$9,449                              | \$283                                   | \$22,857   |   |
| Cost of revenues   | 681   | 10,374                                | 3,971                                | 2,350                                   | 17,376     |   |
| Other expenses   | 255   | 999                                   | 12,055                               | 459                                     | 13,768     |   |
| Total expenses   | 936   | 11,373                                | 16,026                               | 2,809                                   | 31,144     |   |
| Gain on disposition of loans and REO                                 |   |                                       |                                      | 3,908                                   | 3,908      |   |
| Income (loss) from operations  | 608   | 208                                   | (6,577)                              | 1,382                                   | (4,379)    | ) |
| Other income   | 1   | 39                                    | 42,858                               | 123                                     | 43,021     |   |
| Net income   | 609   | 247                                   | 36,281                               | 1,505                                   | 38,642     |   |
| Less: income attributable to noncontrolling interest                 |   |                                       |                                      | (903)                                   | (903)      | ) |
| Net income attributable to controlling interest                      | 609   | 247                                   | 36,281                               | 602                                     | 37,739     |   |
| Other comprehensive income   |   |                                       | 786                                  |   | 786        |   |
| Total comprehensive income   | \$609                                       | \$247                                 | \$37,067                             | \$602                                   | \$38,525   |   |
| Company's equity in earnings (losses) of unconsolidated entities (3) | \$(32)                                      | ) \$182                               | \$23,750                             | \$(985)                                 | ) \$22,915 |   |

|  | For the three months ended January 31, 2013 |                                       |                                      |   |          |   |
|--|---|---------------------------------------|--------------------------------------|---|----------|---|
|  | Land<br>Development<br>Joint<br>Ventures    | Home<br>Building<br>Joint<br>Ventures | Rental<br>Property Joint<br>Ventures | Structured<br>Asset<br>Joint<br>Venture | Total    |   |
| Revenues   | \$1,627                                     | \$8,970                               | \$9,682                              | \$9,705                                 | \$29,984 |   |
| Cost of revenues   | 1,219                                       | 7,105                                 | 4,293                                | 10,338                                  | 22,955   |   |
| Other expenses   | 191   | 464                                   | 5,495                                | 1,058                                   | 7,208    |   |
| Total expenses   | 1,410                                       | 7,569                                 | 9,788                                | 11,396                                  | 30,163   |   |
| Gain on disposition of loans and REO                             |   |                                       |                                      | 26,892                                  | 26,892   |   |
| Income (loss) from operations                                    | 217   | 1,401                                 | (106)                                | 25,201                                  | 26,713   |   |
| Other income   | 3   | 14                                    | 5                                    | 79                                      | 101      |   |
| Net income (loss)  | 220   | 1,415                                 | (101)                                | 25,280                                  | 26,814   |   |
| Less: income attributable to noncontrolling interest             |   |                                       |                                      | (15,168)                                | (15,168) | ) |
| Net income (loss) attributable to controlling interest           | 220   | 1,415                                 | (101)                                | 10,112                                  | 11,646   |   |
| Other comprehensive income                                       |   |                                       | 302                                  |   | 302      |   |
| Total comprehensive income                                       | \$220                                       | \$1,415                               | \$201                                | \$10,112                                | \$11,948 |   |
| Company's equity in earnings (losses) of unconsolidated entities | \$(98)                                      | ) \$710                               | \$558                                | \$1,913                                 | \$3,083  |   |

(3)

Differences between the Company's equity in earnings (losses) of unconsolidated entities and the underlying net income (loss) of the entities is primarily a result of prior impairments related to the Company's investment in (3) unconsolidated entities, distributions from entities in excess of the carrying amount of the Company's net investment, and the Company's share of the entities' profits related to home sites purchased by the Company which reduces the Company's cost basis of the home sites.

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## 4. Investments in Distressed Loans and Foreclosed Real Estate

## Investments in Distressed Loans

The Company's investments in distressed loans consisted of the following as of the dates indicated (amounts in thousands):

|                            | January 31,<br>2014 | October 31,<br>2013 |
|----------------------------|---------------------|---------------------|
| Unpaid principal balance   | \$36,465            | \$63,381            |
| Discount on acquired loans | (17,212)            | (27,007)            |
| Carrying value             | \$19,253            | \$36,374            |

The Company's investments in distressed loans includes performing loans and non-performing loans and also includes investments in loan participations classified as secured borrowings under ASC 860, "Transfers and Servicing."

For acquired distressed loans where it is probable that the Company will collect less than the contractual amounts due under the terms of the loan based, at least in part, on the assessment of the credit quality of the borrowers, the loans are accounted for under ASC 310-30, "Loans and Debt Securities Acquired with Deteriorated Credit Quality" ("ASC 310-30"). Under ASC 310-30, provided the Company does not presently have the intention to utilize real estate secured by the loans for use in its operations or to significantly improve the collateral for resale, the amount by which the future cash flows expected to be collected at the acquisition date exceeds the estimated fair value of the loan, or accretible yield, is recognized in "Other income - net" over the estimated remaining life of the loan using a level yield methodology. The difference between the contractually required payments of the loan as of the acquisition date and the total cash flows expected to be collected, or nonaccretible difference, is not recognized.

The accretible yield activity for the Company's investments in distressed loans accounted for under ASC 310-30 for the three-month periods ended January 31, 2014 and 2013 was as follows (amounts in thousands):

|                              | Three months ended January 31, |          |
|------------------------------|--------------------------------|----------|
|                              | 2014                           | 2013     |
| Balance, beginning of period | \$6,606                        | \$17,196 |
| Additions                    | 169                            |          |
| Deletions                    | (3,183)                        | (2,387)  |
| Accretion                    | (502)                          | (1,403)  |
| Balance, end of period       | \$3,090                        | \$13,406 |

Additions primarily represent the reclassification to accretible yield from nonaccretible yield and the impact of impairments. Deletions primarily represent loan dispositions, which include foreclosure of the underlying collateral and resulting removal of the loans from the accretible yield portfolios, and reclassifications from accretible yield to nonaccretible yield. The reclassifications between accretible and nonaccretible yield and the accretion of interest income are based on various estimates regarding loan performance and the value of the underlying real estate securing the loans. As the Company continues to gather additional information regarding the loans and the underlying collateral, the accretible yield may change. Therefore, the amount of accretible income recorded in the three-month periods ended January 31, 2014 and 2013 is not necessarily indicative of future results.

The Company may acquire distressed loans where it has determined that (1) it is possible to collect all contractual amounts due under the terms of the loan, (2) it expects to utilize the real estate secured by the loans in its operations, or (3) forecasted cash flows cannot be reasonably estimated. For non-performing loans acquired meeting any of these conditions, in accordance with ASC 310-10, "Receivable," ("ASC 310-10"), the loans are classified as nonaccrual and interest income is not recognized. When a loan is classified as nonaccrual, any subsequent cash receipt is accounted for using the cost recovery method. For performing loans, payments are applied to principal and interest in accordance with the terms of the loan when received. As of January 31, 2014 and October 31, 2013, the Company had investments in non-performing loans, accounted for in accordance with ASC 310-10, of \$11.7 million and \$21.4 million, respectively. At October 31, 2013, the Company had investments in performing loans of \$0.8 million. The Company had no investments in performing loans as of January 31, 2014.



# Foreclosed Real Estate Owned (REO)

The table below provides, for the periods indicated, the activity in REO (amounts in thousands):

|                              | Three months ended January 31, |          |
|------------------------------|--------------------------------|----------|
|                              | 2014                           | 2013     |
| Balance, beginning of period | \$72,972                       | \$58,353 |
| Additions                    | 7,165                          | 11,040   |
| Sales                        | (808)                          | (439)    |
| Impairments                  |                                | (15)     |
| Depreciation                 | (62)                           | (175)    |
| Balance, end of period       | \$79,267                       | \$68,764 |

As of January 31, 2014, approximately \$18.9 million and \$60.4 million of REO was classified as held-for-sale and held-and-used, respectively. As of January 31, 2013, approximately \$5.9 million and \$62.8 million of REO was classified as held-for-sale and held-and-used, respectively. For the three-month periods ended January 31, 2014 and 2013, the Company recorded gains of \$1.5 million and \$0.6 million, respectively, from acquisitions of REO through foreclosure.

## General

The Company's earnings from Gibraltar's operations, excluding its investment in the Structured Asset Joint Venture, are included in "Other income - net" in its Condensed Consolidated Statements of Operations. In the three-month periods ended January 31, 2014 and 2013, the Company recognized \$4.3 million and \$0.2 million of earnings (excluding earnings from its investment in the Structured Asset Joint Venture), respectively, from Gibraltar's operations.

## 5. Credit Facilities, Senior Notes and Mortgage Company Loan Facility

### Credit Facility

On August 1, 2013, the Company entered into an \$1.035 billion ("Aggregate Credit Commitment") unsecured, five-year Credit Facility with 15 banks which extends to August 1, 2018. Up to 75% of the Aggregate Credit Commitment is available for letters of credit. The Credit Facility has an accordion feature under which the Company may, subject to certain conditions set forth in the agreement, increase the Credit Facility up to a maximum aggregate amount of \$2.0 billion. The Company may select interest rates for the Credit Facility equal to (i) LIBOR plus an applicable margin or (ii) the lenders' base rate plus an applicable margin, which in each case is based on the Company's credit rating and leverage ratio. The Company is obligated to pay an undrawn commitment fee which is based on the average daily unused amount of the Aggregate Credit Commitment and the Company's credit ratings and leverage ratio. Any proceeds from borrowings under the Credit Facility may be used for general corporate purposes.

Under the terms of the Credit Facility, the Company is not permitted to allow its maximum leverage ratio (as defined in the Credit Agreement) to exceed 1.75 to 1.00 and is required to maintain a tangible net worth (as defined in the Credit Facility) of no less than approximately \$2.42 billion. Under the terms of the Credit Agreement, at January 31, 2014, the Company's leverage ratio was approximately 0.51 to 1.00 and its tangible net worth was approximately 3.57 billion. Based upon the minimum tangible net worth requirement at January 31, 2014, the Company's ability to repurchase its common stock is limited to approximately 1.67 billion.

At January 31, 2014, the Company had no outstanding borrowings under the Credit Facility but had outstanding letters of credit of approximately \$71.1 million. As part of the Shapell acquisition, the Company borrowed \$370 million under the Credit Facility on February 3, 2014. The Company repaid \$170 million of the borrowing on February 12, 2014 and the remainder was repaid on February 26, 2014.

### Term Loan Facility and 364-Day Facility

In February 2014, the Company entered into a Term Loan Facility and a 364-Day Facility. See Note 1 - "Significant Accounting Policies - Subsequent Events" for more information.

## Senior Notes

At January 31, 2014, the Company, through Toll Brothers Finance Corp, had nine issues of Senior Notes outstanding with an aggregate principal amount of \$2.93 billion.

In November 2013, the Company issued \$350 million principal amount of 4.0% Senior Notes due 2018 (the "4.0% Senior Notes") and \$250 million principal amount of 5.625% Senior Notes due 2024 (the "5.625% Senior Notes"). The Company received \$596.2 million of net proceeds from the issuance of the 4.0% Senior Notes and the 5.625% Senior Notes.

In September 2013, the Company repaid the \$104.8 million of outstanding 5.95% Senior Notes due September 15, 2013.

On April 3, 2013, the Company issued \$300 million principal amount of 4.375% Senior Notes due 2023 (the "4.375% Senior Notes") at par. The Company received \$298.1 million of net proceeds from this issuance of 4.375% Senior Notes.

On May 13, 2013, the Company issued an additional \$100.0 million principal amount of 4.375% Senior Notes at a price equal to 103% of par value. The Company received \$102.3 million of net proceeds from this additional issuance of 4.375% Senior Notes.

In November 2012, the Company repaid the \$59.1 million of outstanding 6.875% Senior Notes due November 15, 2012.

## Mortgage Company Loan Facility

In July 2013, TBI Mortgage Company ("TBI Mortgage"), the Company's wholly-owned mortgage subsidiary, amended its Master Repurchase Agreement (the "Repurchase Agreement") with Comerica Bank. The purpose of the Repurchase Agreement is to finance the origination of mortgage loans by TBI Mortgage and it is accounted for as a secured borrowing under ASC 860, "Transfers and Servicing." The Repurchase Agreement, as amended, provides for loan purchases of up to \$50 million, subject to certain sublimits. In addition, the Repurchase Agreement provides for an accordion feature under which TBI Mortgage may request that the aggregate commitments under the Repurchase Agreement be increased to an amount up to \$75 million for a short period of time. The Repurchase Agreement, as amended, expires on July 22, 2014 and bears interest at LIBOR plus 2.00% per annum, with a minimum rate of 3.00%. At January 31, 2014, the Company had \$51.5 million of outstanding borrowings under the Repurchase Agreement.

## 6. Accrued Expenses

Accrued expenses at January 31, 2014 and October 31, 2013 consisted of the following (amounts in thousands):

|   | January 31,<br>2014 | October 31,<br>2013 |
|---|---------------------|---------------------|
| Land, land development and construction | \$ 135,523          | \$ 152,674          |
| Compensation and employee benefits      | 107,080             | 111,561             |
| Insurance and litigation                | 91,820              | 89,104              |
| Warranty                                | 42,688              | 43,819              |
| Interest                                | 46,500              | 25,675              |
| Commitments to unconsolidated entities  | 4,260               | 3,804               |
| Other                                   | 88,226              | 96,350              |
|   | \$516,097           | \$522,987           |

The Company accrues for expected warranty costs at the time each home is closed and title and possession are transferred to the home buyer. Warranty costs are accrued based upon historical experience. The table below provides, for the periods indicated, a reconciliation of the changes in the Company's warranty accrual (amounts in thousands):

|   | Three months ended January 31,<br>2014 | 2013     |
|---|--|----------|
| Balance, beginning of period                                      | \$43,819                               | \$41,706 |
| Additions – homes closed during the period                        | 3,097                                  | 2,289    |
| Increase (decrease) in accruals for homes closed in prior periods | 344                                    | (267)    |
| Charges incurred  | (4,572)                                | (2,487)  |

|                        |          |          |
|------------------------|----------|----------|
| Balance, end of period | \$42,688 | \$41,241 |
|------------------------|----------|----------|

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## 7. Income Taxes

The table below provides, for the periods indicated, reconciliations of the Company's effective tax rate from the federal statutory tax rate (amounts in thousands):

|   | Three months ended January 31, |        |       |        |
|---|--------------------------------|--------|-------|--------|
|   | 2014                           |        | 2013  |        |
|   | \$                             | %*     | \$    | %*     |
| Federal tax provision at statutory rate         | 24,932                         | 35.0   | 2,914 | 35.0   |
| State tax provision, net of federal benefit     | 2,985                          | 4.2    | 346   | 4.2    |
| Domestic production activities deduction        | (1,833                         | ) (2.6 | )     |        |
| Other permanent differences                     | (1,014                         | ) (1.4 | )     |        |
| Valuation allowance – reversed                  | (448                           | ) (0.6 | (216  | ) (2.6 |
| Accrued interest on anticipated tax assessments | 786                            | 1.1    | 1,166 | 14.0   |
| Other   | 247                            | 0.3    | (316  | ) (3.8 |
| Income tax provision                            | 25,655                         | 36.0   | 3,894 | 46.8   |

\* Due to rounding, amounts may not add.

The Company currently operates in 20 states and is subject to various state tax jurisdictions. The Company estimates its state tax liability based upon the individual taxing authorities' regulations, estimates of income by taxing jurisdiction, and the Company's ability to utilize certain tax-saving strategies. Based on the Company's estimate of the allocation of income or loss among the various taxing jurisdictions and changes in tax regulations and their impact on the Company's tax strategies, the Company estimated its rate for state income taxes at 6.5% for fiscal 2014 and 2013. For state tax purposes, due to past and projected losses in certain jurisdictions where the Company does not have carryback potential and/or cannot sufficiently forecast future taxable income, the Company has recognized net cumulative valuation allowances against its state deferred tax assets of \$55.3 million and \$55.7 million as of January 31, 2014 and October 31, 2013, respectively.

## 8. Stock-Based Benefit Plans

The Company grants stock options, restricted stock and various types of restricted stock units to its employees and its non-employee directors. Additionally, the Company has an employee stock purchase plan that allows employees to purchase Company stock at a discount.

Beginning in fiscal 2012, the Company changed the mix of stock-based compensation to its employees (other than certain senior executives) by reducing the number of stock options it grants and, in their place, issued non-performance based restricted stock units ("RSUs") as a form of compensation. The Company also replaced its stock price-based restricted stock unit ("Stock Price-Based RSUs") awards for certain senior executives with a performance-based restricted stock ("Performance-Based RSUs") award program.

