

Comstock Holding Companies, Inc.  
Form 10-K  
March 27, 2013  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**Form 10-K**

(Mark One)

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

For the fiscal year ended December 31, 2012

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 001-32375

**Comstock Holding Companies, Inc.**

(Exact name of registrant as specified in its charter)

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

**Delaware** **20-1164345**  
(State or other jurisdiction of **(I.R.S. Employer**  
  
incorporation or organization) **Identification No.)**  
**1886 Metro Center Drive, 4th Floor, Reston, Virginia 20190**  
  
(Address of principal executive offices) (Zip Code)

**Registrant's telephone number, including area code (703) 883-1700**

**Securities registered pursuant to Section 12(b) of the Act:**

<b>Title of each class</b>	<b>Name of each exchange on which registered</b>
<b>Class A Common Stock, par value \$0.01 per share</b>	<b>The Nasdaq Stock Market LLC</b>
<b>Preferred Stock Purchase Rights</b>	<b>Nasdaq Capital Market</b>

**Securities registered pursuant to Section 12(g) of the Act:**

**None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

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

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

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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. (check one)

Large Accelerated filer <input type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input checked="" type="checkbox"/>

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

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

The aggregate market value of voting and non-voting common equity held by non-affiliates of the registrant (10,247,394 shares) based on the last reported sale price of the registrant's common equity on the Nasdaq Global Market ( NASDAQ ) on June 30, 2012, which was the last business day of the registrant's most recently completed second fiscal quarter, was \$13,424,086. For purposes of this computation, all officers, directors, and 10% beneficial owners of the registrant are deemed to be affiliates. This determination of affiliate status is not necessarily conclusive for other purposes.

As of March 27, 2013, there were outstanding 18,243,052 shares of the registrant's Class A common stock, par value \$0.01 per share, and 2,733,500 shares of the registrant's Class B common stock, par value \$0.01 per share.

### **DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the registrant's definitive Proxy Statement for the 2013 Annual Meeting of Stockholders, to be filed within 120 days after the registrant's fiscal year ended December 31, 2012, are incorporated by reference into Part III of this Form 10-K.

**Table of Contents**

**COMSTOCK HOLDING COMPANIES, INC.**

**ANNUAL REPORT ON FORM 10-K**

**For the Fiscal Year Ended December 31, 2012**

**TABLE OF CONTENTS**

<b><u>PART I</u></b>		1
Item 1.	<u>Business</u>	1
Item 1A.	<u>Risk Factors</u>	6
Item 1B.	<u>Unresolved Staff Comments</u>	13
Item 2.	<u>Properties</u>	13
Item 3.	<u>Legal Proceedings</u>	13
Item 4.	<u>Mine Safety Disclosures</u>	13
<b><u>PART II</u></b>		16
Item 5.	<u>Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u>	13
Item 6.	<u>Selected Financial Data</u>	14
Item 7.	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	14
Item 7A.	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	23
Item 8.	<u>Financial Statements and Supplementary Data</u>	23
Item 9.	<u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u>	23
Item 9A.	<u>Controls and Procedures</u>	23
Item 9B.	<u>Other Information</u>	23
<b><u>PART III</u></b>		24
Item 10.	<u>Directors, Executive Officers and Corporate Governance</u>	24
Item 11.	<u>Executive Compensation</u>	24
Item 12.	<u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u>	24
Item 13.	<u>Certain Relationships and Related Transactions, and Director Independence</u>	24
Item 14.	<u>Principal Accountant Fees and Services</u>	24
<b><u>PART IV</u></b>		25
Item 15.	<u>Exhibits and Financial Statement Schedules</u>	25
<b><u>SIGNATURES</u></b>		29
<b><u>INDEX TO CONSOLIDATED FINANCIAL STATEMENTS</u></b>		F-1

---

**Table of Contents**

**PART I**

**CAUTIONARY NOTES REGARDING FORWARD-LOOKING STATEMENTS**

Some of the statements contained in this report include forward-looking statements. These forward-looking statements can be identified by the use of words such as anticipate, believe, estimate, may, intend, expect, will, should, seeks or other similar expressions. Forward-looking statements are based largely on our expectations and involve inherent risks and uncertainties including certain risks described in this report. When considering those forward-looking statements, you should keep in mind the risks, uncertainties and other cautionary statements made in this report. You should not place undue reliance on any forward-looking statement, which speaks only as of the date made. Some factors which may affect the accuracy of the forward-looking statements apply generally to the real estate industry, while other factors apply directly to us. Any number of important factors which could cause actual results to differ materially from those in the forward-looking statements include: general economic and market conditions, including interest rate levels; our ability to service our debt; inherent risks in investment in real estate; our ability to compete in the markets in which we operate; regulatory actions; fluctuations in operating results; our anticipated growth strategies; shortages and increased costs of labor or building materials; the availability and cost of land in desirable areas; natural disasters; our ability to raise debt and equity capital and grow our operations on a profitable basis and our continuing relationships with affiliates.

Many of these factors are beyond our control. For a discussion of factors that could cause actual results to differ, please see the discussion in this report under the heading **Risk Factors** in Item 1A.

**Item 1. Business**

The following business description should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this Annual Report on Form 10-K.

**Overview**

Comstock Holding Companies, Inc. is a multi-faceted real estate development and services company focused on the Washington, D.C. metropolitan area. We have substantial experience with building a diverse range of products including apartments, single-family homes, townhouses, mid-rise condominiums, high-rise multi-family condominiums and mixed-use (residential and commercial) developments. Since our founding in 1985, and as of December 31, 2012, we have built and delivered more than 5,500 units generating total revenue in excess of \$1.4 billion. References in this Form 10-K to Comstock, Company, we, our and us refer to Comstock Holding Companies, Inc. together in each case with our subsidiaries and any predecessor entities unless the context suggests otherwise. Dollars in thousands unless otherwise indicated.

**Our Operating Market**

We are exclusively focused on the Washington, D.C. market, which is the eighth largest metropolitan statistical area in the United States. Our expertise in developing traditional and non-traditional housing products enables us to focus on a wide range of opportunities within our core market. We build homes and apartment buildings in suburban communities, where we focus on low density products such as single family detached homes, townhomes and mid-rise multi-family buildings, and in urban areas, where we focus on high density multi-family and mixed use products. For our homebuilding operations, we develop properties with the intent that they be sold either as fee-simple properties or condominiums to individual unit buyers or as investment properties sold to private or institutional investors. Our homebuilding products are designed to attract first-time, early move-up and secondary move-up buyers. We focus on products that we are able to offer for sale in the middle price points within the markets where we operate, avoiding the very low-end and high-end products. We believe our middle market strategy positions our products such that they are affordable to a significant segment of potential home buyers in our market.

Our apartment buildings are developed as rental properties to be held and operated for our own purposes, converted at some point to for-sale condominium units or sold on a merchant build basis. When developing rental communities, we design our products to be affordable for tenants that fit one of two groups; (i) young first time tenants; or (ii) renters by choice.

We believe that our significant experience over the past 27 years, combined with our ability to navigate through two major housing downturns (early 1990s and late 2000s) have provided us the experience necessary to capitalize on attractive opportunities in our core market of Washington, D.C. and to build shareholder value. We believe that our focus on the Washington, D.C. market, which has historically been characterized by economic conditions less volatile than many other major homebuilding markets, should provide an opportunity to generate attractive returns on investment and for growth.



**Table of Contents**

**Our Business Strategy**

Our business strategy is designed to leverage our extensive capabilities and market knowledge to maximize returns on invested capital on our various real estate related activities. We execute our strategy through three related business segments:

*Homebuilding* We target new home building opportunities where our building experience and ability to manage highly complex entitlement, development and related issues provides us with a competitive advantage.

*Apartments* We seek opportunities in the multi-family rental market where our experience and core capabilities can be leveraged. We will either position the assets for sale to institutional buyers when completed or operate the asset within our own portfolio. Operating the asset for our own account affords us the flexibility of converting the units to condominiums in the future.

*Real Estate Services* Our management team has significant experience in all aspects of real estate management, including strategic planning, land development, entitlement, property management, sales and marketing, workout and turnaround strategies, financing and general construction. We are able to provide a wide range of construction management, general contracting and real estate related services to other property owners. This business line not only allows us to generate positive fee income from our highly qualified personnel but also serves as a potential catalyst for joint venture and acquisition opportunities.

These business units work in concert to leverage the collective skill sets of our organization. The talent and experience of our personnel allows workflow flexibility and a multitasking approach to managing various projects. In a capital constrained environment, we use creative problem solving and financing approaches by working closely with banks, borrowers and other parties in an effort to generate value for all constituents. We believe that our business network within the Washington, D.C. real estate market provides us a competitive advantage in sourcing and executing investment opportunities.

With respect to our homebuilding operations, we seek to minimize risk associated with fluctuating market conditions by primarily building pre-sold units and limiting the number of spec units (units that are not pre-sold) held in inventory. In each new community that we develop we build model homes to demonstrate our products and to house our on-site sales operations. We limit the building of spec units to locations where there is a demonstrated demand for immediate delivery homes or where the majority of the units within a multi-family building (such as townhouses or condominiums) have been pre-sold. We believe that by limiting the number of spec units held in inventory we reduce our exposure to cyclical fluctuations in market values and minimize costs associated with holding inventory, such as debt service.

**Our Operations**

We believe that we are properly staffed for current market conditions and that we have the ability to manage growth as market conditions warrant. Our operations are focused on the Washington, D.C. market, where we believe our 27 years of market experience provides us the best opportunity to enhance shareholder value.

**Our Communities**

We are currently operating, or developing in the following counties in Virginia: Loudoun, Prince William, Arlington, and Fairfax. We also have communities in the Maryland counties of Frederick and Montgomery and the District of Columbia. The following table summarizes certain information regarding our communities as of December 31, 2012:

As of December 31, 2012 (dollars in thousands)								Average New Order Revenue to Date
Project	State	Product Type (2)	Estimated Units at Completion	Units Settled	Backlog (3)	Lots Owned Unsold		
Eclipse on Center Park (1)	VA	Condo	465	446	3		\$	413

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Penderbrook Square (1)	VA	Condo	424	422	1	\$	240
Emerald Farm (4)	MD	SF	84	78		\$	452
The Hampshires (5)	DC	SF/TH	111		5	\$	
Villas at Eastgate (5)	VA	Condo	66			\$	
Falls Grove (5)	VA	Condo	129			\$	
Residences at Shady Grove/BLVD Shady Grove (5)	MD	SF/TH/APT	156			\$	
BLVD Newell (5)	MD	Apartment	187			\$	
<b>Total</b>							

- (1) For sale communities.
- (2) SF means single family home, TH means town home and Condo means condominium.
- (3) Backlog means we have an executed order with a buyer, but the settlement has not yet taken place.
- (4) Developed and available for sale.
- (5) Community under our control currently in development.



## **Table of Contents**

### ***Northern Virginia Market***

*The Eclipse on Center Park* is a 465-unit, high-rise condominium complex in Arlington, Virginia. The project is just minutes from downtown Washington D.C., the Pentagon and Reagan National Airport. The project is an upscale, urban-style, mixed-use complex with residential condominiums above an 83,000 square foot retail center, which includes a Harris Teeter grocery store and other convenience-oriented retailers. Condominium sales began in the second quarter of 2004 and settlements began in November 2006. At December 31, 2012, 19 units remain in our inventory.

*Penderbrook Square* is a 424-unit rental apartment complex in the Fair Oaks area of Fairfax County, Virginia that we purchased as a condominium conversion project. We acquired the property in 2005 and made significant improvements to common areas, building exteriors, and heating and air-conditioning systems within units and have completed the conversion and sale of a majority of the units to condominiums. Sales and settlements began in 2005. At December 31, 2012, two units remained in our inventory. The Company exited this project in January 2013 with the settlement of the two remaining units.

*Falls Grove* is a new community located in northern Prince William County near Centreville, Virginia. The property will be developed as 19 single family homes and 110 townhouses with prices expected to be starting from \$200 s for the townhomes and \$400 s for the single-family homes. The Company anticipates development to commence in the first half of 2013, and unit sales to commence in the second half of 2013.

*Villas at Eastgate* is a new community located in Loudoun County near Chantilly, Virginia. The project consists of 66 single-level condominiums in a cluster of two-level buildings, situated within the 400-unit Eastgate master-planned community. The construction of the first building, containing six units, two of which are model homes, commenced in December 2012, with sales commencing in the first quarter of 2013. Initial unit pricing is expected to start in the \$300 s.