Information regarding the amount of total stock-based compensation expense and tax benefit recognized by the Company, for the periods indicated, is as follows (amounts in thousands):

|   | Three months ended January 31, |         |
|---|--------------------------------|---------|
|   | 2014                           | 2013    |
| Total stock-based compensation expense recognized | \$7,669                        | \$5,684 |
| Income tax benefit recognized                     | \$2,972                        | \$2,079 |

At January 31, 2014 and October 31, 2013, the aggregate unamortized value of outstanding stock-based compensation awards was approximately \$37.8 million and \$19.9 million, respectively.

Information about the Company's more significant stock-based compensation programs is outlined below.

## Stock Options

The fair value of each option award is estimated on the date of grant using a lattice-based option valuation model that uses assumptions noted in the following table. The lattice-based option valuation model incorporates ranges of assumptions for inputs, which are disclosed in the table below. Expected volatilities were based on implied volatilities from traded options on the Company's stock, historical volatility of the Company's stock and other factors. The expected lives of options granted were derived from the historical exercise patterns and anticipated future patterns and represent the period of time that options granted are expected to be outstanding; the range given below results from certain groups of employees exhibiting different behaviors. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

The weighted-average assumptions and the fair value used for stock option grants in fiscal 2014 and 2013 were as follows:

|   | 2014            | 2013            |
|---|-----------------|-----------------|
| Expected volatility   | 36.44% - 44.71% | 44.04% - 48.13% |
| Weighted-average volatility   | 42.71%          | 46.70%          |
| Risk-free interest rate   | 1.45% - 2.71%   | 0.64% - 1.56%   |
| Expected life (years)   | 4.55 - 9.02     | 4.48 - 8.88     |
| Dividends   | none            | none            |
| Weighted-average grant date fair value per share of options granted | \$14.26         | \$13.05         |

Stock compensation expense, related to stock options, for the periods indicated, was as follows (amounts in thousands):

|                                | 2014    | 2013    |
|--------------------------------|---------|---------|
| Three months ended January 31, | \$4,030 | \$3,475 |

## Performance-Based Restricted Stock Units

The Executive Compensation Committee of the Company's Board of Directors ("Executive Compensation Committee") approved awards of Performance-Based RSUs relating to shares of the Company's common stock to certain of its senior management. The Performance-Based RSUs are based on the attainment of certain performance metrics of the Company in the fiscal year of grant if the performance targets are met. The number of shares underlying the Performance-Based RSUs that will be issued to the recipients may range from 90% to 110% of the base award depending on actual performance as compared to the target performance goals. The Performance-Based RSUs vest over a four-year period provided the recipients continue to be employed by the Company or serve on the board of directors of the Company (as applicable) as specified in the award document.

The value of the Performance-Based RSUs was determined to be equal to the estimated number of shares of the Company's common stock to be issued multiplied by the closing price of the Company's common stock on the New York Stock Exchange ("NYSE") on the later of the date the performance goals were approved by the Executive Compensation Committee, or on the date the Performance-Based RSUs were granted ("Valuation Date"). The Company evaluates the performance goals quarterly and estimates the number of shares underlying the Performance-Based RSUs that are probable of being issued. Information regarding the issuance, valuation assumptions and amortization of the Company's Performance-Based RSUs issued in fiscal 2014 and 2013 is provided below.

|   | 2014     | 2013     |
|---|----------|----------|
| Number of shares underlying Performance-Based RSUs to be issued                               | 288,667  | 302,511  |
| Closing price of the Company's common stock on Valuation Date                                 | \$35.16  | \$37.78  |
| Aggregate fair value of Performance-Based RSUs to be issued (in thousands)                    | \$10,150 | \$11,429 |
| Performance-Based RSU expense recognized in the three months ended January 31, (in thousands) | \$2,071  | \$514    |

Note: The fiscal 2014 number of shares underlying Performance-Based RSUs to be issued and their aggregate fair value is estimated.





Information regarding the aggregate number of outstanding Performance-Based RSUs and the aggregate unamortized value of the outstanding Performance-Based RSUs, as of the date indicated, is provided below.

|   | January 31,<br>2014 | October 31,<br>2013 |
|---|---------------------|---------------------|
| Aggregate outstanding Performance-Based RSUs                          | 961,354             | 672,687             |
| Cumulative unamortized value of Performance-Based RSUs (in thousands) | \$16,198            | \$8,120             |

#### Stock Price-Based Restricted Stock Units

Information regarding the amortization of the Company's Stock Price-Based RSUs, for the periods indicated, is provided below (amounts in thousands):

|                                | 2014  | 2013  |
|--------------------------------|-------|-------|
| Three months ended January 31, | \$231 | \$562 |

Information regarding the aggregate number of outstanding Stock Price-Based RSUs and aggregate unamortized value of the outstanding Stock Price-Based RSUs, as of the date indicated, is provided below:

|   | January 31,<br>2014 | October 31,<br>2013 |
|---|---------------------|---------------------|
| Aggregate outstanding Stock Price-Based RSUs                          | —                   | 306,000             |
| Cumulative unamortized value of Stock Price-Based RSUs (in thousands) | \$—                 | \$231               |

In December 2013 and 2012, the Company distributed 306,000 and 200,000 shares, respectively, of stock pursuant to a Stock Price-Based RSU award.

#### Non-Performance Based Restricted Stock Units

The Company issued RSUs to various officers, employees and non-employee directors. The value of the RSUs was determined to be equal to the number of shares of the Company's common stock to be issued pursuant to the RSUs, multiplied by the closing price of the Company's common stock on the NYSE on the date the RSUs were awarded. Information regarding these RSUs issued in the three months ended January 31, 2014 and 2013 is as follows:

|   | 2014    | 2013    |
|---|---------|---------|
| Number of RSUs issued   | 99,336  | 94,080  |
| Closing price of the Company's common stock on date of issuance | \$35.16 | \$32.22 |
| Aggregate fair value of RSUs issued (in thousands)              | \$3,493 | \$3,031 |

Information regarding the amortization of the Company's RSUs, for the periods indicated, is as follows (amounts in thousands):

|                                | 2014    | 2013    |
|--------------------------------|---------|---------|
| Three months ended January 31, | \$1,311 | \$1,112 |

Information regarding the aggregate number of outstanding RSUs and aggregate unamortized value of the outstanding RSUs, as of the date indicated, is as follows:

|   | January 31,<br>2014 | October 31,<br>2013 |
|---|---------------------|---------------------|
| Aggregate outstanding RSUs                          | 307,798             | 225,252             |
| Cumulative unamortized value of RSUs (in thousands) | \$3,852             | \$1,706             |

# 9. Employee Retirement Plans

The Company has two unfunded supplemental retirement plans ("SERPs"). The table below provides, for the periods indicated, costs recognized and payments made related to its SERPs (amounts in thousands):

|  | Three months ended January 31, |       |
|--|--------------------------------|-------|
|  | 2014                           | 2013  |
| Service cost                             | \$118                          | \$118 |
| Interest cost                            | 318                            | 261   |
| Amortization of prior service obligation | 161                            | 210   |
| Amortization of unrecognized losses      | 3                              | 36    |
| Total costs                              | \$600                          | \$625 |
| Benefits paid                            | \$233                          | \$233 |

# 10. Accumulated Other Comprehensive (Loss) Income

The tables below provide, for the periods indicated, the components of accumulated other comprehensive (loss) income (amounts in thousands):

|   | Three months ended January 31, 2014 |                               |                        |            |
|---|-------------------------------------|-------------------------------|------------------------|------------|
|   | Employee retirement plans           | Available-for-sale securities | Derivative instruments | Total      |
| Balance, beginning of period  | \$(2,112)                           | ) \$ (5                       | ) \$(270               | ) \$(2,387 |
| Other comprehensive (loss) income before reclassifications                    | (77                                 | ) (29                         | ) 393                  | 287        |
| Gross amounts reclassified from accumulated other comprehensive income (loss) | 164                                 | (21                           | )                      | 143        |
| Income tax (expense) benefit  | (34                                 | ) 19                          | (152                   | ) (167     |
| Other comprehensive income (loss), net of tax                                 | 53                                  | (31                           | ) 241                  | 263        |
| Balance, end of period  | \$(2,059                            | ) \$ (36                      | ) \$(29                | ) \$(2,124 |
|   | Three months ended January 31, 2013 |                               |                        |            |
|   | Employee retirement plans           | Available-for-sale securities | Derivative instruments | Total      |
| Balance, beginning of period  | \$(4,446                            | ) \$ 180                      | \$(553                 | ) \$(4,819 |
| Other comprehensive (loss) income before reclassifications                    | (519                                | ) 138                         | 151                    | (230       |
| Gross amounts reclassified from accumulated other comprehensive income (loss) | 247                                 |                               |                        | 247        |
| Income tax (expense) benefit  | 99                                  | (42                           | ) (58                  | ) (1       |
| Other comprehensive income (loss), net of tax                                 | (173                                | ) 96                          | 93                     | 16         |
| Balance, end of period  | \$(4,619                            | ) \$ 276                      | \$(460                 | ) \$(4,803 |

Reclassifications for the amortization of the employee retirement plans are included in "Selling, general and administrative" expense in the Condensed Consolidated Statements of Operations. See Note 9 for additional information.

Reclassifications for the realized loss on available-for-sale securities are included in "Other income - net" in the Condensed Consolidated Statements of Operations.

# 11. Stock Issuance & Stock Repurchase Program

## Stock Issuance

In November 2013, in anticipation of the Shapell acquisition, the Company issued 7.2 million shares of its common stock, par value \$0.01 per share, at a price to the public of \$32.00 per share. The Company received \$220.4 million of net proceeds from the issuance.

## Stock Repurchase Program

In March 2003, the Company's Board of Directors authorized the repurchase of up to 20 million shares of its common stock, par value \$.01, from time to time, in open market transactions or otherwise, for the purpose of providing shares for its various employee benefit plans.

The table below provides, for the periods indicated, information about the Company's share repurchase program:

|  | Three months ended January 31, |         |
|--|--------------------------------|---------|
|  | 2014                           | 2013    |
| Number of shares purchased (in thousands)            | 3                              | 3       |
| Average price per share                              | \$33.23                        | \$32.59 |
| Remaining authorization at January 31 (in thousands) | 8,266                          | 8,764   |

## 12. Income per Share Information

The table below provides, for the periods indicated, information pertaining to the calculation of income per share, common stock equivalents, weighted-average number of anti-dilutive options and shares issued (amounts in thousands except per share amounts):

|  | Three months ended January 31, |         |
|--|--------------------------------|---------|
|  | 2014                           | 2013    |
| Numerator:   |                                |         |
| Net income as reported   | \$45,580                       | \$4,432 |
| Plus: Interest and costs attributable to 0.5% Exchangeable Senior Notes, net of income tax benefit | 397                            |         |
| Numerator for diluted earnings per share   | \$45,977                       | \$4,432 |
| Denominator:   |                                |         |
| Basic weighted-average shares  | 176,474                        | 169,064 |
| Common stock equivalents (a)   | 2,556                          | 2,839   |
| Shares attributable to 0.5% Exchangeable Senior Notes  | 5,858                          |         |
| Diluted weighted-average shares  | 184,888                        | 171,903 |
| Other information:   |                                |         |
| Weighted-average number of anti-dilutive options and restricted stock units (b)                    | 1,602                          | 980     |
| Shares issued under stock incentive and employee stock purchase plans                              | 1,013                          | 523     |

Common stock equivalents represent the dilutive effect of outstanding in-the-money stock options using the (a) treasury stock method, Stock Price-Based RSUs whose Target Price criteria have been met but are unpaid and shares expected to be issued under Performance-Based Restricted Stock Units.

(b) Based upon the average closing price of the Company's common stock on the NYSE for the period.

### 13. Fair Value Disclosures

#### Fair Value Disclosures

The Company uses ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820"), to measure the fair value of certain assets and liabilities. ASC 820 provides a framework for measuring fair value in accordance with GAAP, establishes a fair value hierarchy which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value, and requires certain disclosures about fair value measurements. The fair value hierarchy is summarized below:

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

Level 2: Fair value determined using significant observable inputs, generally either quoted prices in active markets for similar assets or liabilities or quoted prices in markets that are not active.

Level 3: Fair value determined using significant unobservable inputs, such as pricing models, discounted cash flows, or similar techniques.

#### Financial Instruments

The table below provides, as of the date indicated, a summary of assets (liabilities) related to the Company's financial instruments, measured at fair value on a recurring basis (amounts in thousands):

| Financial Instrument  | Fair value hierarchy | Fair value January 31, 2014 | October 31, 2013 |
|---|----------------------|-----------------------------|------------------|
| Corporate Securities  | Level 2              | \$13,017                    | \$52,508         |
| Residential Mortgage Loans Held for Sale                          | Level 2              | \$58,131                    | \$113,517        |
| Forward Loan Commitments—Residential Mortgage Loans Held for Sale | Level 2              | \$(191)                     | \$(496)          |
| Interest Rate Lock Commitments ("IRLCs")                          | Level 2              | \$(121)                     | \$(181)          |
| Forward Loan Commitments—IRLCs                                    | Level 2              | \$121                       | \$181            |

At January 31, 2014 and October 31, 2013, the carrying value of cash and cash equivalents and restricted cash approximated fair value.

#### Mortgage Loans Held for Sale

The table below provides, as of the date indicated, the aggregate unpaid principal and fair value of mortgage loans held for sale (amounts in thousands):

|                     | Aggregate unpaid principal balance | Fair value | Excess  |
|---------------------|------------------------------------|------------|---------|
| At January 31, 2014 | \$57,421                           | \$58,131   | \$710   |
| At October 31, 2013 | \$111,896                          | \$113,517  | \$1,621 |

At the end of the reporting period, the Company determines the fair value of its mortgage loans held for sale and the forward loan commitments it has entered into as a hedge against the interest rate risk of its mortgage loans using the market approach to determine fair value. The evaluation is based on the current market pricing of mortgage loans with similar terms and values as of the reporting date and by applying such pricing to the mortgage loan portfolio. The Company recognizes the difference between the fair value and the unpaid principal balance of mortgage loans held for sale as a gain or loss. In addition, the Company recognizes the fair value of its forward loan commitments as a gain or loss. These gains and losses are included in "Other income - net". Interest income on mortgage loans held for sale is calculated based upon the stated interest rate of each loan and is included in "Other income - net".

IRLCs represent individual borrower agreements that commit the Company to lend at a specified price for a specified period as long as there is no violation of any condition established in the commitment contract. These commitments have varying degrees of interest rate risk. The Company utilizes best-efforts forward loan commitments ("Forward Commitments") to hedge the interest rate risk of the IRLCs and residential mortgage loans held for sale. Forward Commitments represent contracts with third-party investors for the future delivery of loans whereby the Company agrees to make delivery at a specified future date at a specified price. The IRLCs and Forward Commitments are considered derivative financial instruments under ASC 815, "Derivatives and Hedging," which requires derivative financial instruments to be recorded at fair value. The Company estimates the fair value of such commitments based on the estimated fair value of the underlying mortgage loan and, in the case of IRLCs, the probability that the mortgage loan will fund within the terms of the IRLC. The fair values of IRLCs and forward loan commitments are included in either "Receivables, prepaid expenses and other assets" or "Accrued expenses", as appropriate. To manage the risk of non-performance of investors regarding the Forward Commitments, the Company assesses the credit worthiness of the investors on a periodic basis.

#### Marketable Securities

The table below provides, as of the date indicated, the amortized cost, gross unrealized holding gains, gross unrealized holding losses and fair value of marketable securities (amounts in thousands):

|                                 | January 31,<br>2014 | October 31,<br>2013 |
|---------------------------------|---------------------|---------------------|
| Amortized cost                  | \$13,061            | \$52,502            |
| Gross unrealized holding gains  | 3                   | 71                  |
| Gross unrealized holding losses | (47                 | ) (65               |
| Fair value                      | \$13,017            | \$52,508            |

The estimated fair values of corporate securities are based on quoted prices provided by brokers. The remaining contractual maturities of marketable securities as of January 31, 2014 ranged from 3 months to 22 months.

#### Inventory

The Company recognizes inventory impairment charges based on the difference in the carrying value of the inventory and its fair value at the time of the evaluation. The fair value of the aforementioned inventory was determined using Level 3 criteria. Estimated fair value is primarily determined by discounting the estimated future cash flow of each community. See Note 1, "Significant Accounting Policies, Inventory" in the audited financial statements contained in the Company's Annual Report on Form 10-K for the year ended October 31, 2013 for additional information regarding the Company's methodology on determining fair value. As further discussed in Note 1 in the Company's Annual Report on Form 10-K, determining the fair value of a community's inventory involves a number of variables, many of which are interrelated. If the Company used a different input for any of the various unobservable inputs used in its impairment analysis, the results of the analysis may have been different, absent any other changes. The table below summarizes, for the periods indicated, the ranges of certain quantitative unobservable inputs utilized in determining the fair value of impaired communities:

|                                     | Selling price per<br>unit (in<br>thousands) | Sales price per<br>year<br>(in units) | Discount rate |
|-------------------------------------|---|---------------------------------------|---------------|
| Three months ended January 31, 2014 | \$388 - \$405                               | 21 - 23                               | 16.6%         |
| Three months ended October 31, 2013 | \$315 - \$362                               | 2 - 7                                 | 15.0%         |
| Three months ended July 31, 2013    | \$475 - \$500                               | 2                                     | 15.0%         |
| Three months ended April 30, 2013   | —   | —                                     | —%            |
| Three months ended January 31, 2013 | \$303 - \$307                               | 15                                    | 15.3%         |

The table below provides, for the periods indicated, the fair value of operating communities whose carrying value was adjusted and the amount of impairment charges recognized (\$ amounts in thousands):

| Three months ended: | Number of communities tested | Impaired operating communities |  |                    |
|---------------------|------------------------------|--------------------------------|--|--------------------|
|                     |                              | Number of communities          | Fair value of communities, net of impairment charges | Impairment charges |
| Fiscal 2014:        |                              |                                |  |                    |
| January 31          | 67                           | 1                              | \$7,131  | \$1,300            |
|                     |                              |                                |  | \$1,300            |
| Fiscal 2013:        |                              |                                |  |                    |
| January 31          | 60                           | 2                              | \$5,377  | \$700              |
| April 30            | 79                           | 1                              | \$749  | 340                |
| July 31             | 76                           | 1                              | \$191  | 100                |
| October 31          | 63                           | 2                              | \$6,798  | 2,200              |
|                     |                              |                                |  | \$3,340            |

#### Investments in Distressed Loans and REO

Gibraltar's investments in distressed loans were recorded at estimated fair value at inception based on the acquisition price as determined by Level 3 inputs and was based on the estimated future cash flows to be generated by the loans discounted at the rates used to value the loans at the acquisition dates. The table below provides, as of the date indicated, the carrying amount and estimated fair value of distressed loans (amounts in thousands):

|                      | January 31, 2014 | October 31, 2013 |
|----------------------|------------------|------------------|
| Carrying amount      | \$19,253         | \$36,374         |
| Estimated fair value | \$23,240         | \$45,355         |

Gibraltar's REO was recorded at estimated fair value at the time it was acquired through foreclosure or deed in lieu actions using Level 3 inputs. The valuation techniques used to estimate fair value are third-party appraisals, broker opinions of value, or internal valuation methodologies (which may include discounted cash flows, capitalization rate analysis or comparable transactional analysis). Unobservable inputs used in estimating the fair value of REO assets are based upon the best information available under the circumstances and take into consideration the financial condition and operating results of the asset, local market conditions, the availability of capital, interest and inflation rates and other factors deemed appropriate by management.

#### Debt

The table below provides, as of the date indicated, the book value and estimated fair value of the Company's debt (amounts in thousands):

|                                     | Fair value hierarchy | January 31, 2014 |                      | October 31, 2013 |                      |
|-------------------------------------|----------------------|------------------|----------------------|------------------|----------------------|
|                                     |                      | Book value       | Estimated fair value | Book value       | Estimated fair value |
| Loans payable (a)                   | Level 2              | \$158,606        | \$158,097            | \$107,222        | \$106,988            |
| Senior notes (b)                    | Level 1              | 2,925,336        | 3,084,026            | 2,325,336        | 2,458,737            |
| Mortgage company warehouse loan (c) | Level 2              | 51,470           | 51,470               | 75,000           | 75,000               |
|                                     |                      | \$3,135,412      | \$3,293,593          | \$2,507,558      | \$2,640,725          |

(a) The estimated fair value of loans payable was based upon interest rates that the Company believed were available to it for loans with similar terms and remaining maturities as of the applicable valuation date.

(b) The estimated fair value of the Company's senior notes is based upon their indicated market prices.

(c) The Company believes that the carrying value of its mortgage company warehouse loan borrowings approximates their fair value.



## 14. Other Income - Net

The table below provides, for the periods indicated, the components of other income - net (amounts in thousands):

|                                  | Three months ended January 31, |         |
|----------------------------------|--------------------------------|---------|
|                                  | 2014                           | 2013    |
| Interest income                  | \$1,064                        | \$1,475 |
| Income from ancillary businesses | 1,613                          | 1,278   |
| Gibraltar                        | 4,332                          | 151     |
| Management fee income            | 1,227                          | 327     |
| Retained customer deposits       | 888                            | 678     |
| Land sales, net                  | 6,258                          | 145     |
| Other                            | 1,159                          | 572     |
| Total other income - net         | \$16,541                       | \$4,626 |

Included in "Land sales, net" is \$2.9 million of previously deferred gains on the Company's initial sales of the properties to Trust II as further described in Note 3 - "Investments in and Advances to Unconsolidated Entities." Income from ancillary businesses includes the activity of the Company's non-core businesses which include its mortgage, title, landscaping, security monitoring, and golf course and country club operations. The table below provides, for the periods indicated, revenues and expenses for the Company's non-core ancillary businesses (amounts in thousands):

|         | Three months ended January 31, |          |
|---------|--------------------------------|----------|
|         | 2014                           | 2013     |
| Revenue | \$20,940                       | \$16,641 |
| Expense | \$19,327                       | \$15,363 |

## 15. Commitments and Contingencies

## Legal Proceedings

The Company is involved in various claims and litigation arising principally in the ordinary course of business. The Company believes that adequate provision for resolution of all current claims and pending litigation has been made for probable losses and the disposition of these matters will not have a material adverse effect on the Company's results of operations and liquidity or on its financial condition.

## Investments in and Advances to Unconsolidated Entities

At January 31, 2014, the Company had investments in and advances to a number of unconsolidated entities, was committed to invest or advance additional funds, and had guaranteed a portion of the indebtedness and/or loan commitments of these entities. See Note 3, "Investments in and Advances to Unconsolidated Entities," for more information regarding the Company's commitments to these entities.

## Land Purchase Commitments

Generally, the Company's option and purchase agreements to acquire land parcels do not require the Company to purchase those land parcels, although the Company may, in some cases, forfeit any deposit balance outstanding if and when it terminates an option and purchase agreement. If market conditions are weak, approvals needed to develop the land are uncertain or other factors exist that make the purchase undesirable, the Company may not acquire the land. Whether an option and purchase agreement is legally terminated or not, the Company reviews the amount recorded for the land parcel subject to the option and purchase agreement to determine if the amount is recoverable. While the Company may not formally terminate the option and purchase agreements for those land parcels that it does not expect to acquire, it writes off any non-refundable deposits and costs previously capitalized to such land parcels in the periods that it determines such costs are not recoverable.



Information regarding the Company's land purchase commitments, excluding the Shapell acquisition, as of the date indicated, is provided in the table below (amounts in thousands):

|  | January 31,<br>2014 | October 31,<br>2013 |
|--|---------------------|---------------------|
| Aggregate purchase commitments:  |                     |                     |
| Unrelated parties  | \$1,155,798         | \$1,301,987         |
| Unconsolidated entities that the Company has investments in            | 12,552              | 61,738              |
| Total  | \$1,168,350         | \$1,363,725         |
| Deposits against aggregate purchase commitments                        | \$76,814            | \$76,986            |
| Additional cash required to acquire land                               | 1,091,536           | 1,286,739           |
| Total  | \$1,168,350         | \$1,363,725         |
| Amount of additional cash required to acquire land in accrued expenses | \$1,753             | \$1,439             |

In addition, the Company expects to purchase approximately 3,800 additional home sites from several joint ventures in which it has interests. The purchase prices of these home sites will be determined at a future date.

At January 31, 2014, the Company had purchase commitments to acquire land for apartment developments of approximately \$56.0 million, of which it had outstanding deposits in the amount of \$2.5 million.

The Company has additional land parcels under option that have been excluded from the aforementioned aggregate purchase amounts since it does not believe that it will complete the purchase of these land parcels and no additional funds will be required from the Company to terminate these contracts.

#### Surety Bonds and Letters of Credit

At January 31, 2014, the Company had outstanding surety bonds amounting to \$427.1 million, primarily related to its obligations to governmental entities to construct improvements in the Company's communities. The Company estimates that \$281.4 million of work remains on these improvements. The Company has an additional \$70.8 million of surety bonds outstanding that guarantee other obligations of the Company. The Company believes it is not probable that any outstanding bonds will be drawn upon.

At January 31, 2014, the Company had outstanding letters of credit of \$83.6 million, including \$71.1 million under its Credit Facility and \$12.5 million collateralized by restricted cash. These letters of credit were issued to secure various financial obligations of the Company including insurance policy deductibles and other claims, land deposits and security to complete improvements in communities which it is operating. The Company believes it is not probable that any outstanding letters of credit will be drawn upon.

#### Acquisition of Shapell Industries, Inc.

On February 4, 2014, the Company completed its previously announced acquisition of Shapell. See Note 1 - "Significant Accounting Policies - Subsequent Events" for more information regarding this acquisition.

#### Backlog

At January 31, 2014, the Company had agreements of sale outstanding to deliver 3,667 homes with an aggregate sales value of \$2.69 billion.

#### Mortgage Commitments

The Company's mortgage subsidiary provides mortgage financing for a portion of the Company's home closings. For those home buyers to whom the Company's mortgage subsidiary provides mortgages, it determines whether the home buyer qualifies for the mortgage based upon information provided by the home buyer and other sources. For those home buyers that qualify, the Company's mortgage subsidiary provides the home buyer with a mortgage commitment that specifies the terms and conditions of a proposed mortgage loan based upon then-current market conditions. Prior to the actual closing of the home and funding of the mortgage, the home buyer will lock in an interest rate based upon the terms of the commitment. At the time of rate lock, the Company's mortgage subsidiary agrees to sell the proposed mortgage loan to one of several outside recognized mortgage financing institutions ("investors") that is willing to honor the terms and conditions, including interest rate, committed to the home buyer. The Company believes that these investors have adequate financial resources to honor their commitments to its mortgage subsidiary.



Information regarding the Company's mortgage commitments, as of the date indicated, is provided in the table below (amounts in thousands):

|                                      | January 31,<br>2014 | October 31,<br>2013 |
|--------------------------------------|---------------------|---------------------|
| Aggregate mortgage loan commitments: |                     |                     |
| IRLCs                                | \$254,179           | \$247,995           |
| Non-IRLCs                            | 659,968             | 645,288             |
| Total                                | \$914,147           | \$893,283           |
| Investor commitments to purchase:    |                     |                     |
| IRLCs                                | \$254,179           | \$247,995           |
| Mortgage loans receivable            | 53,623              | 107,873             |
| Total                                | \$307,802           | \$355,868           |

#### 16. Information on Operating Segments

At October 31, 2013, the Company determined that it operates in two segments: Traditional Home Building and Urban Infill ("City Living"). Amounts reported in the prior period have been reclassified to conform to the current period.

The Company has determined that its Traditional Home Building operations operate in four geographic segments: North, Mid-Atlantic, South and West. The states comprising each geographic segment are as follows:

North: Connecticut, Illinois, Massachusetts, Michigan, Minnesota, New Jersey and New York

Mid-Atlantic: Delaware, Maryland, Pennsylvania and Virginia

South: Florida, North Carolina, South Carolina and Texas

West: Arizona, California, Colorado, Nevada and Washington

Revenue and income (loss) before income taxes for each of the Company's reportable segments, for the periods indicated, were as follows (amounts in thousands):

|                                    | Three months ended January 31, |            |
|------------------------------------|--------------------------------|------------|
|                                    | 2014                           | 2013       |
| Revenues:                          |                                |            |
| Traditional Home Building:         |                                |            |
| North                              | \$127,644                      | \$82,319   |
| Mid-Atlantic                       | 169,096                        | 129,591    |
| South                              | 150,559                        | 87,185     |
| West                               | 186,226                        | 112,595    |
| Traditional Home Building          | 633,525                        | 411,690    |
| City Living                        | 10,156                         | 12,911     |
| Total                              | \$643,681                      | \$424,601  |
| Income (loss) before income taxes: |                                |            |
| Traditional Home Building:         |                                |            |
| North                              | \$8,346                        | \$4,720    |
| Mid-Atlantic                       | 21,551                         | 14,850     |
| South                              | 17,368                         | 2,814      |
| West                               | 34,668                         | 8,047      |
| Traditional Home Building          | 81,933                         | 30,431     |
| City Living                        | (1,058)                        | ) 2,697    |
| Corporate and other                | (9,640)                        | ) (24,802) |
| Total                              | \$71,235                       | \$8,326    |

"Corporate and other" is comprised principally of general corporate expenses such as the offices of the Executive Officers of the Company and the corporate finance, accounting, audit, tax, human resources, risk management, marketing and legal groups; interest income and income from certain of the Company's ancillary businesses, including Gibraltar; and income from a number of the Company's unconsolidated entities.

Total assets for each of the Company's geographic segments, as of the date indicated, are shown in the table below (amounts in thousands).

|                            | January 31,<br>2014 | October 31,<br>2013 |
|----------------------------|---------------------|---------------------|
| Traditional Home Building: |                     |                     |
| North                      | \$1,000,985         | \$963,597           |
| Mid-Atlantic               | 1,254,409           | 1,231,438           |
| South                      | 1,126,470           | 953,955             |
| West                       | 1,547,449           | 1,290,388           |
| Traditional Home Building  | 4,929,313           | 4,439,378           |
| City Living                | 781,698             | 674,302             |
| Corporate and other        | 2,049,244           | 1,713,779           |
| Total                      | \$7,760,255         | \$6,827,459         |

"Corporate and other" is comprised principally of cash and cash equivalents, marketable securities, restricted cash, deferred tax assets and the assets of the Company's Gibraltar investments, manufacturing facilities and mortgage subsidiary.

The Company provided for inventory impairment charges and the expensing of costs that it believed not to be recoverable and recoveries of prior charges for the periods indicated, as shown in the table below; the net carrying value of inventory and investments in and advances to unconsolidated entities for each of the Company's geographic segments, as of the dates indicated, are also shown in the table below (amounts in thousands):

|   | Net Carrying Value        |                           | Impairments   |        |
|---|---------------------------|---------------------------|---|--------|
|   | At January<br>31,<br>2014 | At October<br>31,<br>2013 | Three months ended January<br>31,<br>2014                      2013 |        |
| Inventory:  |                           |                           |   |        |
| Land controlled for future communities:                 |                           |                           |   |        |
| Traditional Home Building:                              |                           |                           |   |        |
| North   | \$ 14,937                 | \$ 16,267                 | \$ 180  | \$ 88  |
| Mid-Atlantic  | 28,172                    | 29,423                    | 246   | 16     |
| South   | 15,163                    | 14,606                    | 249   | 355    |
| West  | 169,919                   | 13,371                    | 7   | (450 ) |
| Traditional Home Building                               | 228,191                   | 73,667                    | 682   | 9      |
| City Living   | 26,358                    | 26,135                    |   |        |
|   | 254,549                   | 99,802                    | 682   | 9      |
| Land owned for future communities:                      |                           |                           |   |        |
| Traditional Home Building:                              |                           |                           |   |        |
| North   | 177,321                   | 135,282                   |   |        |
| Mid-Atlantic  | 285,761                   | 308,585                   |   |        |
| South   | 254,989                   | 158,457                   |   |        |
| West  | 460,963                   | 448,125                   |   |        |
| Traditional Home Building                               | 1,179,034                 | 1,050,449                 | —   | —      |
| City Living   | 312,171                   | 237,181                   |   |        |
|   | 1,491,205                 | 1,287,630                 | —   | —      |
| Operating communities:                                  |                           |                           |   |        |
| Traditional Home Building:                              |                           |                           |   |        |
| North   | 788,391                   | 785,175                   | 1,300   | 500    |
| Mid-Atlantic  | 911,138                   | 866,256                   |   |        |
| South   | 729,757                   | 690,302                   |   |        |
| West  | 819,421                   | 697,573                   |   | 200    |
| Traditional Home Building                               | 3,248,707                 | 3,039,306                 | 1,300   | 700    |
| City Living   | 241,186                   | 223,674                   |   |        |
|   | 3,489,893                 | 3,262,980                 | 1,300   | 700    |
| Total   | \$5,235,647               | \$4,650,412               | \$ 1,982  | \$ 709 |
| Investments in and advances to unconsolidated entities: |                           |                           |   |        |
| Traditional Home Building:                              |                           |                           |   |        |
| Mid-Atlantic  | \$ 11,850                 | \$ 11,850                 |   |        |
| South   | 91,097                    | 50,452                    |   |        |
| West  | 84,502                    | 110,467                   |   |        |
| Traditional Home Building                               | 187,449                   | 172,769                   | —   | —      |
| City Living   | 145,748                   | 135,950                   |   |        |
| Corporate and other                                     | 97,418                    | 94,414                    |   |        |
| Total   | \$430,615                 | \$403,133                 | \$—   | \$—    |