### ***Maryland***

*Emerald Farm* is an 84-unit development of single-family homes in Frederick, Maryland conveniently located near major transportation routes. It is our intention to pursue construction financing for homes on the six remaining finished building lots in the near future and as market conditions warrant.

*BLVD Newell* is a newly planned 187-unit apartment community located proximate to the metro rail station in downtown Silver Spring, MD. The Company has initiated the process of securing rezoning and land development permits. Securing the rezoning and land development permits requires local government approval from the County within which the property resides. There can be no assurances made regarding the Company's ability to secure the rezoning and land development permits necessary for its intended use of the property.

*Residences at Shady Grove/BLVD Shady Grove* is a new residential project in Rockville, Maryland, immediately adjacent to the Shady Grove metro station, the terminus of DC's Red Line. The project will be developed as 3 single family homes, 36 upscale townhomes and 117 luxury apartments. The Company acquired the subject land on December 27, 2012, and land development is expected to start in spring 2013. Sale of homes will begin in mid-2013 with first delivery expected late 2013. Leasing of the apartments will commence in 2014.

### ***District of Columbia***

*The Hampshires* is a new community located within the Lamond-Riggs neighborhood in the Northeast quadrant of Washington, D.C. The property will be developed as 111 residential units, consisting of 38 single-family homes and 73 townhomes. The Hampshires is located proximate to two metro rail stations just inside the Washington, D.C. Maryland border. The first, of two, single-family model home sales offices was completed and opened in August 2012, with the second opening in December 2012. Sales began in August 2012, and there are five single-family units in backlog at December 31, 2012. The Company anticipates settlements to commence in the first quarter of 2013.

### **Construction**

Our home designs are selected or prepared in each of our communities to appeal to the tastes and preferences of local homebuyers. We also offer optional interior and exterior features to allow homebuyers to enhance the basic home design and to allow us to generate additional revenues from each home sold.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Substantially all of our construction work is performed by subcontractors. Subcontractors typically are selected after a competitive bidding process and retained for a specific subdivision pursuant to a contract that obligates the subcontractor to complete construction at an agreed-upon price. Agreements with the subcontractors and suppliers generally are negotiated for each subdivision. We compete with other homebuilders for qualified subcontractors, raw materials and lots in the markets where we operate. We employ construction superintendents to monitor homes under construction, participate in major design and building decisions, coordinate the activities of subcontractors and suppliers, review the work of subcontractors for quality and cost control and monitor compliance with zoning and building codes. In addition, our construction superintendents play a significant role in working with our homebuyers by assisting with option selection and home modification decisions, educating buyers on the construction process and instructing buyers on post-closing home maintenance.

Construction time for our homes depends on the weather, availability of labor, materials and supplies, size of the home, and other factors. We typically complete the construction of a home within three to six months.

## **Table of Contents**

We typically do not maintain significant inventories of construction materials, except for work in progress materials for homes under construction. Generally, the construction materials used in our operations are readily available from numerous sources. In recent years, we have not experienced delays in construction due to shortages of materials or labor that have materially affected our consolidated operating results.

### **Warranty**

We provide our single-family and townhouse home buyers with a one-year limited warranty covering workmanship and materials. The limited warranty is transferable to subsequent buyers not under direct contract with us and requires that all home buyers agree to the definitions and procedures set forth in the warranty. Typically, we provide our condominium home buyers with a two-year limited warranty, or as required by statute. In addition, we periodically provide structural warranty of longer durations pursuant to applicable statutory requirements. From time to time, we assess the appropriateness of our warranty reserves and adjust accruals as necessary. When deemed appropriate by us, we will accrue additional warranty reserves. We require our general contractors and sub-contractors to warrant the work they perform and they are contractually obligated to correct defects in their work that arise during the applicable warranty period. We seek to minimize our risk associated with warranty repairs through our quality assurance program and by selecting contractors with good reputations, sufficient resources and adequate insurance. It is typical that there is a gap in the warranty coverage provided by contractors and by home builders, which we have self-insured in the past. It is our experience that the warranty claims which we self insured have not been significant in nature but we periodically obtain additional insurance to protect against this unquantifiable risk.

### **Competition**

The real estate development industry is highly competitive. We compete primarily on the basis of price, location, design, quality, service and reputation. We compete with small private builders and large regional or national builders. In addition to competing for home buyers and renters, builders compete for construction financing, raw materials and skilled labor. Additionally, under normal market conditions competition exists within the industry for prime development sites, especially those where developed building lots are available under option lot contracts. We compete with other local, regional and national builders in all of these areas. Many of our competitors have significantly greater financial, marketing, sales and other resources than we have. Some of the national builders against which we compete include Pulte Homes, DR Horton, Toll Brothers, Ryland Homes, NVR, K. Hovnanian and Lennar.

Competition among home builders and apartment developers is often specific to product types being offered in a particular area. Often we do not find ourselves competing with the large national developers in the urban communities where we develop high-rise and mixed use products. This is primarily because most national builders tend to focus on a narrower range of products than what we offer. We believe this provides us a distinct advantage in terms of attracting potential home buyers and renters in certain areas. We believe the factors that home buyers consider in deciding whether to purchase or rent from us include the product type, location, value quality, and reputation of the developer. We believe that our projects and product offerings compare favorably on these factors and we continually strive to maintain our reputation of building quality products.

Additionally, we compete with the resale market of existing homes including foreclosures and short-sales. The dramatic increase of inventory of existing homes available for sale beginning in 2006 created significant competition among builders and home sellers for a shrinking number of prospective home buyers. This led to downward pressure on home prices in many areas that still persist in many markets. However, for the twelve months ended December 31, 2012, modest improvement in the economy and moderate change in buyer's perceptions appear to be stabilizing home prices and accordingly reducing sales incentives.

### **Regulation**

We are subject to various local, state and federal statutes, ordinances, rules and regulations concerning zoning, building design, construction and similar matters, including local regulation, which imposes restrictive zoning and density requirements in order to limit the number of residential units that can ultimately be built within the boundaries of a particular project. We and our competitors may also be subject to periodic delays or may be precluded entirely from developing in certain communities due to building moratoriums or slow-growth or no-growth initiatives that could be implemented in the future in the states in which we operate. Local and state governments also have broad discretion regarding the imposition of development fees for projects in their jurisdiction.

At December 31, 2012, the Company has initiated the process of securing rezoning and land development permits related to the BLVD Newell project. Securing the rezoning and land development permits requires local government approval from the County within which the property resides. There can be no assurances made regarding the Company's ability to secure the rezoning and land development permits necessary for its intended use of the property.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

We and our competitors are also subject to a variety of local, state and federal statutes, ordinances, rules and regulations concerning protection of the environment. Some of the laws to which we and our properties are subject may impose requirements concerning development in waters of the United States, including wetlands, the closure of water supply wells, management of asbestos-containing materials, exposure to radon and similar issues. The particular environmental laws that apply to any given community vary based on several factors including but not limited to the environmental conditions related to a particular property and the present and former uses of the property. These environmental laws may result in delays, may cause us and our competitors to incur substantial compliance related costs, and may prohibit or severely restrict development in certain environmentally sensitive areas. To date, environmental laws have not had a material adverse impact on our operations.

## Table of Contents

### **Technology and Intellectual Property**

We are committed to the use of Internet-based technology for managing our business, communicating with our customers, and marketing our projects. For customer relationship management, we use Builder's Co-Pilot, a management information system that was custom developed in accordance with our needs and requirements. This system allows for online and collaborative efforts between our sales and marketing functions and integrates our sales, production and divisional office operations in tracking the progress of construction on each of our projects. We believe that real-time access to our construction progress information and our sales and marketing data and documents through our systems increases the effectiveness of our sales and marketing efforts as well as management's ability to monitor our business.

We utilize our technology infrastructure to facilitate marketing of our projects as well. Through our web site, [www.comstockhomebuilding.com](http://www.comstockhomebuilding.com), our customers and prospective customers receive automatic electronic communications from us on a regular basis. Our corporate marketing directors work with in-house marketing and technology specialists to develop advertising and public relations programs for each project that leverage our technology capabilities. During 2012, we continued to increase our utilization of internet based marketing platforms in lieu of print advertisements. We believe that the home buying population will continue to increase its reliance on information available on the internet to help guide their home buying decision. Accordingly, our marketing efforts will continue to seek to leverage this trend in an effort to lower per sale marketing costs while maximizing potential sales.

For accounting and purchasing management purposes we use the JD Edwards Enterprise One software system.

Our Chief Executive Officer and Chairman of the Board, Christopher Clemente, has licensed his ownership interest in the Comstock brand and trademark to us in perpetuity and free of charge. We do not own the brand or the trademark and are not in a position to be able to adequately protect it against infringement from third parties. Additionally, Mr. Clemente has retained the right to continue using the Comstock brand and trademark individually and through his affiliates, including real estate development projects in our current or future markets that are unrelated to the Company.

### **Employees**

At December 31, 2012, we had 37 full-time and 1 part time employees. Our employees are not represented by any collective bargaining agreement and we have never experienced a work stoppage. We believe we have good relations with our employees.

### **Executive Officers of the Registrant**

Our executive officers and other management employees and their respective ages and positions as of December 31, 2012 are as follows:

<b>Name</b>	<b>Age</b>	<b>Current Position</b>
Christopher Clemente	53	Chairman and Chief Executive Officer
Gregory V. Benson	58	President, Chief Operating Officer
Joseph M. Squeri	47	Chief Financial Officer
Jubal R. Thompson	43	General Counsel and Secretary

*Christopher Clemente* founded Comstock in 1985 and has been a director since May 2004. Since 1992, Mr. Clemente has served as our Chairman and Chief Executive Officer. Mr. Clemente has over 25 years of experience in all aspects of real estate development and home building, and more than 30 years of experience as an entrepreneur.

*Gregory V. Benson* joined us in 1991 as President and Chief Operating Officer and has been a director since May 2004. Mr. Benson is also a member of our board of directors. Mr. Benson has over 30 years of home building experience including over 14 years at national home builders, including NVHomes, Ryan Homes and Centex Homes.

*Joseph M. Squeri* has served as our Chief Financial Officer since August 2010. Mr. Squeri has more than a decade of public company leadership experience in corporate finance, strategic planning, accounting and operations. From October 2008 to August 2010, Mr. Squeri served as an independent financial and business consultant to privately held companies. From January 2008 to September 2008, Mr. Squeri served as the Executive Vice President-Chief Financial Officer and Treasurer of the Federal Realty Investment Trust (NYSE: FRT) with responsibility for capital markets, financial reporting and investor relations functions. From 1997 through 2007, Mr. Squeri served in a variety of positions at Choice Hotels International (NYSE: CHH), including chief financial officer starting in 1999, and then more significant operating roles culminating his position as president and chief operating officer. Mr. Squeri is a certified public accountant.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

*Jubal R. Thompson* has served as our General Counsel since October 1998 and our Secretary since December 2004. Mr. Thompson has significant experience in areas of real estate acquisitions and dispositions, real estate and corporate finance, corporate governance, mergers and acquisition and risk management.

---

## **Table of Contents**

### **Item 1A. Risk Factors Risks Relating to Our Business**

We engage in construction and real estate activities, which involve a high degree of risk. Our business, financial condition, operating results and cash flows may be impacted by a number of factors. A discussion of the risks associated with these factors is included below.

*Our operations require significant capital and our continuing operations and future growth depends on the availability of construction, acquisition and development loans, which may not be available at the time it is needed or at favorable terms.*

The real estate development industry is capital intensive and requires significant expenditures for operations, land purchases, land development and construction as well as potential acquisitions of other homebuilders or developers. In order to maintain our operations, we will need to obtain additional financing. These funds can be generated through public or private debt or equity financings, operating cash flow, additional bank borrowings or from strategic alliances or joint ventures. In light of the current economic climate we may not be successful in obtaining additional funds in a timely manner, on favorable terms or at all. Moreover, certain of our bank financing agreements contain provisions that limit the type and amount of debt we may incur in the future without our lenders' consent. In addition, to finance projects, we have historically utilized construction, acquisition and development loans. These credit facilities tend to be project-oriented and generally have variable rates and require significant management time to administer. Further, this type of financing is typically characterized by short-term loans, which are subject to call. The availability of borrowed funds, especially for land acquisition and construction financing, has been greatly reduced, and lenders may require us to invest increased amounts of equity in a project in connection with both new loans and the extension of existing loans. Furthermore, if financial institutions discontinue providing these facilities to us, we would lose our primary source of financing our operations or the cost of retaining or replacing these credit facilities could increase dramatically. If we do not have access to additional capital or funds to continue our operations or grow our business, we may be required to delay, scale back or abandon some or all of our operating strategies or reduce capital expenditures and the size of our operations. As a result, such an inability to access additional capital would likely cause us to experience a material adverse effect on our business, results of operations and financial condition.