# 17. Supplemental Disclosure to Condensed Statements of Cash Flows

The following are supplemental disclosures to the Condensed Consolidated Statements of Cash Flows for the three months ended January 31, 2014 and 2013 (amounts in thousands):

|  | 2014     | 2013     |
|--|----------|----------|
| Cash flow information:   |          |          |
| Interest capitalized, net of amount paid   | \$17,359 | \$6,801  |
| Income tax payment   | \$4,961  |          |
| Income tax refunds   |          | \$469    |
| Non-cash activity:   |          |          |
| Cost of inventory acquired through seller financing or municipal bonds, net                                    | \$60,661 | \$15,998 |
| Reduction in inventory for Company's share of earnings in land purchased from unconsolidated entities          | \$2,342  |          |
| Miscellaneous decreases in inventory   |          | \$(144 ) |
| Defined benefit plan amendment   | \$77     | \$519    |
| Increase in accrued expenses related to Stock Price-Based RSUs paid  | \$4,968  | \$2,939  |
| Increase in investments in unconsolidated entities due to increase in letters of credit or accrued liabilities |          | \$(24 )  |
| Transfer of inventory to investment in unconsolidated entities   | \$700    |          |
| Unrealized gain on derivative held by equity investee  | \$393    | \$151    |
| Increase in investments in unconsolidated entities for change in the fair value of debt guarantees             | \$430    |          |
| Miscellaneous (decreases) increases to investments in unconsolidated entities                                  | \$(450 ) | \$86     |

# 18. Supplemental Guarantor Information

A 100% owned subsidiary of the Company, Toll Brothers Finance Corp. (the "Subsidiary Issuer"), has issued the following Senior Notes (amounts in thousands):

|   | Original Amount Issued | Amount outstanding at January 31, 2014 |
|---|------------------------|--|
| 4.95% Senior Notes due 2014             | \$300,000              | \$267,960                              |
| 5.15% Senior Notes due 2015             | \$300,000              | \$300,000                              |
| 8.91% Senior Notes due 2017             | \$400,000              | \$400,000                              |
| 6.75% Senior Notes due 2019             | \$250,000              | \$250,000                              |
| 5.875% Senior Notes due 2022            | \$419,876              | \$419,876                              |
| 4.375% Senior Notes due 2023            | \$400,000              | \$400,000                              |
| 0.5% Exchangeable Senior Notes due 2032 | \$287,500              | \$287,500                              |
| 4.0% Senior Notes due 2018              | \$350,000              | \$350,000                              |
| 5.625% Senior Notes due 2024            | \$250,000              | \$250,000                              |

The obligations of the Subsidiary Issuer to pay principal, premiums, if any, and interest are guaranteed jointly and severally on a senior basis by the Company and substantially all of the Company's 100% owned home building subsidiaries (the "Guarantor Subsidiaries"). The guarantees are full and unconditional. The Company's non-home building subsidiaries and several of its home building subsidiaries (together, the "Non-Guarantor Subsidiaries") do not guarantee the debt. The Subsidiary Issuer generates no operating revenues and does not have any independent operations other than the financing of other subsidiaries of the Company by lending the proceeds from the above described debt issuances.

Separate financial statements and other disclosures concerning the Guarantor Subsidiaries are not presented because management has determined that such disclosures would not be material to investors.





Supplemental consolidating financial information of Toll Brothers, Inc., the Subsidiary Issuer, the Guarantor Subsidiaries, the Non-Guarantor Subsidiaries and the eliminations to arrive at Toll Brothers, Inc. on a consolidated basis is presented below (\$ amounts in thousands).

Condensed Consolidating Balance Sheet at January 31, 2014:

|  | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|--|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| <b>ASSETS</b>  |                           |                      |                           |                                   |              |              |
| Cash and cash equivalents                              | —                         | —                    | 1,070,746                 | 119,743                           | —            | 1,190,489    |
| Marketable securities                                  |                           |                      | 2,990                     | 10,027                            |              | 13,017       |
| Restricted cash  | 15,196                    |                      | 15,744                    | 1,235                             |              | 32,175       |
| Inventory  |                           |                      | 5,137,927                 | 97,720                            |              | 5,235,647    |
| Property, construction and office equipment, net       |                           |                      | 116,490                   | 14,700                            |              | 131,190      |
| Receivables, prepaid expenses and other assets         | 18                        | 19,460               | 114,645                   | 122,200                           | (16,289 )    | 240,034      |
| Mortgage loans held for sale                           |                           |                      |                           | 58,131                            |              | 58,131       |
| Customer deposits held in escrow                       |                           |                      | 45,834                    |                                   |              | 45,834       |
| Investments in and advances to unconsolidated entities |                           |                      | 152,929                   | 277,686                           |              | 430,615      |
| Investments in distressed loans                        |                           |                      |                           | 19,253                            |              | 19,253       |
| Investments in foreclosed real estate                  |                           |                      |                           | 79,267                            |              | 79,267       |
| Investments in and advances to consolidated entities   | 3,421,229                 | 2,953,186            | 4,740                     |                                   | (6,379,155 ) | —            |
| Deferred tax assets, net of valuation allowances       | 284,603                   |                      |                           |                                   |              | 284,603      |
|  | 3,721,046                 | 2,972,646            | 6,662,045                 | 799,962                           | (6,395,444 ) | 7,760,255    |
| <b>LIABILITIES AND EQUITY</b>                          |                           |                      |                           |                                   |              |              |
| <b>Liabilities:</b>                                    |                           |                      |                           |                                   |              |              |
| Loans payable  |                           |                      | 158,606                   |                                   |              | 158,606      |
| Senior notes   |                           | 2,885,496            |                           |                                   | 36,355       | 2,921,851    |
| Mortgage company warehouse loan                        |                           |                      |                           | 51,470                            |              | 51,470       |
| Customer deposits                                      |                           |                      | 218,747                   |                                   |              | 218,747      |
| Accounts payable                                       |                           |                      | 166,266                   | 20                                |              | 166,286      |
| Accrued expenses                                       | 37                        | 46,176               | 333,601                   | 152,942                           | (16,659 )    | 516,097      |
| Advances from consolidated entities                    |                           |                      | 2,414,287                 | 576,405                           | (2,990,692 ) | —            |
| Income taxes payable                                   | 99,825                    |                      |                           |                                   |              | 99,825       |
| Total liabilities                                      | 99,862                    | 2,931,672            | 3,291,507                 | 780,837                           | (2,970,996 ) | 4,132,882    |
| <b>Equity:</b>   |                           |                      |                           |                                   |              |              |
| <b>Stockholders' equity:</b>                           |                           |                      |                           |                                   |              |              |
| Common stock   | 1,776                     |                      | 48                        | 3,006                             | (3,054 )     | 1,776        |
| Additional paid-in capital                             | 683,965                   | 49,400               |                           | 1,734                             | (51,134 )    | 683,965      |
| Retained earnings (deficits)                           | 2,937,583                 | (8,426 )             | 3,370,542                 | 8,144                             | (3,370,260 ) | 2,937,583    |
| Treasury stock, at cost                                | (81 )                     |                      |                           |                                   |              | (81 )        |
| Accumulated other comprehensive loss                   | (2,059 )                  |                      | (52 )                     | (13 )                             |              | (2,124 )     |
| Total stockholders' equity                             | 3,621,184                 | 40,974               | 3,370,538                 | 12,871                            | (3,424,448 ) | 3,621,119    |
| Noncontrolling interest                                |                           |                      |                           | 6,254                             |              | 6,254        |

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|              |           |           |           |         |              |           |
|--------------|-----------|-----------|-----------|---------|--------------|-----------|
| Total equity | 3,621,184 | 40,974    | 3,370,538 | 19,125  | (3,424,448 ) | 3,627,373 |
|              | 3,721,046 | 2,972,646 | 6,662,045 | 799,962 | (6,395,444 ) | 7,760,255 |

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## Condensed Consolidating Balance Sheet at October 31, 2013:

|   | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|---|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| <b>ASSETS</b>   |                           |                      |                           |                                   |              |              |
| Cash and cash equivalents                                 | —                         | —                    | 670,102                   | 102,870                           | —            | 772,972      |
| Marketable securities                                     |                           |                      | 42,491                    | 10,017                            |              | 52,508       |
| Restricted cash   | 15,182                    |                      | 16,007                    | 847                               |              | 32,036       |
| Inventory   |                           |                      | 4,625,252                 | 25,160                            |              | 4,650,412    |
| Property, construction and office<br>equipment, net       |                           |                      | 116,809                   | 14,511                            |              | 131,320      |
| Receivables, prepaid expenses and<br>other assets         | 33                        | 15,675               | 101,321                   | 131,701                           | (19,435 )    | 229,295      |
| Mortgage loans held for sale                              |                           |                      |                           | 113,517                           |              | 113,517      |
| Customer deposits held in escrow                          |                           |                      | 46,888                    |                                   |              | 46,888       |
| Investments in and advances to<br>unconsolidated entities |                           |                      | 175,159                   | 227,974                           |              | 403,133      |
| Investments in distressed loans                           |                           |                      |                           | 36,374                            |              | 36,374       |
| Investments in foreclosed real estate                     |                           |                      |                           | 72,972                            |              | 72,972       |
| Investments in and advances to<br>consolidated entities   | 3,113,203                 | 2,334,503            | 4,740                     |                                   | (5,452,446 ) | —            |
| Deferred tax assets, net of valuation<br>allowances       | 286,032                   |                      |                           |                                   |              | 286,032      |
|   | 3,414,450                 | 2,350,178            | 5,798,769                 | 735,943                           | (5,471,881 ) | 6,827,459    |
| <b>LIABILITIES AND EQUITY</b>                             |                           |                      |                           |                                   |              |              |
| <b>Liabilities:</b>                                       |                           |                      |                           |                                   |              |              |
| Loans payable   |                           |                      | 107,222                   |                                   |              | 107,222      |
| Senior notes  |                           | 2,282,719            |                           |                                   | 38,723       | 2,321,442    |
| Mortgage company warehouse loan                           |                           |                      |                           | 75,000                            |              | 75,000       |
| Customer deposits   |                           |                      | 212,669                   |                                   |              | 212,669      |
| Accounts payable  |                           |                      | 167,733                   | 54                                |              | 167,787      |
| Accrued expenses  |                           | 25,045               | 355,590                   | 161,402                           | (19,050 )    | 522,987      |
| Advances from consolidated entities                       |                           |                      | 1,627,130                 | 467,929                           | (2,095,059 ) | —            |
| Income taxes payable                                      | 81,188                    |                      |                           |                                   |              | 81,188       |
| Total liabilities   | 81,188                    | 2,307,764            | 2,470,344                 | 704,385                           | (2,075,386 ) | 3,488,295    |
| <b>Equity:</b>  |                           |                      |                           |                                   |              |              |
| <b>Stockholders' equity:</b>                              |                           |                      |                           |                                   |              |              |
| Common stock  | 1,694                     |                      | 48                        | 3,006                             | (3,054 )     | 1,694        |
| Additional paid-in capital                                | 441,677                   | 49,400               |                           | 1,734                             | (51,134 )    | 441,677      |
| Retained earnings (deficits)                              | 2,892,003                 | (6,986 )             | 3,328,629                 | 20,664                            | (3,342,307 ) | 2,892,003    |
| Treasury stock, at cost                                   |                           |                      |                           |                                   |              | —            |
| Accumulated other comprehensive<br>loss                   | (2,112 )                  |                      | (252 )                    | (23 )                             |              | (2,387 )     |
| Total stockholders' equity                                | 3,333,262                 | 42,414               | 3,328,425                 | 25,381                            | (3,396,495 ) | 3,332,987    |
| Noncontrolling interest                                   |                           |                      |                           | 6,177                             |              | 6,177        |
| Total equity  | 3,333,262                 | 42,414               | 3,328,425                 | 31,558                            | (3,396,495 ) | 3,339,164    |
|   | 3,414,450                 | 2,350,178            | 5,798,769                 | 735,943                           | (5,471,881 ) | 6,827,459    |



Condensed Consolidating Statement of Operations and Comprehensive Income (Loss) for the three months ended January 31, 2014:

|  | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|--|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| Revenues                                   |                           |                      | 650,772                   | 15,602                            | (22,693 )    | 643,681      |
| Cost of revenues                           |                           |                      | 515,637                   | 2,602                             | (4,207 )     | 514,032      |
| Selling, general and administrative        | 55                        | 937                  | 102,700                   | 13,637                            | (19,459 )    | 97,870       |
|  | 55                        | 937                  | 618,337                   | 16,239                            | (23,666 )    | 611,902      |
| Income (loss) from operations              | (55 )                     | (937 )               | 32,435                    | (637 )                            | 973          | 31,779       |
| Other:                                     |                           |                      |                           |                                   |              |              |
| Income (loss) from unconsolidated entities |                           |                      | 24,207                    | (1,292 )                          |              | 22,915       |
| Other income - net                         | 2,365                     |                      | 10,572                    | 6,200                             | (2,596 )     | 16,541       |
| Intercompany interest income               |                           | 38,144               |                           |                                   | (38,144 )    | —            |
| Interest expense                           |                           | (39,574 )            |                           | (193 )                            | 39,767       | —            |
| Income from subsidiaries                   | 68,925                    |                      | 1,711                     |                                   | (70,636 )    | —            |
| Income (loss) before income taxes          | 71,235                    | (2,367 )             | 68,925                    | 4,078                             | (70,636 )    | 71,235       |
| Income tax provision (benefit)             | 25,655                    | (928 )               | 27,012                    | 1,598                             | (27,682 )    | 25,655       |
| Net income (loss)                          | 45,580                    | (1,439 )             | 41,913                    | 2,480                             | (42,954 )    | 45,580       |
| Other comprehensive income                 | 53                        |                      | 200                       | 10                                |              | 263          |
| Total comprehensive income (loss)          | 45,633                    | (1,439 )             | 42,113                    | 2,490                             | (42,954 )    | 45,843       |

Condensed Consolidating Statement of Operations and Comprehensive Income (Loss) for the three months ended January 31, 2013:

|                                     | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|-------------------------------------|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| Revenues                            |                           |                      | 430,222                   | 15,046                            | (20,667 )    | 424,601      |
| Cost of revenues                    |                           |                      | 348,703                   | 4,992                             | (7,758 )     | 345,937      |
| Selling, general and administrative | 16                        | 687                  | 84,508                    | 10,140                            | (17,304 )    | 78,047       |
|                                     | 16                        | 687                  | 433,211                   | 15,132                            | (25,062 )    | 423,984      |
| Income (loss) from operations       | (16 )                     | (687 )               | (2,989 )                  | (86 )                             | 4,395        | 617          |
| Other:                              |                           |                      |                           |                                   |              |              |
| Income from unconsolidated entities |                           |                      | 1,096                     | 1,987                             |              | 3,083        |
| Other income - net                  | 2,386                     |                      | 6,027                     | 2,494                             | (6,281 )     | 4,626        |
| Intercompany interest income        |                           | 29,727               |                           |                                   | (29,727 )    | —            |
| Interest expense                    |                           | (31,422 )            |                           | (191 )                            | 31,613       | —            |
| Income from subsidiaries            | 5,956                     |                      | 1,822                     |                                   | (7,778 )     | —            |
| Income (loss) before income taxes   | 8,326                     | (2,382 )             | 5,956                     | 4,204                             | (7,778 )     | 8,326        |
| Income tax provision (benefit)      | 3,894                     | (933 )               | 2,333                     | 1,647                             | (3,047 )     | 3,894        |
| Net income (loss)                   | 4,432                     | (1,449 )             | 3,623                     | 2,557                             | (4,731 )     | 4,432        |
| Other comprehensive income (loss)   | (173 )                    |                      | 225                       | (36 )                             |              | 16           |
| Total comprehensive income (loss)   | 4,259                     | (1,449 )             | 3,848                     | 2,521                             | (4,731 )     | 4,448        |

## Condensed Consolidating Statement of Cash Flows for the three months ended January 31, 2014:

|  | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|--|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| Net cash (used in) provided by operating activities                  | 31,235                    | 23,383               | (279,194 )                | (17,808 )                         | (8,004 )     | (250,388 )   |
| Cash flow used in investing activities:                              |                           |                      |                           |                                   |              |              |
| Purchase of property and equipment - net                             |                           |                      | (2,659 )                  | (194 )                            |              | (2,853 )     |
| Sale and redemption of marketable securities                         |                           |                      | 39,243                    |                                   |              | 39,243       |
| Investments in and advances to unconsolidated entities               |                           |                      | (4,879 )                  | (55,529 )                         |              | (60,408 )    |
| Return of investments in unconsolidated entities                     |                           |                      | 29,429                    | 3,000                             |              | 32,429       |
| Investments in distressed loans and foreclosed real estate           |                           |                      |                           | (191 )                            |              | (191 )       |
| Return of investments in distressed loans and foreclosed real estate |                           |                      |                           | 17,574                            |              | 17,574       |
| Deposit - acquisition of a business                                  |                           |                      | (161,000 )                |                                   |              | (161,000 )   |
| Dividend received - intercompany                                     |                           |                      | 15,000                    |                                   | (15,000 )    | —            |
| Intercompany advances  | (270,826 )                | (618,683 )           |                           |                                   | 889,509      | —            |
| Net cash used in investing activities                                | (270,826 )                | (618,683 )           | (84,866 )                 | (35,340 )                         | 874,509      | (135,206 )   |
| Cash flow provided by financing activities:                          |                           |                      |                           |                                   |              |              |
| Net proceeds from issuance of senior notes                           |                           | 600,000              |                           |                                   |              | 600,000      |
| Debt issuance costs for senior notes                                 |                           | (4,700 )             |                           |                                   |              | (4,700 )     |
| Proceeds from loans payable  |                           |                      |                           | 275,334                           |              | 275,334      |
| Principal payments of loans payable                                  |                           |                      | (8,331 )                  | (298,864 )                        |              | (307,195 )   |
| Net proceeds from issuance of common stock                           | 220,357                   |                      |                           |                                   |              | 220,357      |
| Proceeds from stock-based benefit plans                              | 18,529                    |                      |                           |                                   |              | 18,529       |
| Excess tax benefits from stock-based compensation                    | 789                       |                      |                           |                                   |              | 789          |
| Receipts related to noncontrolling interest                          |                           |                      |                           | 81                                |              | 81           |
| Purchase of treasury stock   | (84 )                     |                      |                           |                                   |              | (84 )        |
| Dividend paid - intercompany   |                           |                      |                           | (15,000 )                         | 15,000       | —            |
| Intercompany advances  |                           |                      | 773,035                   | 108,470                           | (881,505 )   | —            |
| Net cash provided by financing activities                            | 239,591                   | 595,300              | 764,704                   | 70,021                            | (866,505 )   | 803,111      |
| Net increase in cash and cash equivalents—                           | —                         | —                    | 400,644                   | 16,873                            | —            | 417,517      |
| Cash and cash equivalents, beginning of period                       | —                         | —                    | 670,102                   | 102,870                           | —            | 772,972      |
| Cash and cash equivalents, end of period                             | —                         | —                    | 1,070,746                 | 119,743                           | —            | 1,190,489    |

## Condensed Consolidating Statement of Cash Flows for the three months ended January 31, 2013:

|  | Toll<br>Brothers,<br>Inc. | Subsidiary<br>Issuer | Guarantor<br>Subsidiaries | Non-<br>Guarantor<br>Subsidiaries | Eliminations | Consolidated |
|--|---------------------------|----------------------|---------------------------|-----------------------------------|--------------|--------------|
| Net cash (used in) provided by operating activities                  | 24,053                    | 12,155               | (377,864 )                | 41,310                            | (5,476 )     | (305,822 )   |
| Cash flow provided by (used in) investing activities:                |                           |                      |                           |                                   |              |              |
| Purchase of property and equipment — net                             |                           |                      | (5,123 )                  | (268 )                            |              | (5,391 )     |
| Purchase of marketable securities                                    |                           |                      | (25,938 )                 | (81 )                             |              | (26,019 )    |
| Sale and redemption of marketable securities                         |                           |                      | 38,775                    |                                   |              | 38,775       |
| Investments in and advances to unconsolidated entities               |                           |                      | (2,280 )                  | (5,334 )                          |              | (7,614 )     |
| Return of investments in unconsolidated entities                     |                           |                      | 17,297                    | 14                                |              | 17,311       |
| Investments in distressed loans and foreclosed real estate           |                           |                      |                           | (16,252 )                         |              | (16,252 )    |
| Return of investments in distressed loans and foreclosed real estate |                           |                      |                           | 3,015                             |              | 3,015        |
| Intercompany advances  | (30,082 )                 | 46,913               |                           |                                   | (16,831 )    | —            |
| Net cash (used in) provided by investing activities                  | (30,082 )                 | 46,913               | 22,731                    | (18,906 )                         | (16,831 )    | 3,825        |
| Cash flow provided by (used in) financing activities:                |                           |                      |                           |                                   |              |              |
| Proceeds from loans payable  |                           |                      |                           | 244,830                           |              | 244,830      |
| Principal payments of loans payable                                  |                           |                      | (25,832 )                 | (274,030 )                        |              | (299,862 )   |
| Redemption of senior notes   |                           | (59,068 )            |                           |                                   |              | (59,068 )    |
| Proceeds from stock-based benefit plans                              | 6,108                     |                      |                           |                                   |              | 6,108        |
| Purchase of treasury stock   | (79 )                     |                      |                           |                                   |              | (79 )        |
| Intercompany advances  |                           |                      | (37,381 )                 | 15,074                            | 22,307       | —            |
| Net cash (used in) provided by financing activities                  | 6,029                     | (59,068 )            | (63,213 )                 | (14,126 )                         | 22,307       | (108,071 )   |
| Net (decrease) increase in cash and cash equivalents                 | —                         | —                    | (418,346 )                | 8,278                             | —            | (410,068 )   |
| Cash and cash equivalents, beginning of period                       | —                         | —                    | 712,024                   | 66,800                            | —            | 778,824      |
| Cash and cash equivalents, end of period                             | —                         | —                    | 293,678                   | 75,078                            | —            | 368,756      |

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS ("MD&A")

This discussion and analysis is based on, should be read with, and is qualified in its entirety by, the accompanying unaudited condensed consolidated financial statements and related notes, as well as our consolidated financial statements, notes thereto, and the related Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the fiscal year ended October 31, 2013. It also should be read in conjunction with the disclosure under "Statement on Forward-Looking Information" in this report.

Unless otherwise stated, net contracts signed represents a number or value equal to the gross number or value of contracts signed during the relevant period, less the number or value of contracts canceled during the relevant period, which includes contracts that were signed during the relevant period and in prior periods.

### OVERVIEW

#### Financial Highlights

In the three-month period ended January 31, 2014, we recognized \$643.7 million of revenues and net income of \$45.6 million, as compared to \$424.6 million of revenues and net income of \$4.4 million in the three-month period ended January 31, 2013. Fiscal 2014 three-month income before income taxes included \$2.0 million of inventory impairments and write-offs, as compared to \$0.7 million in the fiscal 2013 three-month period. During the fiscal 2014 three-month period, we recognized an income tax provision of \$25.7 million, as compared to \$3.9 million in the fiscal 2013 period.

At January 31, 2014, we had \$1.20 billion of cash, cash equivalents and marketable securities on hand and approximately \$963.9 million available under our \$1.035 billion revolving credit facility that matures in August 2018. In February 2014, we borrowed \$370 million under our revolving credit facility to partially fund the acquisition of all of the equity interests in Shapell Industries, Inc. ("Shapell"). We repaid \$170 million of the borrowing on February 12, 2014 and the remainder was repaid on February 26, 2014. See "Acquisition" section of this "Overview."

#### Our Business

We design, build, market and arrange financing for detached and attached homes in luxury residential communities. We cater to move-up, empty-nester, active-adult, age-qualified and second-home buyers in the United States. We also build and sell homes in urban infill markets through Toll City Living® ("City Living"). At January 31, 2014, we were operating in 20 states.

Over the past several years, we have acquired control of a number of land parcels as for-rent apartment projects, including two student housing sites. At January 31, 2014, we controlled a number of land parcels as for-rent apartment projects containing approximately 5,300 units. See "Toll Brothers Apartment Living/Toll Brothers Campus Living" section of this "Overview." Through Toll Brothers Realty Trust ("Trust"), we also have interests in approximately 1,500 operating apartment units in the Washington, D.C. area and in Princeton Junction, NJ.

We operate our own land development, architectural, engineering, mortgage, title, landscaping, security monitoring, lumber distribution, house component assembly, and manufacturing operations. We also develop, own and operate golf courses and country clubs, which generally are associated with several of our master planned communities. We have investments in a number of joint ventures to develop land for the sole use of the venture participants, including ourselves, and to develop land for sale to the joint venture participants and to unrelated builders. We are a participant in joint ventures with unrelated parties to develop luxury condominium projects, including for-sale and rental residential units and commercial space, a single master planned community, and a high-rise luxury for-sale condominium/hotel project. In addition, we formed and own interests in Toll Brothers Realty Trust II ("Trust II") to invest in commercial real estate opportunities. In December 2013, Trust II sold substantially all of its assets to an unrelated party. As a result of this sale, we realized a profit of approximately \$23.5 million in the fiscal 2014 period representing our share of the gain on the sale; this gain is included in "Income from unconsolidated entities" in our Condensed Consolidated Statements of Operations. In addition, we recognized \$2.9 million of previously deferred gains on the Company's initial sales of the properties to Trust II; this gain is included in "Other income - net" in our Condensed Consolidated Statements of Operations.

In fiscal 2010, we formed Gibraltar Capital and Asset Management LLC ("Gibraltar") to invest in distressed real estate opportunities. Gibraltar focuses primarily on residential loans and properties, from unimproved ground to partially and



fully improved developments, as well as commercial opportunities. See “Gibraltar” section of this "Overview."

## Acquisition

On February 4, 2014, we completed our previously announced acquisition of Shapell pursuant to the Purchase and Sale Agreement (the "Purchase Agreement"), dated November 6, 2013, with Shapell Investment Properties, Inc. ("SIPI"). Pursuant to the Purchase Agreement, we acquired, for cash, all of the equity interests in Shapell from SIPI for an aggregate purchase price of approximately \$1.60 billion (the "Acquisition"). We acquired the single-family residential real property development business of Shapell, including a portfolio of approximately 4,950 home sites in California, some of which we expect to sell to other builders. As of the acquisition date, Shapell's home building operation had 11 active selling communities in Northern California and Southern California, within which it is focused on a select number of premium markets. In addition, we acquired approximately \$120.0 million of cash. As part of the acquisition, we assumed contracts from Shapell to deliver approximately 126 homes with an aggregate value of approximately \$105.3 million. At January 31, 2014, we had deposited \$161.0 million of the purchase price with an escrow agent.

The purchase price is subject to post-closing adjustments in accordance with the terms of the Purchase Agreement. We financed the Acquisition with a combination of \$370 million of borrowings under its \$1.035 billion unsecured revolving credit facility, \$485 million from the term loan facility, and with the proceeds from debt and equity financings completed in November 2013. See Note 1, "Significant Accounting Policies - Subsequent Events" of our condensed consolidated financial statements for more information on these transactions.

Shapell was founded in 1955 as a home construction company that built custom-quality single-family home communities in Southern California. Shapell designed, constructed and marketed single-family detached and attached homes and developed land in master-planned communities and neighborhoods throughout coastal Northern and Southern California. Shapell's revenues from home building totaled \$354 million, \$252 million, \$272 million and \$447 million for calendar years 2010, 2011, 2012 and 2013, respectively.

Following the closing of the acquisition, we expect to selectively sell assets to reduce land concentration and outstanding borrowings; however, the timing and size of any asset sale transactions will be dependent on market and other factors, some of which are outside of our control. We make no assurance that we will be able to complete asset sale transactions on attractive terms or at all.

## Our Challenging Business Environment and Current Outlook

During fiscal 2012 and the first nine months of fiscal 2013, we saw a strong recovery in the number and value of new sales contracts signed. Our net contracts signed in fiscal 2012 and 2013, as compared to fiscal 2011, increased approximately 50% and 90%, respectively, in the number of net contracts signed and 59% and 126%, respectively, in the value of net contracts signed. Although the number and value of fiscal 2012 and 2013 net contracts signed increased over fiscal 2011, they were still significantly below what we recorded in fiscal 2005. We have witnessed a leveling of demand which began in the fourth quarter of our fiscal 2013 and has continued into fiscal 2014. In the six-month period ended January 31, 2014, we signed 2,079 contracts with an aggregate value of \$1.54 billion, compared to 2,071 contracts with an aggregate value of \$1.30 billion in the six-month period ended January 31, 2013. We believe this to be a temporary pause triggered by a rapid rise in interest rates and home prices, uncertainty from the political discord in Washington and the negative impact on our business due to the severe weather we have seen in many of our markets in the fiscal 2014 period.

We are still affected by the 2006-2011 downturn in the housing market. We believe the downturn started with a decline in consumer confidence, an overall softening of demand for new homes and an oversupply of homes available for sale. The downturn was exacerbated by, among other things, a decline in the overall economy, increased unemployment, the large number of homes that were vacant and homes that had been foreclosed on due to the economic downturn, a fear of job loss, a decline in home prices and the resulting reduction in home equity, the inability of some of our home buyers, or some prospective buyers of their homes, to sell their current homes, the deterioration in the credit markets, and the direct and indirect impact of the turmoil in the mortgage loan market. We believe that the demographics of the move-up, empty-nester, active-adult, age-qualified and second-home upscale markets will provide us with the potential for growth in the coming decade. According to the U.S. Census Bureau, the number of households earning \$100,000 or more (in constant 2012 dollars) at September 2013 stood at 26.9 million, or approximately 22% of all U.S. households. This group has grown at three times the rate of increase of all U.S.

households since 1980. According to Harvard University's June 2012 "The State of the Nation's Housing," the growth and aging of the current population, assuming the economic recovery is sustained over the next few years, supports the addition of about 1.2 million new household formations per year during the next decade.

According to the U.S. Census Bureau, during the period 1970 through 2006, total housing starts in the United States averaged approximately 1.6 million per year, while in the period 2007 through 2012, total housing starts averaged approximately 0.8 million per year. In addition, based on the trend of household formations in relation to population growth during the period 2000 through 2007, the number of households formations formed in the four year period of 2008 through 2011 was approximately 2.9 million less than would have been expected.

During the 2006-2011 downturn, in many markets, the pipeline of approved and improved home sites dwindled as many builders and developers lacked both the capital and the economic benefit for bringing sites through approvals. Therefore, we believe that, as demand continues to strengthen, builders and developers with approved land in well-located markets will be poised to benefit. We believe that this will be particularly true for us because our land portfolio is heavily weighted in the metro-Washington, DC to metro-Boston corridor where land is scarce, approvals are more difficult to obtain, and overbuilding has been relatively less prevalent than in the Southeast and Western regions.

We continue to believe that many of our communities are in desirable locations that are difficult to replace and in markets where approvals have been increasingly difficult to achieve. We believe that many of these communities have substantial embedded value that may be realized in the future as the housing recovery strengthens.

#### Competitive Landscape

Based on our experience during prior downturns in the housing industry, we believe that attractive land acquisition opportunities arise in difficult times for those builders that have the financial strength to take advantage of them. In the current environment, we believe our strong balance sheet, liquidity, access to capital, broad geographic presence, diversified product line, experienced personnel, and national brand name all position us well for such opportunities now and in the future.

We continue to see reduced competition from the small and mid-sized private builders that had been our primary competitors in the luxury market. We believe that many of these builders are no longer in business and that access to capital by the remaining private builders continues to be severely constrained. There are fewer and more selective lenders serving our industry as the market rebounds and we believe it is likely that those lenders will gravitate to the home building companies that offer them the greatest security, the strongest balance sheets, and the broadest array of potential business opportunities. While some builders may re-emerge with new capital, the scarcity of attractive land is a further impediment to their re-emergence. We believe that reduced competition, combined with attractive long-term demographics, will reward those well-capitalized builders that can persevere through the current challenging environment.

We believe that geographic and product diversification, access to lower-cost capital, and strong demographics benefit those builders, like us, who can control land and persevere through the increasingly difficult regulatory approval process. We believe that these factors favor a large publicly traded home building company with the capital and expertise to control home sites and gain market share. We also believe that over the past five years, many builders and land developers reduced the number of home sites that were taken through the approval process. The process continues to be difficult and lengthy, and the political pressure from no-growth proponents continues to increase, but we believe our expertise in taking land through the approval process and our already-approved land positions will allow us to grow in the years to come as market conditions improve.