*Our ability to sell homes and, accordingly, our results of operations, will be affected by the availability of mortgage financing to potential home buyers.*

Most home buyers finance their purchase of a new home through third-party mortgage financing. As a result, residential real estate demand is adversely affected by increases in interest rates and decreases in the availability of consumer mortgage financing. Increased monthly mortgage costs and the unavailability of financing to potential home buyers have depressed the market for new homes. For instance, recent initiatives to tighten underwriting standards have made mortgage financing more difficult to obtain for some of our entry-level home buyers, which has led to decreased demand from these buyers. Even if potential home buyers do not experience difficulty securing mortgage financing for their purchase of a new home, increases in interest rates and decreased mortgage availability or significant alterations to mortgage product types could make it harder for them to sell their existing homes. This could continue to adversely affect our operating results and financial condition.

*Fluctuations in market conditions may affect our ability to sell our land and home inventories at expected prices, if at all, which could adversely affect our revenues, earnings and cash flows.*

We are subject to the potential for significant fluctuations in the market value of our land and home inventories. We must constantly locate and acquire new tracts of undeveloped and developed land if we are to support growth in our home building operations. There is a lag between the time we acquire control of undeveloped land or developed home sites and the time that we can bring communities built on that land to market. This lag time varies from site to site as it is impossible to predict with any certainty the length of time it will take to obtain governmental approvals and building permits. The risk of owning undeveloped land, developed land and homes can be substantial. The market value of undeveloped land, buildable lots and housing inventories can fluctuate significantly as a result of changing economic and market conditions. Inventory carrying costs can be significant and can result in losses in a poorly performing development or market. Material write-downs of the estimated value of our land and home inventories could occur if market conditions deteriorate or if we purchase land or build home inventories at higher prices during stronger economic periods and the value of those land or home inventories subsequently declines during weaker economic periods. We could also be forced to sell homes, land or lots for prices that generate lower profit than we anticipated, or at a loss, and may not be able to dispose of an investment in a timely manner when we find dispositions advantageous or necessary. Furthermore, a continued decline in the market value of our land or home inventories may give rise to additional impairments of our inventory and write-offs of contract deposits and feasibility cost, which may result in a breach of financial covenants contained in one or more of our credit facilities, which could cause a default under those credit facilities. Defaults in these credit facilities are often times the responsibility of Comstock, as Comstock is the guarantor of most of its subsidiary's debts.

We evaluated all of our projects to determine if recorded carrying amounts were recoverable by evaluating discount rates, sales prices, absorption and our analysis of the best approach to marketing our projects for sale. This evaluation resulted in an aggregate 2012 impairment

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

charge of \$2.4 million. Impairment charges are recorded as a reduction in our capitalized costs. The impairment charge was calculated based on the estimated fair value less costs to sell under the Company's revised disposition strategy. See real estate held for development and sale Note 4 within the Notes to the Consolidated Financial Statements.



---

## **Table of Contents**

***Our ability to use our Net Operating Losses ( NOLs ) and, in certain circumstances, future built-in losses and depreciation deductions can be negatively affected if there is an ownership change as defined under Section 382 of the Internal Revenue Code.***

We currently have approximately \$116 million in federal and state NOLs with a potential value of up to approximately \$45 million in tax savings. These deferred tax assets are currently fully reserved. If unused, these NOLs will begin expiring in 2028. Under Internal Revenue Code Section 382 rules, if a change of ownership is triggered, our NOL asset and possibly certain other deferred tax assets may be impaired. We estimate that as of December 31, 2012, the cumulative shift in the Company's stock would not cause an inability to utilize any of our NOL asset.

The Company's ability to use its NOLs (and in certain circumstances, future built-in losses and depreciation deductions) can be negatively affected if there is an ownership change as defined under Section 382. In general, an ownership change occurs whenever there is a shift in ownership by more than 50 percentage points by one or more 5% shareholders over a specified time period (generally three years). Given Section 382's broad definition, an ownership change could be the unintended consequence of otherwise normal market trading in the Company's stock that is outside of the Company's control. In an effort to preserve the availability of these NOLs, Comstock adopted a Section 382 stockholder rights plan (the Rights Plan). The Rights Plan was adopted to reduce the likelihood of such an unintended ownership change and thus assist in preserving the value of these tax benefits. Similar plans have been adopted by a number of companies holding similar significant tax assets over the past several years. This plan was submitted to a vote of the Company's shareholders on June 17, 2011, and the plan was approved at that meeting.

***Home prices and sales activities in the Washington, D.C. geographic market have a large impact on our results of operations because we conduct substantially all of our business in this market.***

We currently develop and sell homes exclusively in the Washington, D.C. market; consequently home prices and sales activities in the Washington, D.C. geographic market have a large impact on our results of operations. Although demand in this area historically has been strong, the historical slowdown in residential real estate demand and reduced availability of consumer mortgage financing have reduced the likelihood of consumers seeking to purchase new homes, which has had and will likely continue to have a negative impact on the pace at which we receive orders for our new homes. As a result of the foregoing and general economic conditions, potential customers may be less willing or able to buy our homes, or we may take longer or incur more costs to build them. We may not be able to recapture increased costs by raising prices in many cases because of market conditions or because we fix our prices in advance of delivery by signing home sales contracts. We may be unable to change the mix of our homes or our offerings or the affordability of our homes to maintain our margins or satisfactorily address changing market conditions in other ways. Our limited geographic diversity means that adverse general economic, weather or other conditions in this market could adversely affect our results of operations and cash flows or our ability to grow our business.

***Because our business depends on the acquisition of new land, the potential limitations on the supply of land could reduce our revenues or negatively impact our results of operations and financial condition.***

We experience competition for available land and developed home sites in the Washington, D.C. market. We have experienced competition for home sites from other, better capitalized, home builders. Our ability to continue our home building activities over the long term depends upon our ability to locate and acquire suitable parcels of land or developed home sites to support our home building operations. If competition for land increases, the cost of acquiring it may rise, and the availability of suitable parcels at acceptable prices may decline. Any need for increased pricing could increase the rate at which consumer demand for our homes declines and, consequently, reduce the number of homes we sell and lead to a decrease in our revenues, earnings and cash flows.

***Our business is subject to governmental regulations that may delay, increase the cost of, prohibit or severely restrict our development and home building projects and reduce our revenues and cash flows.***

We are subject to extensive and complex laws and regulations that affect the land development and home building process, including laws and regulations related to zoning, permitted land uses, levels of density (number of dwelling units per acre), building design, access to water and other utilities, water and waste disposal and use of open spaces. In addition, we and our subcontractors are subject to laws and regulations relating to worker health and safety. We also are subject to a variety of local, state and federal laws and regulations concerning the protection of health and the environment. In some of our markets, we are required to pay environmental impact fees, use energy saving construction materials and give commitments to provide certain infrastructure such as roads and sewage systems. We are also subject to real estate taxes and other local government fees on real estate purchases. We must also obtain permits and approvals from local authorities to complete residential development or home construction. The laws and regulations under which we and our subcontractors operate, and our and their obligations to comply with them, may result in delays in construction and development, cause us to incur substantial compliance and other increased costs, and prohibit or severely restrict development and home building activity in certain areas in which we operate. If we are unable to continue to develop communities and build and deliver homes as a result of these restrictions or if our compliance costs increase substantially, our revenues, earnings and cash flows may be reduced.



## **Table of Contents**

***Cities and counties in which we operate have adopted, or may adopt, slow or no-growth initiatives that would reduce our ability to build and sell homes in these areas and could adversely affect our revenues, earnings and cash flows.***

From time to time, certain cities and counties in which we operate have approved, and others in which we operate may approve, various slow-growth or no-growth initiatives and other similar ballot measures. Such initiatives restrict development within localities by, for example, limiting the number of building permits available in a given year. Approval of slow- or no-growth measures could reduce our ability to acquire land, obtain building permits and build and sell homes in the affected markets and could create additional costs and administration requirements, which in turn could have an adverse effect on our revenues, earnings and cash flows.

Increased regulation in the housing industry increases the time required to obtain the necessary approvals to begin construction and has prolonged the time between the initial acquisition of land or land options and the commencement and completion of construction. These delays increase our costs, decrease our profitability and increase the risks associated with the land inventories we maintain.

Municipalities may restrict or place moratoriums on the availability of utilities, such as water and sewer taps. If municipalities in which we operate take actions like these, it could have an adverse effect on our business by causing delays, increasing our costs or limiting our ability to build in those municipalities. This, in turn, could reduce the number of homes we sell and decrease our revenues, earnings and cash flows.

***The competitive conditions in the home building industry could increase our costs, reduce our revenues and earnings and otherwise adversely affect our results of operations and cash flows.***

The home building industry is highly competitive and fragmented. We compete with a number of national, regional and local builders for customers, undeveloped land and home sites, raw materials and labor. For example, in the Washington, D.C. market, we compete against multiple publicly-traded national home builders, and many privately-owned regional and local home builders. We do not compete against all of the builders in all of our product types or submarkets, as some builders focus on particular types of projects within those markets, such as large estate homes, that are not in competition with our projects.

We compete primarily on the basis of price, location, design, quality, service and reputation. Some of our competitors have greater financial resources, more established market positions and better opportunities for land and home site acquisitions than we do and have greater amounts of unrestricted cash resources on hand, lower costs of capital, labor and material than us. The competitive conditions in the home building industry could, among other things:

make it difficult for us to acquire suitable land or home sites in desirable locations at acceptable prices and terms, which could adversely affect our ability to build homes;

require us to increase selling commissions and other incentives, which could reduce our profit margins;

result in delays in construction if we experience delays in procuring materials or hiring trades people or laborers;

result in lower sales volume and revenues; and

increase our costs and reduce our earnings.

We also compete with sales of existing homes and condominiums, foreclosure sales of existing homes and condominiums and available rental housing. A continued oversupply of competitively priced resale, foreclosure or rental homes in our markets could adversely affect our ability to sell homes profitably.

***We are dependent on the services of certain key employees, and the loss of their services could harm our business.***

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Our success largely depends on the continuing services of certain key employees, including Christopher Clemente, our Chairman and Chief Executive Officer; Gregory Benson, our Chief Operating Officer; Jubal Thompson, our General Counsel and Secretary; and Joseph Squeri, our Chief Financial Officer. Our continued success also depends on our ability to attract and retain qualified personnel. We believe that Messrs. Clemente, Benson, Thompson and Squeri each possess valuable industry knowledge, experience and leadership abilities that would be difficult in the short term to replicate. The loss of these or other key employees could harm our operations, business plans and cash flows.

*A significant portion of our business plan involves and may continue to involve mixed-use developments and high-rise projects with which we have less experience.*

We are actively involved in the construction and development of mixed-use and high-rise residential projects. Our experience is largely based on smaller wood-framed structures that are less complex than high-rise construction or the development of mixed-use projects. A mixed-use project is one that integrates residential and non-residential uses in the same structure or in close proximity to each other, on the same land. As we continue to expand into these new product types, we expect to encounter operating, marketing, customer service, warranty and management challenges with which we have less familiarity. We had previously expanded our management team to include individuals with significant experience in this type of real estate development but then were forced to furlough some of them as we downsized our operation. If we are unable to successfully manage the challenges of this portion of our business, we may incur additional costs and our results of operations and cash flows could be adversely affected.

## **Table of Contents**

***If we experience shortages of labor or supplies or other circumstances beyond our control, there could be delays or increased costs in developing our projects, which would adversely affect our operating results and cash flows.***

We, from time to time, may be affected by circumstances beyond our control, including:

work stoppages, labor disputes and shortages of qualified trades people, such as carpenters, roofers, electricians and plumbers;

lack of availability of adequate utility infrastructure and services;

Increases in transportation cost for delivery of materials;

our need to rely on local subcontractors who may not be adequately capitalized or insured; and

shortages or fluctuations in prices of building materials.

These difficulties have caused and likely will cause unexpected construction delays and short-term increases in construction costs. In an attempt to protect the margins on our projects, we often purchase certain building materials with commitments that lock in the prices of these materials for 90 to 120 days or more. However, once the supply of building materials subject to these commitments is exhausted, we are again subject to market fluctuations and shortages. We may not be able to recover unexpected increases in construction or materials costs by raising our home prices because, typically, the price of each home is established at the time a customer executes a home sale contract. Furthermore, sustained increases in construction costs may, over time, erode our profit margins and may adversely affect our results of operations and cash flows.

***We depend on the availability and skill of subcontractors and their willingness to work with us.***

Substantially all of our construction work is done by subcontractors with us acting as the general contractor or by subcontractors working for a general contractor we select for a particular project. Accordingly, the timing and quality of our construction depends on the availability and skill of those subcontractors. We do not have long-term contractual commitments with subcontractors or suppliers. Although we believe that our relationships with our suppliers and subcontractors are good, we cannot assure that skilled subcontractors will continue to be available at reasonable rates and in the areas in which we conduct our operations. The inability to contract with skilled subcontractors or general contractors at reasonable costs on a timely basis could limit our ability to build and deliver homes and could erode our profit margins and adversely affect our results of operations and cash flows. Recent cash flow and credit facility limitations have forced us to negotiate settlements with our vendors at less than the entire amounts owed. This may result in vendor hesitation to work with us on future projects.

***Construction defect and product liability litigation and claims that arise in the ordinary course of business may be costly or negatively impact sales, which could adversely affect our results of operations and cash flows.***

Our home building business is subject to construction defect and product liability claims arising in the ordinary course of business. These claims are common in the home building industry and can be costly. Among the claims for which developers and builders have financial exposure are property damage, environmental claims and bodily injury claims and latent defects that may not materialize for an extended period of time. Damages awarded under these suits may include the costs of remediation, loss of property and health-related bodily injury. In response to increased litigation, insurance underwriters have attempted to limit their risk by excluding coverage for certain claims associated with environmental conditions, pollution and product and workmanship defects. As a developer and a home builder, we may be at risk of loss for mold-related property, bodily injury and other claims in amounts that exceed available limits on our comprehensive general liability policies and those of our subcontractors. In addition, the costs of insuring against construction defect and product liability claims are high and the amount of coverage offered by insurance companies is limited. Uninsured construction defect, product liability and similar claims, claims in excess of the limits under our insurance policies, defense costs and the costs of obtaining insurance to cover such claims could have a material adverse effect on our revenues, earnings and cash flows.

***Increased insurance risk could negatively affect our business, results of operations and cash flows.***

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Insurance and surety companies have reassessed many aspects of their business and, as a result, may take actions that could negatively affect our business. These actions could include increasing insurance premiums, requiring higher self-insured retentions and deductibles, requiring additional collateral on surety bonds, reducing limits, restricting coverages, imposing exclusions, and refusing to underwrite certain risks and classes of business. Any of these actions may adversely affect our ability to obtain appropriate insurance coverage at reasonable costs, which could have a material adverse effect on our business. Additionally, coverage for certain types of claims, such as claims relating to mold, is generally unavailable. Further, we rely on surety bonds, typically provided by insurance companies, as a means of limiting the amount of capital utilized in connection with the public improvement sureties that we are required to post with governmental authorities in connection with land development and construction activities. The cost of obtaining these surety bonds is, from time to time, unpredictable and these surety bonds may be unavailable to us for new projects. These factors can delay or prohibit commencement of development projects and adversely affect revenue, earnings and cash flows.

## **Table of Contents**

### ***We are subject to warranty claims arising in the ordinary course of business that could be costly.***

We provide service warranties on our homes for a period of one year or more post closing and provide warranties on occasion as required by applicable statutory requirements for extended periods. We self-insure our warranties from time to time and reserve an amount we believe will be sufficient to satisfy any warranty claims on homes we sell and periodically purchase insurance related coverage to cover the costs associated with potential claims. Additionally, we also attempt to pass much of the risk associated with potential defects in materials and workmanship on to the subcontractors performing the work and the suppliers and manufacturers of the materials and their insurance carriers. In such cases, we still may incur unanticipated costs if a subcontractor, supplier, manufacturer or its insurance carrier fails to honor its obligations regarding the work or materials it supplies to our projects. If the amount of actual claims materially exceeds our aggregate warranty reserves, any available insurance coverage and/or the amounts we can recover from our subcontractors and suppliers, our operating results and cash flows would be adversely affected.

### ***Our business, results of operations and financial condition may be affected by adverse weather conditions or natural disasters.***

Adverse weather conditions, such as extended periods of rain, snow or cold temperatures, and natural disasters, such as hurricanes, tornadoes, floods and fires, can delay completion and sale of homes, damage partially complete or other unsold homes in our inventory and/or decrease the demand for homes or increase the cost of building homes. To the extent that natural disasters or adverse weather events occur, our business and results may be adversely affected. To the extent our insurance is not adequate to cover business interruption losses or repair costs resulting from these events, our results of operations and financial conditions may be adversely affected.

### ***We are subject to certain environmental laws and the cost of compliance could adversely affect our business, results of operations and cash flows.***

As a current or previous owner or operator of real property, we may be liable under federal, state, and local environmental laws, ordinances and regulations for the costs of removal or remediation of hazardous or toxic substances on, under or in the properties or in the proximity of the properties we develop. These laws often impose liability whether or not we knew of, or were responsible for, the presence of such hazardous or toxic substances. The cost of investigating, remediating or removing such hazardous or toxic substances may be substantial. The presence of any such substance, or the failure promptly to remediate any such substance, may adversely affect our ability to sell the property, to use the property for our intended purpose, or to borrow funds using the property as collateral. In addition, the construction process involves the use of hazardous and toxic materials. We could be held liable under environmental laws for the costs of removal or remediation of such materials. In addition, our existing credit facilities also restrict our access to the loan proceeds if the properties that are used to collateralize the loans are contaminated by hazardous substances and require us to indemnify the bank against losses resulting from such occurrence for significant periods of time, even after the loan is fully repaid.

Our Eclipse project is part of a larger development located at Potomac Yard in Northern Virginia. Potomac Yard was formerly part of a railroad switching yard contaminated as a result of rail-related activities. Remediation of the property was conducted under supervision of the U.S. Environmental Protection Agency, or EPA, in coordination with state and local authorities. In 1998, federal, state and local government agencies authorized redevelopment of the property. Our development at the project was consistent with those authorizations. Although concentrations of contaminants remain on the property under the EPA-approved remediation work plan, the EPA has determined that they do not present an unacceptable risk to human health or the environment. However, the EPA's determination does not preclude private lawsuits and it is possible that we could incur costs to defend against any claims that may be brought in the future relating to any such contaminants.

### ***If we are not able to develop our communities successfully, results of operations and financial condition could be adversely impacted.***

Before a community generates any revenues, material expenditures are required to acquire land, to obtain development approvals and to construct significant portions of project infrastructure, amenities, model homes and sales facilities. It can take a year or more for a community development to achieve cumulative positive cash flow. Our inability to develop and market our communities successfully and to generate positive cash flows from these operations in a timely manner would have a material adverse effect on our ability to service our debt and to meet our working capital requirements.

### ***Our operating results, including revenue and net income, have varied over time due to a number of conditions. If we are unable to successfully manage these conditions or factors, our operating results may continue to vary and may also suffer.***

The homebuilding industry is cyclical and we expect to experience variability in our revenues and net income. The volume of sales contracts and closings typically varies from month to month and from quarter to quarter depending on several factors, including the stages of development of our projects, the uncertain timing and cost of real estate closings, weather and other factors beyond our control. The homebuilding industry is

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

cyclical. In the early stages of a project's development, we incur significant start-up costs associated with, among other things, project design, land acquisition and development, construction and marketing expenses. Since revenues from sales of properties are generally recognized only upon the transfer of title at the closing of a sale, no revenue is recognized during the early stages of a project unless land parcels or residential home sites are sold to other developers. Periodic sales of properties may be insufficient to fund operating expenses. Further, if sales and other revenues are not adequate to cover operating expenses, we will be required to seek sources of additional operating funds. Accordingly, our financial results will vary from community to community and from time to time.



## **Table of Contents**

### ***Acts of war or terrorism may seriously harm our business.***

Acts of war, any outbreak or escalation of hostilities between the United States and any foreign power or acts of terrorism, may cause disruption to the U.S. economy, or the Washington, D.C. metro area, cause shortages of building materials, increase costs associated with obtaining building materials, result in building code changes that could increase costs of construction, affect job growth and consumer confidence, or cause economic changes that we cannot anticipate, all of which could reduce demand for our homes and adversely impact our revenues, earnings and cash flows.

### ***We do not own the Comstock brand or trademark, but use the brand and trademark pursuant to the terms of a perpetual license granted by Christopher Clemente, our Chief Executive Officer and Chairman of the Board.***

Our Chief Executive Officer and Chairman of the Board, Christopher Clemente, has licensed his ownership interest in the Comstock brand and trademark to us in perpetuity and free of charge. We do not own the brand or the trademark and are not in a position to be able to adequately protect it against infringement from third parties. Additionally, Mr. Clemente has retained the right to continue using the Comstock brand and trademark individually and through his affiliates, including real estate development projects in our current or future markets that are unrelated to the Company. We will be unable to control the quality of projects undertaken by Mr. Clemente or others using the Comstock brand and trademark and therefore will be unable to prevent any damage to its goodwill that may occur. We will further be unable to preclude Mr. Clemente from licensing or transferring the ownership of the Comstock trademark to third parties, some of whom may compete against us. Consequently, we are at risk that our brand could be damaged which could have a material adverse effect on our business, operations and cash flows.

### **Risks Related to our Common Stock and Level of Indebtedness**

#### ***Our level of indebtedness may harm our financial condition and results of operations.***

Our level of indebtedness will have several important effects on our future operations, including, without limitation:

A portion of our cash flows from operations will be dedicated to the payment of any interest or amortization required with respect to outstanding indebtedness;

Increases in our outstanding indebtedness and leverage will increase our vulnerability to adverse changes in general economic and industry conditions, as well as to competitive pressure; and

Depending on the levels of our outstanding debt, our ability to obtain additional financing for working capital, acquisitions, capital expenditures, general corporate and other purposes may be limited.

At the scheduled maturity of our credit facilities or in the event of an acceleration of a debt facility following an event of default, the entire outstanding principal amount of the indebtedness under the facility, together with all other amounts payable thereunder from time to time, will become due and payable. It is possible that we may not have sufficient funds to pay such obligations in full at maturity or upon such acceleration. If we default and are not able to pay any such obligations due, our lenders have liens on substantially all of our assets and could foreclose on our assets in order to satisfy our obligations.

#### ***Our stock has been volatile and we expect that it will continue to be volatile.***

Our stock price has been volatile, and we expect it will continue to be volatile. For example during the year ended December 31, 2012, the closing price of our common stock ranged from a high of \$1.94 to a low of \$1.10. The volatility of our stock price can be due to factors such as:

quarterly variations in our operating results;

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

general conditions in the home building industry;

interest rate changes;

changes in the market's expectations about our operating results;

our operating results failing to meet the expectation of securities analysts or investors in a particular period;

changes in financial estimates and recommendations by securities analysts concerning our Company or of the home building industry in general;

operating and stock price performance of other companies that investors deem comparable to us;

news reports relating to trends in our markets;

changes in laws and regulations affecting our business;

material announcements by us or our competitors;

material announcements by our construction lenders or the manufacturers and suppliers we use;

## **Table of Contents**

sales of substantial amounts of Class A common stock by our directors, executive officers or significant stockholders or the perception that such sales could occur; and

general economic and political conditions such as recessions and acts of war or terrorism.

Investors may not be able to resell their shares of our Class A common stock following periods of volatility because of the market's adverse reaction to that volatility. Our Class A common stock may not trade at the same levels as the stock of other homebuilders, and the market in general may not sustain its current prices.

***Investors in our Class A common stock may experience dilution with the future exercise of stock options and warrants, the grant of restricted stock and issuance of stock in connection with our acquisitions of other companies.***

From time to time, we have issued and we will continue to issue stock options or restricted stock grants to employees and non-employee directors pursuant to our equity incentive plan. We expect that these options or restricted stock grants will generally vest commencing one year from the date of grant and continue vesting over a four-year period. Investors may experience dilution as the options vest and are exercised by their holders and the restrictions lapse on the restricted stock grants. In addition, we may issue stock in connection with acquisitions of other companies, or warrants in connection with the settlement of obligations and or indebtedness with vendors and suppliers, which may result in investors experiencing dilution.