#### Land Acquisition and Development

Because of the length of time that it takes to obtain the necessary approvals on a property, complete the land improvements on it, and deliver a home after a home buyer signs an agreement of sale, we are subject to many risks. In certain cases, we attempt to reduce some of these risks by utilizing one or more of the following methods: controlling land for future development through options (also referred to herein as “land purchase contracts” or “option and purchase agreements”), thus allowing the necessary governmental approvals to be obtained before acquiring title to the land; generally commencing construction of a detached home only after executing an agreement of sale and receiving a substantial down payment from the buyer; and using subcontractors to perform home construction and land development work on a fixed-price basis.

Based on our belief that the housing market has begun to recover, the increased attractiveness of land available for purchase, and the revival of demand in certain areas, we have increased our land positions. During fiscal 2013 and

2012, we acquired control of approximately 12,500 home sites (net of options terminated) and 6,100 home sites (net of options terminated), respectively. During the three-month period ended January 31, 2014, we acquired control of approximately 3,500 home sites (net of lot options terminated), including approximately 4,350 home sites in the Shapell acquisition. In February 2014, we acquired all of the equity interests in the single-family residential real property development business of Shapell, including a portfolio of approximately 4,950 home sites in California of which we currently expect to develop approximately 4,350 home sites and sell the remaining to other builders. See "Overview - Acquisition" in this MD&A for more information about the Shapell acquisition.

At January 31, 2014, we controlled approximately 51,200 home sites of which we owned approximately 34,100. Significant improvements were completed on approximately 13,500 of the 34,100 home sites. At January 31, 2014, we were selling from 238 communities, compared to 232 at October 31, 2013 and 225 communities at January 31, 2013. We acquired 11 well-established selling communities in February 2014 as part of the Shapell acquisition. In addition, we expect to purchase approximately 3,800 additional home sites from several joint ventures in which we have interests.

We expect to be selling from 250 to 290 communities at October 31, 2014. At January 31, 2014, we had 22 communities that were temporarily closed due to market conditions and that we do not expect to re-open during the next twelve months.

#### Availability of Customer Mortgage Financing

We maintain relationships with a widely diversified group of mortgage financial institutions, many of which are among the largest and, we believe, most reliable in the industry. We believe that regional and community banks continue to recognize the long-term value in creating relationships with high-quality, affluent customers such as our home buyers, and these banks continue to provide such customers with financing.

We believe that our home buyers generally are, and should continue to be, better able to secure mortgages due to their typically lower loan-to-value ratios and attractive credit profiles as compared to the average home buyer.

Nevertheless, in recent years, tightened credit standards have reduced the pool of potential home buyers and hindered accessibility of or eliminated certain loan products previously available to our home buyers. Our home buyers continue to face stricter mortgage underwriting guidelines, higher down payment requirements and narrower appraisal guidelines than in the past. In addition, some of our home buyers continue to find it more difficult to sell their existing homes as prospective buyers of their homes may face difficulties obtaining a mortgage. In addition, other potential buyers may have little or negative equity in their existing homes and may not be able or willing to purchase a larger or more expensive home.

While the range of mortgage products available to a potential home buyer is not what it was in the period 2005 through 2007, we have seen improvements over the past several years. Indications from industry participants, including commercial banks, mortgage banks, mortgage real estate investment trusts and mortgage insurance companies are that availability, parameters and pricing of jumbo loans are all improving. We believe that improvement should not only enhance financing alternatives for existing jumbo buyers, but also help to offset the reduction in Fannie Mae/Freddie Mac-eligible loan amounts in some markets. Based on the mortgages provided by our mortgage subsidiary, we do not expect the change in the Fannie Mae/Freddie Mac-eligible loan amounts to have a significant impact on our business.

There has been significant media attention given to mortgage put-backs, a practice by which a buyer of a mortgage loan tries to recoup losses from the loan originator. We do not believe this is a material issue for our mortgage subsidiary. Of the approximately 17,900 loans sold by our mortgage subsidiary since November 1, 2004, only 31 have been the subject of either actual indemnification payments or take-backs or contingent liability loss provisions related thereto. We believe that this is due to (i) our typical home buyer's financial position and sophistication, (ii) on average, our home buyers who use mortgage financing to purchase a home pay approximately 30% of the purchase price in cash, (iii) our general practice of not originating certain loan types such as option adjustable rate mortgages and down payment assistance products, and our origination of few sub-prime and high loan-to-value/no documentation loans, (iv) our elimination of "early payment default" provisions from each of our agreements with our mortgage investors several years ago, and (v) the quality of our controls, processes and personnel in our mortgage subsidiary. We have entered into two agreements with investors that contain limited early payment default provisions. At January 31, 2014, we sold one loan under these agreements. We believe that these limited early payment default provisions will not expose us to a significant risk.

The Dodd-Frank Wall Street Reform and Consumer Protection Act provides for a number of new requirements relating to residential mortgage lending practices. These include, among others, minimum standards for mortgages and related lender practices, the definitions and parameters of a Qualified Mortgage and a Qualified Residential Mortgage, future risk retention requirements, limitations on certain fees, prohibition of certain tying arrangements, and remedies for borrowers in foreclosure proceedings in the event that a lender violates fee limitations or minimum standards. We

do not believe that the effect of these requirements on our mortgage subsidiary will be significant, although it will restrict us from providing a comprehensive package of services to our home buyer due to fee restrictions imposed upon our home buyers as to what they are permitted to pay to our affiliated businesses.

Gibraltar

We continue to look for distressed real estate opportunities through Gibraltar. Gibraltar continues to selectively review new opportunities, including bank portfolios and other distressed real estate investments.

In the three month period ended January 31, 2013, Gibraltar acquired three loans directly and invested in a loan participation for an aggregate purchase price of approximately \$16.1 million. No loans were acquired in the three month period ended January 31, 2014.

At January 31, 2014, Gibraltar had investments in distressed loans of approximately \$19.3 million, investments in foreclosed real estate of \$79.3 million and an investment in a structured asset joint venture of \$22.6 million. In the fiscal 2014 and 2013 periods, we recognized income, including Gibraltar's equity in the earnings (losses) from its investment in a structured asset joint venture, of \$3.3 million and \$2.1 million from the Gibraltar operations, respectively.

#### Toll Brothers Apartment Living/Toll Brothers Campus Living

Over the past several years, we have acquired control of a number of land parcels as for-rent apartment projects, including two student housing sites. At January 31, 2014, we controlled a number of land parcels as for-rent apartment projects containing approximately 5,300 units. These projects, which are located in the metro-Boston to metro-Washington, D.C. corridor, are being developed or will be developed with partners under the brand names Toll Brothers Apartment Living and Toll Brothers Campus Living. A number of these sites had been acquired by us as part of a larger purchase or were originally acquired to develop as for-sale homes. Of the 5,300 planned units, 1,500 are owned by joint ventures in which we have a 50% interest; approximately 1,900 are owned by us; 1,200 of them are under contract to be purchased; and 700 of them are under letters of intent. Through the Trust, we also have interests in approximately 1,500 operating apartment units in the Washington, D.C. area and in Princeton Junction, NJ.

#### CONTRACTS AND BACKLOG

The aggregate value of net contracts signed increased \$87.3 million or 14.2% in the three-month period ended January 31, 2014, as compared to the three-month period ended January 31, 2013. The value of net contracts signed was \$701.7 million (916 homes) and \$614.4 million (973 homes) in the three-month periods ended January 31, 2014 and 2013, respectively. The increase in the aggregate value of net contracts signed in the fiscal 2014 period, as compared to the fiscal 2013 period, was the result of a 21.3% increase in the average value of each contract signed, offset, in part, by a 5.9% decline in the number of net contracts signed. The increase in the average value of each contract signed in the fiscal 2014 period, as compared to the fiscal 2013 period, was due primarily to a change in mix of contracts signed to more expensive areas, higher priced products, increased prices and reduced incentives given on new contracts signed. The decrease in the number of net contracts signed was primarily due to the previously discussed leveling in demand, as well as the negative impact on our business due to the severe weather we have seen in many of our markets in the fiscal 2014 period.

In the three-month period ended January 31, 2014, home buyers canceled \$47.2 million (69 homes) of signed contracts. In the three-month period ended January 31, 2013, home buyers canceled \$45.3 million (64 homes) of signed contracts. The cancellation rates of new contracts signed in the fiscal 2014 periods and 2013 periods were within our pre-downturn historical ranges.

Backlog consists of homes under contract but not yet delivered to our home buyers. The value of our backlog at January 31, 2014 of \$2.69 billion (3,667 homes) increased 44.5%, as compared to our backlog at January 31, 2013 of \$1.86 billion (2,796 homes). Our backlog at October 31, 2013 and 2012 was \$2.63 billion (3,679 homes) and \$1.67 billion (2,569 homes), respectively. The increase in the value of the backlog at January 31, 2014, as compared to the backlog at January 31, 2013, was primarily attributable to the higher backlog at October 31, 2013, as compared to the backlog at October 31, 2012 and the increase in the aggregate value of net contracts signed in the three-month period ended January 31, 2014, as compared to the three-month period ended January 31, 2013, offset, in part, by the increase in the aggregate value of our deliveries in the three-month period ended January 31, 2014, as compared to the aggregate value of deliveries in the three-month period ended January 31, 2013. The 57.5% and 43.2% increases in the value and number of homes in backlog at October 31, 2013, as compared to October 31, 2012, were due to the increase in the number and the average value of net contracts signed in fiscal 2013, as compared to fiscal 2012, offset, in part, by the increase in the aggregate value and number of our deliveries in fiscal 2013, as compared to the aggregate value and number of deliveries in fiscal 2012.

In February 2014, as part of the Shapell acquisition, we assumed contracts to deliver approximately 126 homes with an aggregate value of approximately \$105.3 million.



For more information regarding revenues, net contracts signed and backlog by operating segment, see “Operating Segments” in this MD&A.

## CRITICAL ACCOUNTING POLICIES

As disclosed in our Annual Report on Form 10-K for the fiscal year ended October 31, 2013, our most critical accounting policies relate to inventory, income taxes-valuation allowances and revenue and cost recognition. Since October 31, 2013, there have been no material changes to those critical accounting policies.

## OFF-BALANCE SHEET ARRANGEMENTS

We have investments in and advances to various unconsolidated entities. Our investments in these entities are accounted for using the equity method of accounting. At January 31, 2014, we had investments in and advances to these entities of \$430.6 million, and were committed to invest or advance \$76.9 million to these entities if they require additional funding. At January 31, 2014, we had joint venture purchase commitments to acquire 115 home sites for approximately \$12.6 million. In addition, we expect to purchase approximately 3,800 additional home sites from several joint ventures in which we have interests. The purchase price of these home sites will be determined at a future date. The unconsolidated entities in which we have investments generally finance their activities with a combination of partner equity and debt financing. In some instances, we and our partners have guaranteed debt of certain unconsolidated entities which may include any, or all, of the following: (i) project completion including any cost overruns, in whole or in part, (ii) repayment guarantees, generally covering a percentage of the outstanding loan, (iii) indemnification of the lender from environmental matters of the unconsolidated entity, (iv) a hazardous material indemnity that holds the lender harmless against any obligations for which the lender may incur liability resulting from the threat or presence of any hazardous or toxic substances at or near the property covered by a loan, and (v) indemnification of the lender from "bad boy acts" of the unconsolidated entity.

In some instances, the guarantees provided in connection with loans to an unconsolidated entity are joint and several. In these situations, we generally have a reimbursement agreement with our partner that provides that neither party is responsible for more than its proportionate share of the guarantee; however, if the joint venture partner does not have adequate financial resources to meet its obligations under the reimbursement agreement, we may be liable for more than our proportionate share.

We believe that as of January 31, 2014, in the event we become legally obligated to perform under a guarantee of the obligation of an unconsolidated entity due to a triggering event, the collateral should be sufficient to repay a significant portion of the obligation. If it is not, we and our partners would need to contribute additional capital to the venture. At January 31, 2014, the unconsolidated entities that have guarantees related to debt had loan commitments aggregating \$424.8 million and had borrowed an aggregate of \$89.8 million. We estimate that our maximum potential exposure under these guarantees, if the full amount of the loan commitments were borrowed, would be \$424.8 million before any reimbursement from our partners. Based on the amounts borrowed at January 31, 2014, our maximum potential exposure under these guarantees is estimated to be \$89.8 million before any reimbursement from our partners.

In addition, we have guaranteed approximately \$11.5 million of ground lease payments and insurance deductibles for three joint ventures.

For more information regarding these joint ventures, see Note 3, "Investments in and Advances to Unconsolidated Entities" in the Notes to Condensed Consolidated Financial Statements in this Form 10-Q.

The trends, uncertainties or other factors that have negatively impacted our business and the industry in general have also impacted the unconsolidated entities in which we have investments. We review each of our investments on a quarterly basis for indicators of impairment. A series of operating losses of an investee, the inability to recover our invested capital, or other factors may indicate that a loss in value of our investment in the unconsolidated entity has occurred. If a loss exists, we further review to determine if the loss is other than temporary, in which case we write down the investment to its fair value. The evaluation of our investment in unconsolidated entities entails a detailed cash flow analysis using many estimates including but not limited to expected sales pace, expected sales prices, expected incentives, costs incurred and anticipated, sufficiency of financing and capital, competition, market conditions and anticipated cash receipts, in order to determine projected future distributions. Each of the unconsolidated entities evaluates its inventory in a similar manner. See "Critical Accounting Policies - Inventory" contained in the MD&A in our Annual Report on Form 10-K for the year ended October 31, 2013 for more detailed disclosure on our evaluation of inventory. If a valuation adjustment is recorded by an unconsolidated entity related to

its assets, our proportionate share is reflected in income (loss) from unconsolidated entities with a corresponding decrease to our investment in unconsolidated entities. Based upon our evaluation of the fair value of our investments in unconsolidated entities, we determined that no impairments of our investments occurred in the three-month periods ended January 31, 2014 and 2013.

**RESULTS OF OPERATIONS**

The following table sets forth, for the three-month periods ended January 31, 2014 and 2013, a comparison of certain items in the Condensed Consolidated Statements of Operations (\$ amounts in millions):

|                                     | Three months ended January 31, |      |       |      |
|-------------------------------------|--------------------------------|------|-------|------|
|                                     | 2014                           |      | 2013  |      |
|                                     | \$                             | %*   | \$    | %*   |
| Revenues                            | 643.7                          |      | 424.6 |      |
| Cost of revenues                    | 514.0                          | 79.9 | 345.9 | 81.5 |
| Selling, general and administrative | 97.9                           | 15.2 | 78.0  | 18.4 |
|                                     | 611.9                          | 95.1 | 424.0 | 99.9 |
| Income from operations              | 31.8                           |      | 0.6   |      |
| Other                               |                                |      |       |      |
| Income from unconsolidated entities | 22.9                           |      | 3.1   |      |
| Other income - net                  | 16.5                           |      | 4.6   |      |
| Income before income taxes          | 71.2                           |      | 8.3   |      |
| Income tax provision                | 25.7                           |      | 3.9   |      |
| Net income                          | 45.6                           |      | 4.4   |      |

\* Percent of revenues

Note: Due to rounding, amounts may not add.

**REVENUES AND COST OF REVENUES**

Revenues for the three months ended January 31, 2014 were higher than those for the comparable period of fiscal 2013 by approximately \$219.1 million, or 51.6%. This increase was primarily attributable to a 24.4% increase in the number of homes delivered and a 21.9% increase in the average price of the homes delivered. In the fiscal 2014 period, we delivered 928 homes with a value of \$643.7 million, as compared to 746 homes in the fiscal 2013 period with a value of \$424.6 million. The average price of the homes delivered in the fiscal 2014 period was \$693,600, as compared to \$569,200 in the fiscal 2013 period. The increase in the number of homes delivered in the three-month period ended January 31, 2014, as compared to the three-month period ended January 31, 2013, was primarily due to the higher number of homes in backlog at the beginning of fiscal 2014, as compared to the beginning of fiscal 2013. The increase in the average price of homes delivered in the fiscal 2014 period, as compared to the fiscal 2013 period, was primarily attributable to a shift in the number of homes delivered to more expensive areas, higher priced products and price increases.

Cost of revenues as a percentage of revenues was 79.9% in the three-month period ended January 31, 2014, as compared to 81.5% in the three-month period ended January 31, 2013. In the three-month periods ended January 31, 2014 and 2013, we recognized inventory impairment charges and write-offs of \$2.0 million and \$0.7 million, respectively. Cost of revenues as a percentage of revenues, excluding inventory impairments, was 79.6% of revenues in the three-month period ended January 31, 2014, as compared to 81.3% in the three-month period ended January 31, 2013. The decrease in cost of revenues, excluding inventory impairment charges, as a percentage of revenue in the fiscal 2014 period, as compared to the fiscal 2013 period, was due primarily to the decreased cost of land, land improvements, materials and labor, lower interest, and increased prices in the fiscal 2014 period, as compared to the fiscal 2013 period. In the three-month periods ended January 31, 2014 and 2013, interest cost as a percentage of revenues was 4.0% and 4.7%, respectively.