***Substantial sales of our Class A common stock, or the perception that such sales might occur, could depress the market price of our Class A common stock.***

A substantial amount of the shares of our Class A common stock are eligible for immediate resale in the public market. Any sales of substantial amounts of our Class A common stock in the public market, or the perception that such sales might occur, could depress the market price of our Class A common stock.

***The holders of our Class B common stocks exert control over us and thus limit the ability of other stockholders to influence corporate matters.***

Messrs. Clemente and Benson own 100% of our outstanding Class B common stock, which, together with their shares of Class A common stock, represent approximately 78% of the combined voting power of all classes of our voting stock as of March 27, 2013. As a result, Messrs. Clemente and Benson, acting together, have control over us, the election of our board of directors and our management and policies. Messrs. Clemente and Benson, acting together, also have control over all matters requiring stockholder approval, including the amendment of certain provisions of our certificate of incorporation and bylaws, the approval of any equity-based employee compensation plans and the approval of fundamental corporate transactions, including mergers. In light of this control, other companies could be discouraged from initiating a potential merger, takeover or any other transaction resulting in a change of control. Such a transaction potentially could be beneficial to our business or to our stockholders. This may in turn reduce the price that investors are willing to pay in the future for shares of our Class A common stock.

***The limited voting rights of our Class A common stock could impact its attractiveness to investors and its liquidity and, as a result, its market value.***

The holders of our Class A and Class B common stock generally have identical rights, except that holders of our Class A common stock are entitled to one vote per share and holders of our Class B common stock are entitled to 15 votes per share on all matters to be voted on by stockholders. The difference in the voting rights of the Class A and Class B common stock could diminish the value of the Class A common stock to the extent that investors or any potential future purchasers of our Class A common stock ascribe value to the superior voting rights of the Class B common stock.

***It may be difficult for a third party to acquire us, which could inhibit stockholders from realizing a premium on their stock price.***

We are subject to the Delaware anti-takeover laws regulating corporate takeovers. These anti-takeover laws prevent Delaware corporations from engaging in business combinations with any stockholder, including all affiliates and employees of a stockholder, who owns 15% or more of the corporation's outstanding voting stock, for three years following the date that the stockholder acquired 15% or more of the corporation's voting stock unless specified conditions are met.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Our amended and restated certificate of incorporation and bylaws contain provisions that have the effect of delaying, deferring or preventing a change in control that stockholders could consider favorable or beneficial. These provisions could discourage proxy contests and make it more difficult for stockholders to elect directors and take other corporate actions. These provisions could also limit the price that investors might be willing to pay in the future for shares of our common stock. These provisions include:

a staggered board of directors, so that it would take three successive annual meetings to replace all directors;

a prohibition of stockholder action by written consent; and

advance notice requirements for the submission by stockholders of nominations for election to the board of directors and for proposing matters that can be acted upon by stockholders at a meeting.

**Table of Contents*****Our issuance of shares of preferred stock could delay or prevent a change of control of us.***

Our Board of Directors has the authority to cause us to issue, without any further vote or action by the stockholders, up to 20,000,000 shares of preferred stock, par value \$0.01 per share, in one or more series, to designate the number of shares constituting any series, and to fix the rights, preferences, privileges and restrictions thereof, including dividend rights, voting rights, rights and terms of redemption, redemption price or prices and liquidation preferences of such series. The issuance of shares of preferred stock may have the effect of delaying, deferring or preventing a change in control of us without further action by the stockholders, even where stockholders are offered a premium for their shares. The issuance of shares of preferred stock with voting and conversion rights may adversely affect the voting power of the holders of Class A common stock, including the loss of voting control. We have no present plans to issue any shares of preferred stock.

**Item 1B. Unresolved Staff Comments**

Not applicable.

**Item 2. Properties**

On December 31, 2009, the Company, through an affiliate, Comstock Property Management, L.C., entered into a three-year lease for approximately 7,620 square feet of office space for its corporate headquarters at 1886 Metro Center Drive, Reston, Virginia from Comstock Asset Management, L.C., an affiliate wholly-owned by our Chief Executive Officer. On September 19, 2012, the Company amended the lease for an additional 2,436 square feet of office space, or a total 10,056 square feet, for its corporate headquarters, with an effective date of July 1, 2012. Refer to related party transactions Note 12 within the Notes to the Consolidated Financial Statements.

For information regarding the properties at our communities, please see Item 1 Business Our Communities.

**Item 3. Legal Proceedings**

Currently, we are not subject to any material legal proceedings. From time to time, however, we are named as a defendant in legal actions arising from our normal business activities. Although we cannot accurately predict the amount of our liability, if any, that could arise with respect to legal actions pending against us, we do not expect that any such liability will have a material adverse effect on our financial position, operating results or cash flows. We believe that we have obtained adequate insurance coverage, rights to indemnification, or where appropriate, have established reserves in connection with these legal proceedings.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities  
Market for Common Stock**

Our Class A common stock is traded on NASDAQ under the symbol CHCI. The following table sets forth the high and low sale prices of our Class A common stock, as reported on NASDAQ, for the periods indicated:

	High	Low
Fiscal Year Ended 2011		
First quarter	\$ 2.07	\$ 1.09
Second quarter	\$ 1.43	\$ 0.90

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Third quarter	\$ 1.59	\$ 0.86
Fourth quarter	\$ 1.22	\$ 0.91
Fiscal Year Ended 2012		
First quarter	\$ 2.03	\$ 1.08
Second quarter	\$ 1.82	\$ 1.13
Third quarter	\$ 1.53	\$ 1.10
Fourth quarter	\$ 1.59	\$ 1.15

### **Dividends**

We have never paid any cash dividends on our common stock and do not anticipate doing so in the foreseeable future.

### **Unregistered Sales of Equity Securities and Use of Proceeds**

None.

## **Table of Contents**

### **Issuer Purchases of Equity Securities**

Our board of directors has previously authorized the repurchase of up to 1.0 million shares of our Class A common stock in one or more open market or privately negotiated transactions. During the twelve months ended December 31, 2012, we did not repurchase any of our outstanding Class A common stock. As of December 31, 2012, 0.6 million shares of Class A common stock authorized for repurchase remain available for repurchase; however, we have no immediate plans to repurchase stock under this authorization. On December 31, 2012, there were approximately 37 record holders of our Class A common stock. On December 31, 2012 there were two holders of our Class B common stock.

### **Item 6. Selected Financial Data**

Not Applicable.

### **Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations**

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our consolidated financial statements and related notes appearing elsewhere in this report. This discussion and analysis contains forward-looking statements that involve risks and uncertainties. Please see *Cautionary Notes Regarding Forward-looking Statements* for more information. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of various factors including, but not limited to, those discussed below and elsewhere in this report, particularly under the headings *Risk Factors* and *Cautionary Notes Regarding Forward-looking Statements*.

#### **Overview**

We are a multi-faceted real estate development and services company. We have substantial experience with building a diverse range of products including apartments, single-family homes, townhouses, mid-rise condominiums, high-rise multi-family condominiums and mixed-use (residential and commercial) developments. We operate our business through three segments: Homebuilding, Apartment Buildings and Real Estate Services as further discussed in Note 2 of our consolidated financial statements. We are currently focused on the Washington, D.C. market, which is the eighth largest metropolitan statistical area in the United States.

#### *Homebuilding*

Our expertise in developing traditional and non-traditional housing products enables us to focus on a wide range of opportunities within our core market. For our homebuilding operations, we develop properties with the intent that they be sold either as fee-simple properties or condominiums to individual unit buyers or as investment properties sold to private or institutional investors. Our for-sale products are designed to attract first-time, early move-up, and secondary move-up buyers. We focus on products that we are able to offer for sale in the middle price points within the markets where we operate, avoiding the very low-end and high-end products. We believe our middle market strategy positions our products such that they are affordable to a significant segment of potential home buyers in our market.

#### *Apartment Buildings*

For Comstock's apartment sector, we develop projects ranging from approximately 75 to 200 units in locations that are supply constrained with demonstrated demand for stabilized assets. We seek opportunities in the multi-family rental market where our experience and core capabilities can be leveraged. We will either position the assets for sale when completed or operate the assets within our own portfolio. Operating the assets for our own account affords us the flexibility of converting the units to condominiums in the future. When developing rental communities, we design our products to be affordable for tenants that fit one of two groups: (i) young first-time renters or (ii) renters by choice.

#### *Real Estate Services*

Our management team has significant experience in all aspects of real estate management including strategic planning, land development, entitlement, property management, sales and marketing, workout and turnaround strategies, financing and general construction. We are able to provide a wide range of construction management, general contracting and other real estate related services to other property owners. This business line not only allows us to generate fee income from our highly qualified personnel but also serves as a potential catalyst for joint venture and acquisition opportunities.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

We believe that our significant experience over the past 27 years, combined with our ability to navigate through two major housing downturns (early 1990s and late 2000s), have provided us the experience necessary to capitalize on attractive opportunities in our core market of Washington, D.C. and to rebuild shareholder value. We believe that our focus on the Washington, D.C. market, which has historically been characterized by economic conditions less volatile than many other major homebuilding markets, should provide an opportunity to generate attractive returns on investment and for growth.



---

## **Table of Contents**

### **Recent Developments**

#### ***New Hampshire Ave. Ventures, LLC***

On August 23, 2012, the Company formed New Hampshire Ave. Ventures, LLC, a consolidated joint venture of its subsidiary Comstock Ventures XVI, L.C. and 6000 New Hampshire Avenue, LLC, to acquire, develop and construct 111 residential units, consisting of 38 single-family homes and 73 townhomes, in Washington, D.C. (the NHA Project ). The Company, through New Hampshire Ave. Ventures, LLC, entered into a \$3.0 million mezzanine loan (the NHA Mezzanine Loan ) in connection with the NHA Project with the Rosalie K. Stahl Trust, utilized to acquire the fully entitled land. Concurrent with the formation of the joint venture, the Company entered into a three-year loan agreement with Eagle Bank pursuant to which the Company secured a \$6.0 million revolving development loan and a \$4.0 million revolving construction loan (collectively, the Eagle NHA Revolver ) to finance the development and construction of the NHA Project. Refer to Note 9 within the Notes to the Consolidated Financial Statements for further discussion of the terms of these financing arrangements.

#### ***Comstock Eastgate, L.C.***

On September 27, 2012, the Company formed Comstock Eastgate, L.C., a consolidated joint venture of Comstock Holding Companies, Inc. and BridgeCom Development II, LLC, to acquire, develop and construct 66 residential condominium units in Loudoun County, VA (the Eastgate Project ). Concurrent with the formation of the joint venture, the Company entered into a loan agreement with Cardinal Bank to which the Company secured a \$2.5 million revolving construction loan to finance the construction of the units. Refer to Note 9 within the Notes to the Consolidated Financial Statements for further discussion of the terms of the financing arrangement.

#### ***Comstock Redland Road, L.C.***

On December 27, 2012, the Company formed Comstock Redland Road, L.C., a wholly owned subsidiary, to acquire, develop and construct 3 single-family moderately priced dwelling units, 36 townhome units and a 117-unit multi-family residential building. Concurrent with formation of the entity, the Company completed the acquisition through securing a \$2.5 million acquisition bridge loan with Eagle Bank and a \$5.75 million Deferred Purchase Money Promissory Note with TSR-Shady Grove, LLC, a Maryland limited liability Company. Refer to Note 9 within the Notes to the Consolidated Financial Statements for further discussion of the terms of these financing arrangements. Further, these financing arrangements were repaid in full on March 25, 2013 through new arrangements with Eagle Bank. Refer to Note 20 within the Notes to the Consolidated Financial Statement for further discussion of the terms of the new arrangement with Eagle Bank.

#### ***Comstock Investors VII, L.C.***

On March 14, 2013, Comstock Investors VII, L.C. ( Investors VII ), a subsidiary of the Company entered into subscription agreements (each a Subscription Agreement ) with certain accredited investors (the Purchasers, and each a Purchaser ), pursuant to which the Purchasers purchased membership interests ( Interests ) in Investors VII for an initial aggregate principal amount of \$6,925 of an up to \$7,000 capital raise (the Private Placement ). Purchasers included unrelated third-party accredited investors along with members of the Company's Board of Directors and the Chief Operating Officer, Chief Financial Officer and General Counsel of the Company. The Subscription Agreement provides that the Purchasers are entitled to a cumulative, compounded, preferred return of 20% per annum, compounded annually on their capital account balances. After six months, the Company has the right to repurchase the Interests of the Purchasers, provided that (i) all of the Purchasers Interests are acquired, (ii) the purchase is made in cash and (iii) the purchase price equals the Purchasers' capital account plus an amount necessary to cause the preferred return to equal a cumulative cash on cash return equal to 20% per annum. The Private Placement provides capital related to the current and planned construction of the Company's following projects: The Residences at Shady Grove in Rockville, Maryland consisting of 36 townhomes, The Hampshires project in Washington, D.C. consisting of 38 single family residences and 73 townhomes, and the Falls Grove project in Prince William County, Virginia consisting of 110 townhomes and 19 single family homes (collectively, the Projects ). Proceeds of the Private Placement are to be utilized (i) to provide capital needed to complete the Projects in conjunction with project financing for the Projects, (ii) to reimburse the Company for prior expenditures incurred on behalf of the Projects, and (iii) for general corporate purposes of the Company.

As part of the Private Placement, the Company also issued warrants to purchase shares of the Company's Class A Common Stock ( Class A Common stock ) ( Warrants, and each a Warrant ) to Purchasers who are not officers, directors or affiliates of the Company that purchased Interests that equaled or exceeded an initial investment amount of \$250. The Warrants represent the right to purchase up to 224 shares of Class A Common Stock, the maximum aggregate amount of warrants approved for issuance under the Private Placement. The Warrants have an initial exercise price which is equal to the average of the closing price of the Class A Common Stock of the 20 trading days preceding the issuance of the Warrant. The Warrants contain a cashless exercise provision. In the event the Purchasers exercise the Warrants on a cashless basis, the Company will not receive any proceeds. Warrants may be exercised at any time prior to March 14, 2023.

**Recent Accounting Pronouncements**

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standard ( IFRS ), which provides a consistent definition of fair value and ensures that the fair value measurement and disclosure requirements are similar between U.S. GAAP and IFRS. The guidance changes certain fair value measurement principles and expands the disclosure requirements, particularly for Level 3 fair value measurements. The guidance was effective for the Company beginning February 1, 2012 and is applied prospectively. The adoption of this guidance, which relates primarily to disclosure, did not have a material impact on our Consolidated Financial Statements.

## **Table of Contents**

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, Statement of Comprehensive Income (ASU2011-05), which requires entities to present net income and other comprehensive income in either a single continuous statement or in two separate, but consecutive, statements of net income and other comprehensive income. The guidance was effective for the Company beginning January 1, 2012 and is applied prospectively. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

### **Critical Accounting Policies and Estimates**

Our consolidated financial statements are prepared in accordance with U.S. GAAP, which require us to make certain estimates and judgments that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting periods. On an ongoing basis, we evaluate our estimates, including those related to the consolidation of variable interest entities, revenue recognition, impairment of real estate held for development and sale, warranty reserve and our environmental liability exposure. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. Actual results may differ materially from these estimates.

A summary of significant accounting policies is provided in Note 2 to our audited consolidated financial statements. The following section is a summary of certain aspects of those accounting policies that require our most difficult, subjective or complex judgments and estimates.

#### ***Real estate held for development and sale***

Real estate held for development and sale includes land, land development costs, construction and other costs. Real estate held for development and use is stated at cost, or when circumstances or events indicate that the real estate is impaired, at estimated fair value. Real estate held for sale is carried at the lower of cost or fair value less estimated costs to sell. Land, land development and indirect land development costs are accumulated by specific project and allocated to various units within that project using specific identification and allocation based upon the relative sales value, unit or area methods. Direct construction costs are assigned to units based on specific identification. Construction costs primarily include direct construction costs and capitalized field overhead. Other costs are comprised of fees, capitalized interest and real estate taxes. Costs incurred to sell real estate are capitalized to the extent they are reasonably expected to be recovered from the sale of the project and are tangible assets or services performed to obtain regulatory approval of sales. Other selling costs are expensed as incurred.

If the project is considered held for sale, it is valued at the lower of cost or fair value less estimated selling costs. For assets held for development and use, estimated fair value is based on comparable sales of real estate in the normal course of business under existing and anticipated market conditions. The evaluation takes into consideration the current status of the property, various restrictions, carrying costs, costs of disposition and any other circumstances that may affect fair value including management's plans for the property. A write-down to estimated fair value is recorded when the net carrying value of the property exceeds its estimated undiscounted future cash flows. These evaluations are made on a property-by-property basis whenever events or changes in circumstances indicate that the net book value may not be recoverable.

The Company has classified its Eclipse and Penderbrook projects as held for sale and accordingly, carries the projects at fair value less costs to sell as determined by discounted cash flow models, by reference to comparable market transactions, or relevant purchase offers. Discounted cash flow models are dependent upon several subjective factors, including estimated average sales prices, estimated sales pace, and the selection of an appropriate discount rate. The estimates of sales prices, sales pace and discount rates used by the Company are based on the best information available at the time the estimates are made.

In the third quarter of 2012, management evaluated its strategic alternatives with respect to its real estate projects classified as held for sale with the objective of creating additional near term liquidity. As a result, a decision was made to market the Potomac Yard project in a bulk sale transaction, rather than by selling directly to prospective home buyers, significantly accelerating absorption. The impairment charge of \$2,358 for the year ended December 31, 2012, reflects the write down to estimated fair value less costs to sell under the revised disposition strategy, however, there can be no assurance that the Company will be successful in the sale of the Potomac Yard project in a bulk sale and in the absence thereof, the Company will continue selling to prospective home buyers. There were no impairment charges recorded during the year ended December 31, 2011.

After impairments and write-offs, real estate held for development and sale consists of the following:

	<b>December 31, 2012</b>	<b>December 31, 2011</b>
Land and land development costs	\$ 19,378	\$ 4,693

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Cost of construction (including capitalized interest and real estate taxes)	8,403	16,519
	\$ 27,781	\$ 21,212

**Table of Contents****Warranty reserve**

Warranty reserves for units settled are established to cover potential costs for materials and labor with regard to warranty-type claims expected to arise during the typical one-year warranty period provided by the Company or within the two-year statutorily mandated structural warranty period for condominiums. Since the Company typically subcontracts its homebuilding work, subcontractors are required to provide the Company with an indemnity and a certificate of insurance prior to receiving payments for their work. Claims relating to workmanship and materials are generally the primary responsibility of the subcontractors and product manufacturers. The warranty reserve is established at the time of closing, and is calculated based upon historical warranty cost experience and current business factors. This reserve is an estimate and actual warranty costs could vary from these estimates. Variables used in the calculation of the reserve, as well as the adequacy of the reserve based on the number of homes still under warranty, are reviewed on a periodic basis. Warranty claims are directly charged to the reserve as they arise. The following table is a summary of warranty reserve activity which is included in accounts payable and accrued liabilities:

	<b>Years ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Balance at beginning period	\$ 1,009	\$ 1,110
Additions	52	110
Releases and/or charges incurred	(98)	(211)
Balance at end of period	\$ 963	\$ 1,009

**Revenue recognition**

We recognize revenues and related profits or losses from the sale of residential properties, including multiple units to the same buyer, finished lots and land sales when closing has occurred, full payment has been received, title and possession of the property has transferred to the buyer and we have no significant continuing involvement in the property. Other revenues include revenue from land sales, rental revenue from leased apartments, which is recognized over the terms of the respective leases, and revenue earned from management and administrative support services provided to related parties, which is recognized as the services are provided.

**Income taxes**

The effective tax rate for the years ended December 31, 2012 and 2011 was 0% and 3%, respectively. This resulted in zero and \$33 in tax expense for the twelve month periods ended December 31, 2012 and 2011, respectively.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company previously recorded valuation allowances for certain tax attributes and other deferred tax assets. At this time, sufficient uncertainty exists regarding the future realization of these deferred tax assets through future taxable income. In the future, if the Company believes that it is more likely than not that these deferred tax benefits will be realized, the valuation allowances will be reversed. With a full valuation allowance, any change in the deferred tax asset or liability is fully offset by a corresponding change in the valuation allowance.

The Company currently has approximately \$116 million in federal and state NOLs, which based on current statutory tax rates, has a potential fair value of approximately \$45 million in tax savings. If unused, these NOLs will begin expiring in 2028. Under Section 382 rules, if a change of ownership is triggered, the Company's NOL assets and possibly certain other deferred tax assets may be impaired. We estimate that as of December 31, 2012, the cumulative shift in ownership of the Company's stock would not cause an impairment of our NOL asset. However, if an ownership change were to occur, the Section 382 limitation would not be expected to materially impact the Company's financial position or results of operations as of December 31, 2012, because of the Company's full valuation allowance on its net deferred tax assets.

The Company's ability to use its NOLs (and in certain circumstances, future built-in losses and depreciation deductions) can be negatively affected if there is an ownership change as defined under Section 382. In general, an ownership change occurs whenever there is a shift in ownership by more than 50 percentage points by one or more 5% shareholders over a specified time period (generally three years). Given Section 382's broad definition, an ownership change could be the unintended consequence of otherwise normal market trading in the Company's stock that is outside of the Company's control. In an effort to preserve the availability of these NOLs, Comstock adopted a Section 382 stockholder rights plan (the Rights Plan). The Rights Plan was adopted to reduce the likelihood of such an unintended ownership change and

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

thus assist in preserving the value of these tax benefits. Similar plans have been adopted by a number of companies holding similar significant tax assets over the past several years. This plan was submitted to a vote of the Company's shareholders on June 17, 2011, and the plan was approved at that meeting.

The Company has not recorded any accruals for tax uncertainties as of December 31, 2012 and 2011, respectively. We file U.S. and state income tax returns in jurisdictions with varying statutes of limitations. The 2009 through 2011 tax years remain subject to examination by federal and most state tax authorities.

## **Table of Contents**

### *Use of estimates*

The preparation of the financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. Actual results could differ from those estimates. Material estimates are utilized in the valuation of real estate held for development and sale, valuation of deferred tax assets, capitalization of costs, consolidation of variable interest entities and warranty reserves.

### **Results of Operations**

#### *Year ended December 31, 2012 compared to year ended December 31, 2011*

##### *Orders, backlog and cancellations*

Gross new order revenue, revenue from all units sold, for the year ended December 31, 2012 increased \$4.4 million to \$18.9 million on 57 units, including condominium units, single-family units and townhome units, as compared to \$14.5 million on 50 units for the year ended December 31, 2011. Net new order revenue, revenue for all units sold less revenue from cancellations, for the year ended December 31, 2012 increased \$2.3 million to \$16.4 million on 51 units as compared to \$14.1 million on 48 units for the year ended December 31, 2011. The average gross new order revenue per unit for the year ended December 31, 2012 increased by \$42 to \$332, as compared to \$290 for the year ended December 31, 2011. Our backlog at December 31, 2012 increased \$4.8 million to \$5.4 million on 9 units as compared to our backlog at December 31, 2011 of \$0.6 million on 3 units.

We have four Washington, D.C. projects where we have units available for sale: Penderbrook Square in Fairfax, VA, the Eclipse at Potomac Yard in Arlington, VA, The Hampshires in Northeast, Washington D.C. and Eastgate in Chantilly, VA. As of December 31, 2012, there were 4 units in backlog for a total of \$1.8 million related to the Penderbrook and Eclipse projects. Because unit sales at these projects are generated from completed inventory, we do not need to construct units after a sales contract is executed with a unit purchaser. As a result, we are able to quickly execute on a sales contract and deliver the unit to the purchaser with deliveries typically made within thirty days of contract execution. The Hampshires project opened its first model home and began sales in August 2012 and at December 31, 2012, there were 5 units in backlog for a total of \$3.6 million. The first model is expected at Eastgate in the 1<sup>st</sup> quarter of 2013, with sales anticipated to begin concurrently with the opening. Unit sales at The Hampshires and Eastgate projects are generated from inventory that must be developed and constructed, thus the delivery of the units to the purchaser typically is made in 90 - 120 days from execution of the sales contract with the purchaser.