**SELLING, GENERAL AND ADMINISTRATIVE EXPENSES ("SG&A")**

SG&A increased by \$19.9 million in the three-month period ended January 31, 2014, as compared to the three-month period ended January 31, 2013. As a percentage of revenues, SG&A was 15.2% in the fiscal 2014 period, as compared to 18.4% in the fiscal 2013 period. The fiscal 2014 period includes \$0.8 million of expenses incurred in the Shapell acquisition. The decline in SG&A, excluding the Shapell acquisition costs, as a percentage of revenues was due to SG&A spending increasing by 24.4% while revenues increased 51.6%. The dollar increase in SG&A costs was due primarily to increased compensation, sales and marketing costs and insurance.



#### INCOME FROM UNCONSOLIDATED ENTITIES

We are a participant in several joint ventures. We recognize our proportionate share of the earnings and losses from these entities. Many of our joint ventures are land development projects or high-rise/mid-rise construction projects and do not generate revenues and earnings for a number of years during the development of the property. Once development is complete, these joint ventures will generally, over a relatively short period of time, generate revenues and earnings until all assets of the entity are sold. Because there is not a steady flow of revenues and earnings from these entities, the earnings recognized from these entities will vary significantly from quarter-to-quarter and year-to-year.

In the three-month period ended January 31, 2014, we recognized \$22.9 million of income from unconsolidated entities, as compared to \$3.1 million in the comparable period of fiscal 2013. The increase in income from unconsolidated entities was due primarily from our recognition of a \$23.5 million gain representing our share of the gain on the sale by Trust II of substantially all of its assets to an unrelated party in December 2013. The increase due to the Trust II gain was partially offset by a loss realized from Gibraltar's Structured Asset Joint Venture in the fiscal 2014 period, as compared to income recognized in the fiscal 2013 period.

#### OTHER INCOME - NET

Other income - net includes the gains and losses from our ancillary businesses, income from Gibraltar, interest income, management fee income, retained customer deposits, income/losses on land sales and other miscellaneous items.

For the three months ended January 31, 2014 and 2013, other income-net was \$16.5 million and \$4.6 million, respectively. The increase in other income - net in the three-month period ended January 31, 2014, as compared to the fiscal 2013 period, was primarily due to an increase in income from higher earnings from land sales, increased income from our Gibraltar operations and higher management fee and other miscellaneous income in the fiscal 2014 period, as compared to the fiscal 2013 period. Included in Land sales, net, is \$2.9 million of previously deferred gains on our initial sales of the properties to Trust II.

#### INCOME BEFORE INCOME TAXES

For the three-month period ended January 31, 2014, we reported income before income taxes of \$71.2 million, as compared to \$8.3 million in the three-month period ended January 31, 2013.

#### INCOME TAX PROVISION

We recognized a \$25.7 million income tax provision in the three-month period ended January 31, 2014. Based upon the federal statutory rate of 35%, our federal tax provision would have been \$24.9 million. The difference between the tax provision recognized and the tax provision based on the federal statutory rate was due primarily to the recognition of \$2.5 million provision for state income taxes, net of a reversal of \$0.5 million of state valuation allowance, and \$0.8 million of accrued interest and penalties (net of federal tax provision) for previously accrued taxes on uncertain tax positions, offset, in part, by a \$1.8 million tax benefit from our utilization of domestic production activities deductions.

We recognized a \$3.9 million tax provision in the three-month period ended January 31, 2013. Based upon the federal statutory rate of 35%, our federal tax provision would have been \$2.9 million. The difference between the tax benefit recognized and the tax provision based on the federal statutory rate was due primarily to the recognition of \$1.2 million of accrued interest and penalties (net of federal tax provision) for previously accrued taxes on uncertain tax positions.

#### CAPITAL RESOURCES AND LIQUIDITY

Funding for our business has been provided principally by cash flow from operating activities before inventory additions, unsecured bank borrowings and the public debt and equity markets. At January 31, 2014, we had \$1.19 billion of cash and cash equivalents and \$13.0 million of marketable securities. At October 31, 2013, we had \$773.0 million of cash and cash equivalents and \$52.5 million of marketable securities. Cash used in operating activities during the three-month period ended January 31, 2014 was \$250.4 million. Cash used in operating activities during the fiscal 2014 period was primarily used for the purchase of inventory, offset, in part, by cash generated from net income, stock-based compensation and depreciation and amortization, an increase in customer deposits, and the sale of mortgage loans to outside investors in excess of mortgage loans originated.

In the three-month period ended January 31, 2014, cash used in our investing activities was \$135.2 million. The cash used in investing activities was primarily related to the \$161.0 million deposited in escrow for the acquisition of Shapell, \$60.4 million used to fund joint venture investments, and \$2.9 million for the purchase of property and equipment, offset, in part, by \$39.2 million of net sales of marketable securities and \$50.0 million of cash received as returns on our investments in unconsolidated entities, distressed loans and foreclosed real estate. We generated \$803.1 million of cash from financing activities in the three-month period ended January 31, 2014, primarily from the issuance of 7.2 million shares of our common stock in November

2013 that raised \$220.4 million, the issuance in November 2013 of \$350 million of 4.0% Senior Notes due 2018 and \$250 million of 5.625% Senior Notes due 2024, and \$18.5 million from the proceeds of our stock-based benefit plans, offset in part, by \$23.5 million of repayments of borrowings under our mortgage company warehouse facility, net of new borrowings under it, and \$8.3 million of net repayments of other loans payable.

At January 31, 2013, we had \$368.8 million of cash and cash equivalents and \$424.8 million of marketable securities. At October 31, 2012, we had \$778.8 million of cash and cash equivalents and \$439.1 million of marketable securities. Cash used in operating activities during the three-month period ended January 31, 2013 was \$305.8 million. Cash used in operating activities during the fiscal 2013 period was primarily used to fund the purchase of inventory, offset, in part, by cash generated from net income before stock-based compensation and depreciation and amortization, the sale of mortgage loans to outside investors in excess of mortgage loans originated, a reduction in restricted cash, and an increase in customer deposits.

In the three-month period ended January 31, 2013, cash provided by our investing activities was \$3.8 million. The cash provided by investing activities was primarily generated from \$12.8 million of net sales of marketable securities, \$20.3 million of cash received as returns on our investments in unconsolidated entities, distressed loans and foreclosed real estate, offset, in part, by \$7.6 million used to fund joint venture projects, \$16.3 million for investments in distressed loans and \$5.4 million for the purchase of property and equipment. We used \$108.1 million of cash from financing activities in the three-month period ended January 31, 2013, primarily for the repayment of \$59.1 million of our 6.875% senior notes in November 2012 and \$29.2 million of repayments of borrowings under our mortgage company warehouse facility, net of new borrowings under it, and \$25.8 million of repayments of other loans, net of new borrowings, offset, in part, by \$6.1 million from the proceeds of our stock-based benefit plans.

On February 4, 2014, we completed our previously announced acquisition of Shapell for an aggregate purchase price of approximately \$1.60 billion in cash. At January 31, 2014, we had deposited with an escrow agent, \$161.0 million of the purchase price. As part of the acquisition, we acquired approximately \$120.0 million of cash. We financed the Acquisition with a combination of (a) \$370 million of borrowings under its \$1.035 billion unsecured revolving credit facility, (b) \$485 million from the term loan facility, as well as with proceeds from debt and equity financings completed in November 2013. See Note 1, "Significant Accounting Policies - Subsequent Events" of our condensed consolidated financial statements for more information on these transactions.

At January 31, 2014, the aggregate purchase price of land parcels under option and purchase agreements was approximately \$1.17 billion. Of the \$1.17 billion of land purchase commitments, we paid or deposited \$76.8 million, and, if we acquire all of these land parcels, we will be required to pay an additional \$1.09 billion. In addition, we expect to acquire an additional 3,800 home sites from joint ventures in which we have a 50% interest; the purchase price of these home sites will be determined in the future. The purchases of these land parcels are scheduled over the next several years. We have additional land parcels under option that have been excluded from the aforementioned aggregate purchase amounts since we do not believe that we will complete the purchase of these land parcels and no additional funds will be required from us to terminate these contracts. At January 31, 2014, we also had purchase commitments to acquire land for apartment developments of approximately \$56.0 million.

In general, our cash flow from operating activities assumes that, as each home is delivered, we will purchase a home site to replace it. Because we owned approximately 34,100 home sites at January 31, 2014, we do not need to buy home sites immediately to replace those which we deliver. Of the 34,100 home sites we owned, approximately 13,500 are substantially improved. In addition, we generally do not begin construction of our single-family detached homes until we have a signed contract with the home buyer. Should our business decline from present levels, we believe that our inventory levels would decrease as we complete and deliver the homes under construction but do not commence construction of as many new homes, or incur additional costs to improve land we already own, and as we sell and deliver the speculative homes that are currently in inventory, all of which should result in additional cash flow from operations. In addition, we might curtail our acquisition of additional land which would further reduce our inventory levels and cash needs. During the three-month period ended January 31, 2014, we acquired control of approximately 3,500 home sites (net of lot options terminated), including approximately 4,350 home sites in the Shapell acquisition. At January 31, 2014, we owned or controlled through options approximately 51,200 home sites, as compared to 48,600 at October 31, 2013 and 43,700 at January 31, 2013.



On August 1, 2013, we entered into an \$1.035 billion unsecured, five-year credit facility with 15 banks which extends to August 1, 2018. Up to 75% of the credit facility is available for letters of credit. Under the terms of the credit facility, we are not permitted to allow our maximum leverage ratio (as defined in the credit agreement) to exceed 1.75 to 1.00, and we are required to maintain a minimum tangible net worth (as defined in the credit agreement) of approximately \$2.42 billion at January 31, 2014. At January 31, 2014, our leverage ratio was approximately 0.51 to 1.00, and our tangible net worth was approximately \$3.57 billion. Based upon the minimum tangible net worth requirement at January 31, 2014, our ability to repurchase our common stock was limited to approximately \$1.67 billion. At January 31, 2014, we had no outstanding borrowings under our credit facility but had outstanding letters of credit of approximately \$71.1 million. As part of the Shapell

acquisition, we borrowed \$370 million under the credit facility on February 3, 2014. We repaid \$170 million of the borrowing on February 12, 2014 and the remainder was repaid on February 26, 2014.

In addition, at January 31, 2014, we had \$12.5 million of letters of credit outstanding which were not part of our credit facility; these letters of credit are collateralized by \$12.7 million of restricted cash deposits.

On February 4, 2014, we entered into a 364-day senior unsecured revolving credit facility (the "364-Day Facility") with five banks. The 364-Day Facility provides for an unsecured revolving credit facility to be made available to us prior to February 3, 2015, in the amount of \$500 million. We intend for this facility to remain undrawn and its existence is to provide us additional liquidity should unforeseen circumstances arise. On February 3, 2014, we entered into a 5-year senior, \$485 million, unsecured term loan facility (the "Term Loan Facility") with ten banks. We borrowed the full amount of the Term Loan Facility on February 3, 2014. The initial interest rate on the Term Loan will be 1.72% per annum.

See Note 1, "Significant Accounting Policies - Subsequent Events" of our condensed consolidated financial statements for more information on these transactions.

We believe that we will be able to continue to fund our current operations and meet our contractual obligations through a combination of existing cash resources and other sources of capital and credit. Due to the tight credit markets and the uncertainties that exist in the economy and for home builders in general, we cannot be certain that we will be able to replace existing financing or find sources of additional financing in the future; moreover, if we are able to replace all or some of such facilities, we may be subjected to more restrictive borrowing terms and conditions.

#### OPERATING SEGMENTS

We operate in two segments: Traditional Home Building and Urban Infill ("City Living"). We operate our Traditional Home Building operations in four geographic segments around the United States: the North, consisting of Connecticut, Illinois, Massachusetts, Michigan, Minnesota, New Jersey and New York; the Mid-Atlantic, consisting of Delaware, Maryland, Pennsylvania, Virginia; the South, consisting of Florida, North Carolina, South Carolina, and Texas; and the West, consisting of Arizona, California, Colorado, Nevada and Washington.

The tables below summarize information related to units delivered and revenues and net contracts signed by segment for the three-month periods ended January 31, 2014 and 2013, and information related to backlog by segment at January 31, 2014 and 2013, and at October 31, 2013 and 2012.

Units Delivered and Revenues (\$ amounts in millions):

|                            | Three months ended January 31, |       |         |         |
|----------------------------|--------------------------------|-------|---------|---------|
|                            | 2014                           | 2013  | 2014    | 2013    |
|                            | Units                          | Units | \$      | \$      |
| Traditional Home Building: |                                |       |         |         |
| North                      | 209                            | 151   | \$127.6 | \$82.3  |
| Mid-Atlantic               | 273                            | 236   | 169.1   | 129.6   |
| South                      | 225                            | 143   | 150.6   | 87.2    |
| West                       | 204                            | 200   | 186.2   | 112.6   |
| Traditional Home Building  | 911                            | 730   | 633.5   | 411.7   |
| City Living                | 17                             | 16    | 10.2    | 12.9    |
| Total                      | 928                            | 746   | \$643.7 | \$424.6 |

## Net Contracts Signed (\$ amounts in millions):

|                            | Three months ended January 31, |       |         |         |
|----------------------------|--------------------------------|-------|---------|---------|
|                            | 2014                           | 2013  | 2014    | 2013    |
|                            | Units                          | Units | \$      | \$      |
| Traditional Home Building: |                                |       |         |         |
| North                      | 181                            | 235   | \$118.2 | \$130.4 |
| Mid-Atlantic               | 263                            | 262   | 163.8   | 146.9   |
| South                      | 222                            | 203   | 168.3   | 137.5   |
| West                       | 199                            | 241   | 187.9   | 177.9   |
| Traditional Home Building  | 865                            | 941   | 638.2   | 592.7   |
| City Living                | 51                             | 32    | 63.5    | 21.7    |
| Total                      | 916                            | 973   | \$701.7 | \$614.4 |

## Backlog (\$ amounts in millions):

|                            | At January 31, |       |           |           | At October 31, |       |           |           |
|----------------------------|----------------|-------|-----------|-----------|----------------|-------|-----------|-----------|
|                            | 2014           | 2013  | 2014      | 2013      | 2013           | 2012  | 2013      | 2012      |
|                            | Units          | Units | \$        | \$        | Units          | Units | \$        | \$        |
| Traditional Home Building: |                |       |           |           |                |       |           |           |
| North                      | 920            | 709   | \$553.1   | \$398.2   | 948            | 625   | \$562.5   | \$350.0   |
| Mid-Atlantic               | 892            | 660   | 567.7     | \$391.8   | 902            | 634   | 573.0     | 374.5     |
| South                      | 953            | 809   | 691.2     | \$533.8   | 956            | 749   | 673.5     | 483.5     |
| West                       | 670            | 548   | 594.8     | \$416.3   | 675            | 507   | 593.2     | 351.0     |
| Traditional Home Building  | 3,435          | 2,726 | 2,406.8   | 1,740.1   | 3,481          | 2,515 | 2,402.2   | 1,559.0   |
| City Living                | 232            | 70    | \$280.7   | \$119.6   | 198            | 54    | 227.3     | 110.9     |
| Total                      | 3,667          | 2,796 | \$2,687.5 | \$1,859.7 | 3,679          | 2,569 | \$2,629.5 | \$1,669.9 |

## Revenues and Income (Loss) Before Income Taxes:

The following table summarizes by segment total revenues and income (loss) before income taxes for the three-month periods ended January 31, 2014 and 2013 (amounts in millions):

|                            | Three months ended January 31, |         |
|----------------------------|--------------------------------|---------|
|                            | 2014                           | 2013    |
| Revenue:                   |                                |         |
| Traditional Home Building: |                                |         |
| North                      | \$127.6                        | \$82.3  |
| Mid-Atlantic               | 169.1                          | 129.6   |
| South                      | 150.6                          | 87.2    |
| West                       | 186.2                          | 112.6   |
| Traditional Home Building  | 633.5                          | 411.7   |
| City Living                | 10.2                           | 12.9    |
| Total                      | \$643.7                        | \$424.6 |

|                                    | Three months ended<br>January 31, |          |
|------------------------------------|-----------------------------------|----------|
|                                    | 2014                              | 2013     |
| Income (loss) before income taxes: |                                   |          |
| Traditional Home Building:         |                                   |          |
| North                              | \$8.3                             | \$4.7    |
| Mid-Atlantic                       | 21.5                              | 14.9     |
| South                              | 17.4                              | 2.8      |
| West                               | 34.7                              | 8.0      |
| Traditional Home Building          | 81.9                              | 30.4     |
| City Living                        | (1.1)                             | ) 2.7    |
| Corporate and other (a)            | (9.6)                             | ) (24.8) |
| Total                              | \$71.2                            | \$8.3    |

“Corporate and other” is comprised principally of general corporate expenses such as the offices of the Executive Officers of the Company; and the corporate finance, accounting, audit, tax, human resources, risk management, marketing and legal groups; interest income and income from the our ancillary businesses, including Gibraltar; and income from a number of our unconsolidated entities.