##### *Revenue homebuilding*

The number of units delivered for the year ended December 31, 2012 decreased by 3 to 45 as compared to 48 units for the year ended December 31, 2011. Average revenue per unit delivered decreased by approximately \$34 to \$259 for the year ended December 31, 2012 as compared to \$293 for the year ended December 31, 2011. Revenue from homebuilding decreased by \$2.5 million to \$11.6 million for the year ended December 31, 2012 as compared to \$14.1 million for the year ended December 31, 2011. For the year ended December 31, 2012, 37 units were settled at Penderbrook and 8 units at Eclipse, as compared to 29 units at Penderbrook and 17 units at Eclipse for the year ended December 31, 2011. The decrease in settlements and decrease in average sales price is largely a function of the available product mix at condominium projects. As of December 31, 2012, there are 19 units remaining in our Eclipse project and 2 units remaining in our Penderbrook project. This compares to 27 units and 39 units, respectively, for Eclipse and Penderbrook at December 31, 2011.

##### *Revenue other*

Revenue other decreased approximately \$5.2 million to \$2.7 million during the year ended December 31, 2012, as compared to \$7.9 million for the year ended December 31, 2011. These decreases are directly attributable to the completion of several general contracting projects in the latter quarters of 2011 and through 2012, as well as from the reduction in rental operations at the Penderbrook and Eclipse developments due to absorption of the units. The Company has encountered a slowdown in general contracting services, but it continues to pursue opportunities within the Real Estate Services segment as they become available.

Revenue other includes \$0.4 million and \$1.2 million of revenue generated by our rental communities during the twelve months ended December 31, 2012 and 2011, respectively. For the year ended December 31, 2012 and 2011, other revenue includes \$1.9 million and \$4.9 million, respectively, of related party real estate service revenue as further discussed in Note 12 to the consolidated financial statements.

We consider revenue to be from homebuilding when there is a structure built or being built on the lot when delivered. Sales of lots occur, and are included in other revenues, when we sell raw land or finished home sites in advance of any home construction.

*Cost of sales homebuilding*

Cost of sales homebuilding for the year ended December 31, 2012 decreased by \$2.5 million, to \$9.7 million as compared to \$12.2 million for the year ended December 31, 2011. The unit mix of homes settled during the year ended December 31, 2012 accounted for the decrease in the aggregate cost of sales figures. For the year ended December 31, 2012, gross margins increased to 16.4% on units settled as compared to 13.5% for the year ended December 31, 2011. The increase in margins is attributable to an increase in traffic and absorption at the two condominium projects resulting in a slight increase in pricing across those units. Further, this is a reflection of impairment charges recorded on the Eclipse project during the 3<sup>rd</sup> quarter of 2012.



---

## **Table of Contents**

### *Cost of sales other*

Cost of sales other decreased approximately \$3.9 million to \$3.5 million during the year ended December 31, 2012 as compared to \$7.4 million for the year ended December 31, 2011. Included in cost of sales other for the year ended December 31, 2012, costs and gross profits (losses) totaled \$1.6 million and \$(1.2) million, respectively, related to rental operations at Penderbrook and Eclipse. Included in cost of sales other for the year ended December 31, 2011, costs and gross profits (losses) totaled \$1.5 million and \$(0.3) million, respectively, related to the same rental operations. As a result of the continued absorption of the condominium units at Penderbrook and Eclipse, rental revenues have declined and the impact of fixed costs on gross profit has been more significant. The Company expects this trend to continue as the final units within the two condominium projects are absorbed.

Included in cost of sales other for the year ended December 31, 2012, were costs and gross profits that totaled \$1.9 million and \$0.4 million, respectively, related to our aforementioned general contracting projects. Included in cost of sales other for the year ended December 31, 2011, costs and gross profits that totaled \$5.9 million and \$0.7 million, respectively, related to the same general contracting business. These decreases in the year ended December 31, 2012 are directly related to the decrease in the number of ongoing general contracting projects. Consequently, the decline in revenues generated within the Real Estate Services segment and the impact relative to the fixed costs on gross profit has been more significant. The Company has one ongoing project and continues to pursue opportunities to expand the Real Estate Services segment.

### *Impairments and write-offs*

We recorded an impairment charge of \$2.4 million during the year ended December 31, 2012, to properly record our for sale project at fair market value less costs to sell consistent with the provisions of ASC 360. No impairment charges were recorded during the twelve months ended December 31, 2011. See real estate held for development and sale Note 4 within the Notes to the Consolidated Financial Statements for discussion and analysis.

We evaluated all of our projects to determine if recorded carrying amounts were recoverable by evaluating discount rates, sales prices, absorption and our analysis of the best approach to marketing our projects for sale. This evaluation resulted in an aggregate 2012 impairment charge of \$2.4 million. The impairment charge was realized related to the Company's revised disposition strategy. See real estate held for development and sale Note 4 within the Notes to the Consolidated Financial Statements.

### *Selling, general and administrative expenses*

Selling, general and administrative expenses for the year ended December 31, 2012 increased \$1.3 million to \$8.7 million, as compared to \$7.4 million for the year ended December 31, 2011. The increase in expenses for the twelve month periods ended in December 31, 2012, is primarily attributable to increases in audit and taxes fees of \$134, consulting expenses of \$385 and stock compensation of \$530.

### *Interest, real estate taxes and indirect costs related to inactive projects*

Interest and real estate taxes incurred relating to the development of lots and parcels are capitalized to real estate held for development and sale during the active development period, which generally commences when borrowings are used to acquire real estate assets and ends when the properties are substantially complete or the property becomes inactive which means that development and construction activities have been suspended indefinitely. Interest is capitalized based on the interest rate applicable to specific borrowings or the weighted average of the rates applicable to other borrowings during the period. Interest and real estate taxes capitalized to real estate held for development and sale are expensed as a component of cost of sales as related units are sold. Approximately, \$351 and \$320 of interest was capitalized to projects during the years ended December 31, 2012 and 2011, respectively.

When a project becomes inactive, its interest, real estate taxes and indirect overhead costs are no longer capitalized but rather expensed in the period in which they are incurred. During the year ended December 31, 2012 and 2011, several of our historical projects were determined to be inactive for accounting purposes. Refer to Note 2 to the Consolidated Financial Statements for the breakdown of the interest, real estate taxes and indirect costs related to inactive projects reported on the consolidated statement of operations.

### *Discontinued operations*

As described in Note 16 to the Consolidated Financial Statements, on March 7, 2012, the Company's subsidiary sold the Cascades Apartments for \$19.35 million. Because the sale of the Cascades Apartments represents a component of the Company, U.S. GAAP requires the results of operations associated with the Cascades Apartments to be included in Discontinued Operations. Accordingly, the net gain from the sale of the project of \$6.5 million is reflected within Discontinued Operations in the accompanying financial statements. Although the sale of the Cascades

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

project is presented in the accompanying financial statements under Discontinued Operations, developing apartments for the purpose of selling is a component of the Company's ongoing strategy and operating activities. The Company continues to pursue such projects within its Apartment Buildings segment and anticipates that sales of similar operating projects will be reflected in this manner.

### *Income taxes*

The effective tax rate for the years ended December 31, 2012 and 2011 was 0% and 3%, respectively. This resulted in zero and \$33 in tax expense for the twelve month periods ended December 31, 2012 and 2011, respectively.

**Table of Contents****Liquidity and Capital Resources**

We require capital to operate, to post deposits on new deals, to purchase and develop land, to construct homes, to fund related carrying costs and overhead and to fund various advertising and marketing programs to generate sales. These expenditures include payroll, community engineering, entitlement, architecture, advertising, utilities and interest as well as the construction costs of our homes. Our sources of capital include, and will continue to include, funds derived from various secured and unsecured borrowings to finance construction on acquired land, cash flow from operations, which includes the sale and delivery of constructed homes, rental apartment projects, finished and raw building lots and the sale of equity and debt securities.

The Company is involved in ongoing discussions with lenders in an effort to provide additional growth capital to fund various new business opportunities. In addition, on March 14, 2013, the Company, through its wholly-owned subsidiary Comstock Investors VII, L.C., entered into subscription agreements with certain accredited investors ( Comstock VII Investors ), pursuant to which the Comstock VII Investors purchased membership interests in the subsidiary for an initial aggregate principal amount of \$6,925, of an up to \$7,000 capital raise. Further, we have executed extensions and obtained new facilities to significantly reduce the debt obligations maturing in 2013. As of December 31, 2012, the maturities and curtailment obligations for 2013 was \$14,027, of which, the new facilities and extensions resulted in \$13,291 of the obligations with revised maturities beginning in 2015 and beyond. Refer to Note 20 for more details on the capital raise and changes to our credit facilities. We are anticipating that through a combination of the capital raised through the aforementioned private placement, current available cash on hand and additional cash from settlement proceeds at existing and under development communities, the Company will have sufficient financial resources to sustain our operations through the next 12 months, though no assurances can be made that we will be successful in our efforts.

**Credit Facilities**

We have outstanding borrowings with various financial institutions and other lenders that have been used to finance the acquisition, development and construction of real estate property.

As of December 31, 2012, maturities and/or curtailment obligations of all of our borrowings are as follows:

2013	\$ 14,027
2014	4,084
2015	6,422
2016	
2017 and thereafter	3,096
 Total	 \$ 27,629

As a result of debt extensions, repayments, and new facilities secured after December 31, 2012, as disclosed in Note 20 to the consolidated financial statements, we have significantly reduced the maturities and curtailment obligations for 2013. As of December 31, 2012, the maturities and curtailment obligations for 2013 was \$14,027, of which, the new facilities and extensions resulted in \$13,291 of the obligations with revised maturities beginning in 2015 and beyond.

The Company has generally financed its development and construction activities on a single or multiple project basis so it is not uncommon for each project or collection of projects the Company develops and builds to have a separate credit facility. Accordingly, the Company typically has had numerous credit facilities and lenders. As described in more detail below, at December 31, 2012 and 2011 our outstanding debt by lender was as follows:

	Balance as of 12/31/12	Balance as of 12/31/11	Recourse
<b>Bank</b>			
SunBridge, net of \$0.0 million and \$0.6 million discount, respectively	\$ 636	\$ 10,178	Secured
Cardinal Bank		9,957	Secured

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Bank of America		3,096	3,751	Unsecured
Cornerstone (Haven Trust)			400	Unsecured
Branch Banking & Trust		263	263	Secured
Wachovia			133	Unsecured
Seller Emerald Farm		100	100	Secured
Fifth Third			25	Unsecured
Eagle Bank Potomac Yard / Penderbrook		4,084		Secured
Eagle Bank New Hampshire Ave.		3,159		Secured
Eagle Bank Redland Road		2,500		Secured
Rosalie K. Stahl Trust		3,000		Secured
TSR-Shady Grove, LLC.		5,750		Secured
		22,588	24,807	
Due to affiliates Stonehenge Funding		5,041	5,008	Unsecured
Total		\$ 27,629	\$ 29,815	

**Table of Contents****Significant 2012 Borrowings***Eagle Bank*

On May 29, 2012, the Company, through its Comstock Potomac Yard, L.C. and Comstock Penderbrook, L.C. subsidiaries, entered into a loan agreement with Eagle Bank pursuant to which the Company secured a \$9.96 million loan with a twenty-seven month term (the Eagle Bank Loan ) to refinance the Company's Eclipse condominium project and Penderbrook Square condominium project. Proceeds from the Eagle Bank Loan were primarily utilized (i) to pay off existing indebtedness of approximately \$7.97 million, (ii) set up an interest reserve escrow pursuant to the term of agreement in the amount \$0.5 million, (iii) pay approximately \$0.1 million in settlement charges and closing costs, and (iv) for general corporate purpose. The interest reserve escrow is held in the name of the bank, and if the borrower defaults under the loan agreement, the bank has sole discretion to apply the funds or portion of the funds to pay off the indebtedness. Commencing thirty days after closing, the Company is required to make monthly payments of interest only on outstanding principal balance, principal curtailment payments upon settlements at the two subsidiaries and a minimum principal curtailment payment of \$4.98 million no later than 12 months following the closing of the Eagle Bank Loan. There is no prepayment penalty associated with the Eagle Bank Loan. The balance outstanding at December 31, 2012 was \$4.08 million.