#### North

Revenues in the three-month period ended January 31, 2014 were higher than those for the comparable period of fiscal 2013 by \$45.3 million, or 55.0%. The increase in revenues was primarily attributable to increases of 38.4% and 12.0% in the number and average selling price of homes delivered, respectively. The increase in the number of homes delivered in the fiscal 2014 period, as compared to the fiscal 2013 period, was due to a higher backlog at October 31, 2013, as compared to October 31, 2012. The increase in the average selling price of the homes delivered in the fiscal 2014 period was primarily due to a shift in the number of homes delivered to more expensive areas and/or products and increases in selling prices in fiscal 2013.

The value of net contracts signed in the three-month period ended January 31, 2014 was \$118.2 million, a 9.4% decrease from the \$130.4 million of net contracts signed during the three-month period ended January 31, 2013. This decrease was primarily due to a decrease of 23.0% in the number of net contracts signed, offset, in part, by a 17.6% increase in the average value of each net contract. The decrease in the number of net contracts signed was primarily due to the previously discussed leveling in demand, as well as the negative impact on our business due to the severe weather we have seen in this region in the fiscal 2014 period. The increase in the average sales price of net contracts signed was primarily due to a shift in the number of contracts signed to more expensive areas and/or products, in the fiscal 2014 period, as compared to the fiscal 2013 period, and increases in base selling prices.

For the three-month period ended January 31, 2014, we reported income before income taxes of \$8.3 million, as compared to \$4.7 million for the three-month period ended January 31, 2013. This increase in income was primarily attributable to higher earnings from the increased revenues, offset, in part, by higher SG&A and higher inventory impairment charges, in the fiscal 2014 period, as compared to the fiscal 2013 period. Inventory impairment charges, in the three-month periods ended January 31, 2014 and 2013, were \$1.5 million and \$0.6 million, respectively.

#### Mid-Atlantic

For the three-month period ended January 31, 2014, revenues were higher than those for the three-month period ended January 31, 2013, by \$39.5 million, or 30.5%. The increase in revenues was primarily attributable to a 15.7% increase in the number of homes delivered and a 12.8% increase in the average selling price of the homes delivered. The increase in the number of homes delivered in the fiscal 2014 period, as compared to the fiscal 2013 period, was primarily due to a higher backlog at October 31, 2013, as compared to October 31, 2012. The increase in the average price of homes delivered in the fiscal 2014 period, as compared to the fiscal 2013 period, was primarily attributable to a shift in the number of homes delivered to more expensive areas and/or products and increases in selling prices in fiscal 2013.

The value of net contracts signed during the three-month period ended January 31, 2014 increased by \$16.9 million, or 11.5%, from the three-month period ended January 31, 2013. The increase was due to a 11.1% increase in the average

value of each net contract signed and a 0.4% increase in the number of net contracts signed. The increase in the average sales price of net contracts signed was primarily due to a shift in the number of contracts signed to more expensive areas and/or products in the fiscal 2014 period, as compared to the fiscal 2013 period and increases in selling prices.

We reported income before income taxes for the three-month periods ended January 31, 2014 and 2013, of \$21.5 million and \$14.9 million, respectively. This increase in the income before income taxes was primarily due to higher earnings from the increased revenues and \$2.9 million of earnings from land sales in the fiscal 2014 period, offset, in part, by higher SG&A costs, in the fiscal 2014 period, as compared to the fiscal 2013 period. The land sales in three months ended January 31, 2014 represents previously deferred gains on our initial sales of the properties to Trust II. South

Revenues in the three-month period ended January 31, 2014 were higher than those for the three-month period ended January 31, 2013 by \$63.4 million, or 72.7%. This increase was attributable to a 57.3% increase in the number of homes delivered and a 9.8% increase in the average price of the homes delivered. The increase in the number of homes delivered in the fiscal 2014 period was primarily due to a higher backlog at October 31, 2013, as compared to October 31, 2012, primarily in Florida and Texas. The increase in the average price of the homes delivered was primarily attributable to a shift in the number of homes delivered to more expensive areas and/or products in the fiscal 2014 period and increases in selling prices in fiscal 2013.

For the three-month period ended January 31, 2014, the value of net contracts signed increased by \$30.8 million, or 22.4%, as compared to the three-month period ended January 31, 2013. The increase was attributable to increases of 9.4% and 11.9% in the number and average value of net contracts signed, respectively. The increase in the number of net contracts signed in the three-month period ended January 31, 2014 was primarily due to increased demand in Florida in the fiscal 2014 period, as compared to the fiscal 2013 period. The increase in the average sales price of net contracts signed was primarily due to a shift in the number of contracts signed to more expensive areas and/or products and increases in base selling prices in the fiscal 2014 period.

For the three-month periods ended January 31, 2014 and 2013, we reported income before income taxes of \$17.4 million and \$2.8 million, respectively. The increase in the income before income taxes was primarily due to land sales of \$3.3 million in the fiscal 2014 period and higher earnings from the increased revenues in the fiscal 2014 period, as compared to the fiscal 2013 period, partially offset by higher SG&A costs.

#### West

Revenues in the three-month period ended January 31, 2014 were higher than those in the three-month period ended January 31, 2013 by \$73.6 million, or 65.4%. The increase in revenues was attributable to a 62.2% increase in the average sales price of the homes delivered and a 2.0% increase in the number of homes delivered. The increase in the average price of the homes delivered was primarily due to a shift in the number of homes delivered to more expensive products and/or locations and an increase in selling prices.

The value of net contracts signed during the three-month period ended January 31, 2014 increased \$10.0 million, or 5.6%, as compared to the three-month period ended January 31, 2013. This increase was due to a 27.9% increase in the average value of each net contract signed, partially offset by a decrease of 17.4% in the number of net contracts signed. The increase in the average sales price of net contracts signed was primarily due to a shift in the number of contracts signed to more expensive areas and/or products and increases in base selling prices. The decrease in the number of net contracts signed was primarily due to a reduction of available inventory in the fiscal 2014, as compared to fiscal 2013, in California.

For the three-month period ended January 31, 2014 and 2013, we reported income before income taxes of \$34.7 million and \$8.0 million, respectively. The increase in income before income taxes was primarily due to higher earnings from the increased revenues and lower cost of revenues as a percentage of revenues, offset, in part, by higher SG&A costs in the fiscal 2014 period. Cost of revenues as a percentage of revenues was 73.7% in the three-month period ended January 31, 2014, as compared to 83.3% in the fiscal 2013 period. The decrease in cost of revenues as a percentage of revenue in the fiscal 2014 period was primarily due to a shift in the number of homes delivered to better margin products and/or locations and increases in selling prices.

#### City Living

For the three-months ended January 31, 2014, revenues were lower than those for the three-months ended January 31, 2013, by \$2.7 million, or 20.9%. The decrease in revenues was primarily attributable to a decrease of 26.0% in the average selling price of the homes delivered, offset, in part, by a 6.3% increase in the number of homes delivered. The decrease in the average sales price of homes delivered was primarily due to a shift in the number of homes delivered

to less expensive areas and/or products. The increase in the number of homes delivered was primarily due to an increase in homes delivered in the Pennsylvania City Living communities, partially offset by decreases in units delivered in the New York and New Jersey urban markets. The increase in the number of homes delivered in Pennsylvania was primarily due to a higher backlog at October 31, 2013, as

compared to October 31, 2012. The decrease in the number of units delivered in the New York and New Jersey urban markets was due to settling out of two of our high rise buildings in fiscal 2013.

For the three-month period ended January 31, 2014, the value of net contracts signed increased by \$41.8 million, or 192.6%, as compared to the three-month period ended January 31, 2013. The increase was attributable to increases of 59.4% and 84.1% in the number and average value of net contracts signed, respectively. The increase in the number of net contracts signed in the three-month period ended January 31, 2014 was primarily due to the commencement of sales at several of our buildings in the second quarter of fiscal 2013. The increase in the average sales price of net contracts signed was primarily due to a shift in the number of contracts signed to more expensive areas and/or products in the fiscal 2014 period.

We reported a loss before income taxes of \$1.1 million in the three-months ended January 31, 2014, as compared to income before income taxes of \$2.7 million in the three-months ended January 31, 2013. The increase in the loss was primarily attributable to higher cost of revenues as a percentage of revenues in three-months ended January 31, 2014, as compared to three-months ended January 31, 2013. Cost of revenues as a percentage of revenues was 89.6% and 68.7% in three-months ended January 31, 2014 and 2013, respectively. This increase in cost of revenues as a percentage of revenues was primarily due to a shift in the number of homes delivered to less expensive areas and/or products.

#### Corporate and Other

For the three-month period ended January 31, 2014 and 2013, corporate and other loss before income taxes was \$9.6 million and \$24.8 million, respectively. The decrease in the loss in the fiscal 2014 period, as compared to the fiscal 2013 period, was primarily due to an increase in income from unconsolidated entities from \$2.5 million in the fiscal 2013 period to \$22.8 million in the fiscal 2013 period, and increased income from our Gibraltar operations in the fiscal 2014 period, as compared to the fiscal 2013 period, offset, in part, by higher unallocated SG&A and lower income from ancillary businesses in the fiscal 2014 period, as compared to the fiscal 2013 period. The increase in unallocated SG&A costs was due primarily to increased compensation and insurance costs as a result of the increase in our business activity.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk primarily due to fluctuations in interest rates. We utilize both fixed-rate and variable-rate debt. For fixed-rate debt, changes in interest rates generally affect the fair market value of the debt instrument, but not our earnings or cash flow. Conversely, for variable-rate debt, changes in interest rates generally do not impact the fair market value of the debt instrument, but do affect our earnings and cash flow. We do not have the obligation to prepay fixed-rate debt prior to maturity, and, as a result, interest rate risk and changes in fair market value should not have a significant impact on our fixed-rate debt until we are required or elect to refinance it.

The table below sets forth, at January 31, 2014, our debt obligations, principal cash flows by scheduled maturity, weighted-average interest rates, and estimated fair value (amounts in thousands):

| Fiscal year of maturity        | Fixed-rate debt |                                | Variable-rate debt (a) |                                |
|--------------------------------|-----------------|--------------------------------|------------------------|--------------------------------|
|                                | Amount          | Weighted-average interest rate | Amount                 | Weighted-average interest rate |
| 2014                           | \$315,802       | 4.95%                          | \$60,905               | 2.56%                          |
| 2015                           | 349,936         | 5.07%                          | 150                    | 0.25%                          |
| 2016                           | 9,346           | 5.40%                          | 150                    | 0.25%                          |
| 2017                           | 404,287         | 8.88%                          | 150                    | 0.25%                          |
| 2018                           | 3,494           | 4.66%                          | 150                    | 0.25%                          |
| Thereafter                     | 1,988,682       | 4.54%                          | 2,360                  | 0.25%                          |
| Discount                       | (3,485)         |                                |                        |                                |
| Total                          | \$3,068,062     | 5.22%                          | \$63,865               | 2.45%                          |
| Fair value at January 31, 2014 | \$3,229,728     |                                | \$63,865               |                                |

(a) Based upon the amount of variable-rate debt outstanding at January 31, 2014, and holding the variable-rate debt balance constant, each 1% increase in interest rates would increase the interest incurred by us by approximately



\$0.6 million per year.

#### ITEM 4. CONTROLS AND PROCEDURES

Any controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints and the benefits of controls must be considered relative to costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected; however, our disclosure controls and procedures are designed to provide reasonable assurance of achieving their objectives.

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this report (the "Evaluation Date"). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, our disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed in our reports under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There has not been any change in our internal control over financial reporting during our quarter ended January 31, 2014 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

#### PART II — OTHER INFORMATION

##### ITEM 1. LEGAL PROCEEDINGS

We are involved in various claims and litigation arising principally in the ordinary course of business. We believe that adequate provision for resolution of all current claims and pending litigation has been made for probable losses and the disposition of these matters will not have a material adverse effect on our results of operations and liquidity or on our financial condition.

##### ITEM 1A. RISK FACTORS

There have been no material changes in our risk factors as previously disclosed in our Form 10-K for the fiscal year ended October 31, 2013.

## ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

### ISSUER PURCHASES OF EQUITY SECURITIES

During the three-month period ended January 31, 2014, we repurchased the following shares of our common stock:

| Period                                | Total number<br>of shares<br>purchased (b) | Average<br>price<br>paid per share | Total number<br>of shares<br>purchased as<br>part of<br>publicly<br>announced<br>plans or<br>programs (a) | Maximum<br>number of<br>shares<br>that may yet<br>be<br>purchased<br>under the<br>plans or<br>programs (a) |
|---------------------------------------|--|------------------------------------|---|--|
|                                       | (in thousands)                             |                                    | (in thousands)  | (in thousands)   |
| November 1, 2013 to November 30, 2013 | 1  | \$35.14                            | 1   | 8,268  |
| December 1, 2013 to December 31, 2013 | 6  | 33.05                              | 2   | 8,266  |
| January 1, 2014 to January 31, 2014   | —  |                                    |   | 8,266  |
| Total                                 | 7  | \$33.09                            | 3   |  |

(a) On March 26, 2003, we announced that our Board of Directors had authorized the repurchase of up to 20 million shares of our common stock, par value \$.01, from time to time, in open market transactions or otherwise, for the purpose of providing shares for our various employee benefit plans. The Board of Directors did not fix an expiration date for the repurchase program.

(b) Our stock incentive plans permit participants to exercise non-qualified stock options using a “net exercise” method at the discretion of the Executive Compensation Committee of our Board of Directors. In a net exercise, we generally withhold from the total number of shares that otherwise would be issued to the participant upon exercise of the stock option that number of shares having a fair market value at the time of exercise equal to the option exercise price and applicable income tax withholdings, and remit the remaining shares to the participant. During the three-month period ended January 31, 2014, the net exercise method was employed to exercise stock options to acquire 86,346 of our common stock; we withheld 52,511 of the shares subject to stock options to cover \$1.7 million of option exercise price and income tax withholdings and we issued the remaining 33,835 shares to the recipients. The shares withheld in connection with the net exercise method are not included in the total number of shares purchased in the table above.

Our stock incentive plans permit us to withhold from the total number of shares that otherwise would be issued to a restricted stock unit recipient upon distribution that number of shares having a fair value at the time of distribution equal to the applicable income tax withholdings due and remit the remaining shares to the restricted stock unit recipient. During the three months ended January 31, 2014, we withheld 144,948 of the shares subject to restricted stock unit to cover \$5.0 million of income tax withholdings and we issued the remaining 176,799 shares to the recipients. The shares withheld in connection with the net exercise method are not included in the total number of shares purchased in the table above.

In addition, our stock incentive plans also permit participants in our stock option plans to use the fair market value of Company common stock they own to pay for the exercise of stock options (“stock swap method”). During the three-month period ended January 31, 2014, we received 4,273 shares with an average fair market value per share of \$33.01 for the exercise of 7,006 option using the stock swap method. The 4,273 shares used under the stock swap method are included in the total number of shares purchased in the table above.

Except as set forth above, we have not repurchased any of our equity securities during the three-month period ended January 31, 2014.

We have not paid any cash dividends on our common stock to date and expect that, for the foreseeable future, we will not do so.



ITEM 6. EXHIBITS

- 31.1\* Certification of Douglas C. Yearley, Jr. pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2\* Certification of Martin P. Connor pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1\* Certification of Douglas C. Yearley, Jr. pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2\* Certification of Martin P. Connor pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INS\* XBRL Instance Document
- 101.SCH\* XBRL Schema Document
- 101.CAL\* XBRL Calculation Linkbase Document
- 101.LAB\* XBRL Labels Linkbase Document
- 101.PRE\* XBRL Presentation Linkbase Document
- 101.DEF\* XBRL Definition Linkbase Document
- \* Filed electronically herewith.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

TOLL BROTHERS, INC.  
(Registrant)

Date: March 10, 2014

By: /s/ Martin P. Connor

Martin P. Connor  
Senior Vice President and Chief Financial  
Officer (Principal Financial Officer)

Date: March 10, 2014

By: /s/ Joseph R. Sicree

Joseph R. Sicree  
Senior Vice President and Chief Accounting  
Officer (Principal Accounting Officer)