On August 23, 2012, the Company, through New Hampshire Ave. Ventures, LLC, a consolidated joint venture of its subsidiary Comstock Ventures XVI, L.C. and 6000 New Hampshire Avenue, LLC, entered into a three-year loan agreement and related documents with Eagle Bank securing a \$6.0 million revolving development loan and a \$4.0 million revolving construction loan (collectively, the Eagle NHA Revolver ) to finance The Hampshires, the Company's 111-unit project located in Washington, D.C. Proceeds from the Eagle NHA Revolver will primarily be utilized to (i) pay for expenses associated with the Eagle NHA Revolver; (ii) reimburse the Company for development costs previously expended and (iii) to pay for the future development and construction related expenses. Under the terms of the Loan Agreement, the Eagle NHA Revolver provides for an initial floating interest rate of LIBOR plus 3% with an interest rate floor of 5.75%. The New Hampshire Ave. Ventures, LLC is required to make monthly interest payments on the Eagle NHA Revolver to the extent not offset by a \$400 interest reserve initially set aside for the benefit of the Borrower and is required to make a minimum principal curtailment under the development portion of the Eagle NHA Revolver of \$3.22 million by December 31, 2013 and additional curtailments on a quarterly basis thereafter. There is no prepayment penalty associated with the Eagle NHA Revolver, which is secured by a first deed of trust and is fully guaranteed by the Company. The balance outstanding at December 31, 2012 was \$3.16 million.

On December 27, 2012, the Company, through Comstock Redland Road, L.C. subsidiary (the Borrower ) entered into an acquisition bridge loan (the Bridge Loan ) with Eagle Bank ( Lender ), pursuant to which the Company secured \$2.5 million to finance the Company's acquisition of the property directly adjacent to the Shady Grove Metro in Rockville, Montgomery County, Maryland. The Company utilized the proceeds from the Eagle Bank Loan (the Bridge Loan ) to (i) pay for the acquisition of land planned for development of 36 townhomes, 3 single family, and a 117-unit multi-family apartments and (ii) to pay for expenses associated with settlement charges and closing costs. Under the terms of the loan agreement, the Bridge Loan provides for an interest rate of 5% per annum. The Company is expected to make monthly interest payments commencing thirty days after closing, with entire principal balance due March 28, 2013. The loan is secured by a promissory note, second deed of trust and security agreement on the property, second deed of trust and security agreement on the Potomac Yard project, a guaranty of Comstock Holding Companies, Inc., Comstock Potomac Yard, L.C. and Christopher Clemente, the Chief Executive Officer of Comstock Holding Companies, Inc., and other ancillary documents (collectively, the Bridge Loan Documents ). There is no prepayment penalty associated with the Bridge Loan. The amount outstanding at December 31, 2012 was \$2.5 million. The Bridge Loan was repaid in full on March 25, 2012 as further described in Note 20 to the consolidated financial statements.

*Rosalie K. Stahl Trust*

On August 23, 2012, the Company, through New Hampshire Ave. Ventures, LLC, a consolidated joint venture of its subsidiary Comstock Ventures XVI, L.C. and 6000 New Hampshire Avenue, LLC, also entered into a \$3.0 million mezzanine loan (the NHA Mezzanine Loan ) in connection with the The Hampshires project with the Rosalie K. Stahl Trust. Proceeds from the NHA Mezzanine Loan, which has a three-year maturity date, were utilized to acquire the land for development of the project. The NHA Mezzanine Loan provides for an interest rate of 13.5% per annum, interest to be paid current on a monthly basis, with the full principal balance being due at maturity. The NHA Mezzanine Loan is secured by a second deed of trust, which is fully subordinate to the Eagle NHA Revolver and is non-recourse to the Company. There is no prepayment penalty associated with the NHA Mezzanine Loan.

---

## **Table of Contents**

### *Cardinal Bank*

On September 27, 2012, the Company, through Comstock Eastgate, L.C. ( *Eastgate* ), a consolidated joint venture of Comstock Holding Companies, Inc. and BridgeCom Development I, LLC, entered into a loan agreement with Cardinal Bank to which the Company secured a \$2.5 million revolving construction loan (the *Cardinal Bank Revolver* ) to finance The Villas at Eastgate, the Company's 66-unit project located in Loudoun County, VA. The loan maturity is twelve months from origination, with an automatic extension of twelve months subject to the Company meeting sales conditions, which include (i) entering into binding contracts for the sale of eighteen units and (ii) settling twelve units, each by the one year anniversary of the loan. The proceeds of Cardinal Bank Revolver will be primarily utilized to pay expenses associated with the loan and future construction expenses of the project. The Cardinal Bank Revolver provides for a variable interest rate of Prime plus 0.5%, with an interest rate floor of 4.75%. Commencing thirty days after loan close, the Company is required to make monthly payments of interest only and upon the closing of the sale of a unit, make principal curtailment payments of 100% of unit costs borrowed. There is no prepayment penalty associated with the Cardinal Bank Revolver.

### *TSR-Shady Grove, LLC*

On December 27, 2012, the Company, through the Comstock Redland Road, L.C. subsidiary, entered into a Deferred Purchase Money Promissory Note with TSR-Shady Grove, LLC, a Maryland Limited liability company, pursuant to which the Company secured \$5.75 million for the acquisition of land planned for development of 36 town houses, 3 single family moderately priced dwelling units and a 117-unit multi-family apartments. The TSR-Shady Grove Loan provides for an interest rate of 6% per annum, interest is payable commencing thirty days after closing, with entire principal balance due March 28, 2013. However, pursuant to the Purchase and Sale Agreement, no interest shall accrue until the property is vacated. Subsequent to December 31, 2012, the tenant vacated the property. The TSR-Shady Grove Loan is secured by a deferred purchase money first deed of trust. There is no prepayment penalty associated with Redland Road Loan. The balance outstanding at December 31, 2012 was \$5.75 million. The Deferred Purchase Money Promissory Note was repaid in full on March 25, 2012 as further described in Note 20 to the consolidated financial statements.

### *Stonehenge*

On March 14, 2013, Stonehenge Funding, LC ( *Stonehenge* ), an entity wholly-owned by the Chief Executive Officer of the Company, entered into an Extension Agreement of the Amended and Restated Senior Note with the Company to extend the maturity date of the financing arrangement to January 1, 2016. Under the terms of the Extension Agreement, the Company is required to pay \$50 monthly to Stonehenge, to be allocated first to accrued and unpaid interest and then to unpaid principal outstanding, beginning on April 1, 2013. The Extension Agreement was subject to the approval by the Company's board of directors and approval was obtained on March 21, 2013.

### ***Cash Flow***

Net cash used in operating activities was \$16.0 million for the year ended December 31, 2012. This represents a decline from the net cash provided by operating activities of \$12.7 million for the year ended December 31, 2011. However, the 2012 cash flows do not reflect the net cash flows from the sale of the Cascades Apartments of approximately \$4.7 million. Although the construction, development and sale of this and potentially other future merchant build projects are an ongoing component of the Company's operations, the sale of the project is required to be presented as Discontinued Operations. Accordingly, the net cash flows are presented within the investing and financing section of the accompanying consolidated statement of cash flows. Additionally, for 2012, other significant outflows relate to a \$1.2 million reduction in accrued interest payable for debt service payments made to lenders, a \$19.3 million dollar change in cash flows related to real estate held for development and sale arising from land acquisitions and expenditures for development activities and a \$0.5 million reduction in payables related to payments made to vendors and compensation paid to employees, reflective of the improved cash position of the Company.

Net cash provided by investing activities was \$18.9 million for the year ended December 31, 2012, primarily attributable to the sale of the Cascades Apartments. Net cash used in investing activities was \$9.8 million for the year ended December 31, 2011, primarily attributable to the development of the Cascades Apartments.

Net cash used in financing activities was \$5.0 million for the year ended December 31, 2012, primarily attributable to the payoff of long outstanding deficiency notes, debt curtailments on settlements and refinancing and retirement of the non-controlling interests, including preferred returns, in full related to the Cascades Apartments. Net cash provided by financing activities was \$2.3 million for the year ended December 31, 2011, primarily attributable to the Private Placement for the Cascades Apartments.

### ***Seasonality and Weather***

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Our business is affected by seasonality with respect to orders and deliveries. In the market in which we operate, the primary selling season is from January through May as well as September and October. Orders in other months typically are lower. In addition, the markets in which we operate are four-season markets that experience significant periods of rain and snow. Construction cycles and efforts are often adversely affected by severe weather.

## **Table of Contents**

### **Inflation**

Inflation can have a significant impact on our business performance and the home building industry in general. Rising costs of land, transportation costs, utility costs, materials, labor, overhead, administrative costs and interest rates on floating credit facilities can adversely affect our business performance. In addition, rising costs of certain items, such as lumber, can adversely affect the expected profitability of our backlog. Generally, we have been able to recover any increases in costs through increased selling prices. However, there is no assurance we will be able to increase selling prices in the future to cover the effects of inflation and other cost increases.

### **Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

Not applicable.

### **Item 8. Financial Statements and Supplementary Data**

Reference is made to the financial statements, the notes thereto, and the report thereon, commencing on page F-1 of this report, which financial statements, notes, and report are incorporated herein by reference.

### **Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

Not applicable.

### **Item 9A. Controls and Procedures**

#### **Evaluation of Disclosure Controls and Procedures**

We have evaluated, with the participation of our Chief Executive Officer and our Chief Financial Officer, the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of December 31, 2012. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded, as of December 31, 2012, that our disclosure controls and procedures were effective, and designed to ensure that (a) information required to be disclosed in our reports filed under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and instructions, and (b) information is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate to allow timely decisions regarding required disclosures.

#### **Limitations on the Effectiveness of Controls**

We do not expect that our disclosure controls and internal controls will prevent all error and all fraud. A control system, no matter how well conceived and operated, can provide only assurance, at the reasonable assurance level, 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 their costs. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, a control may become inadequate because of changes in conditions or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and may not be detected.

#### **Management's Report on Internal Control Over Financial Reporting**



## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Management is responsible for establishing and maintaining adequate internal control over our financial reporting, as such term is defined in Rule 13a-15(f)/15d-15(f) of the Exchange Act.

Our management assessed the effectiveness of our internal control over financial reporting as of December 31, 2012, based on criteria set forth in the framework in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). This evaluation included review of the documentation of controls, evaluation of the design effectiveness of controls, testing of the operating effectiveness of controls and a conclusion on this evaluation. Our management determined that, as of December 31, 2012, our internal control over financial reporting is effective.

**Changes in Internal Control**

No change has occurred in our internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) of the Exchange Act) during our last fiscal quarter ended December 31, 2012, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**Item 9B. Other Information**

None.

**Table of Contents**

**PART III**

**Item 10. Directors, Executive Officers and Corporate Governance**

The information required by this Item is incorporated herein by reference to the definitive Proxy Statement to be filed pursuant to Regulation 14A of the Exchange Act for our 2013 Annual Meeting of Stockholders, except that the information relating to our executive officers is included in Item 1, Business Executive Officers of this report.

**Item 11. Executive Compensation**

The information required by this Item is incorporated herein by reference to the definitive Proxy Statement to be filed pursuant to Regulation 14A of the Exchange Act for our 2013 Annual Meeting of Stockholders.

**Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters**

The information required by this Item is incorporated herein by reference to the definitive Proxy Statement to be filed pursuant to Regulation 14A of the Exchange Act for our 2013 Annual Meeting of Stockholders.

**Item 13. Certain Relationships and Related Transactions, and Director Independence**

The information required by this Item is incorporated herein by reference to the definitive Proxy Statement to be filed pursuant to Regulation 14A of the Exchange Act for our 2013 Annual Meeting of Stockholders.

**Item 14. Principal Accountant Fees and Services**

The information required by this Item is incorporated herein by reference to the definitive Proxy Statement to be filed pursuant to Regulation 14A of the Exchange Act for our 2013 Annual Meeting of Stockholders.

**Table of Contents**

**PART IV**

**Item 15. Exhibits and Financial Statement Schedules**

(a) The following documents are filed as part of this report:

- (1) Financial Statements are listed in the Index to Financial Statements on page F-1 of this report.
- (2) Schedules have been omitted because they are not applicable or because the information required to be set forth therein is included in the consolidated and combined financial statements or notes thereto.
- (3) Exhibits

<b>Exhibit</b>	
<b>Number</b>	<b>Exhibit</b>
3.1(2)	Amended and Restated Certificate of Incorporation
3.2(2)	Amended and Restated Bylaws
4.1(1)	Specimen Stock Certificate
10.1(1)	Lease Agreement, dated as of January 31, 2004, with Comstock Partners, L.C.
10.2(1)	Agreement of Sublease, dated as of October 1, 2004, with Comstock Asset Management, L.C.
10.3(1)	Form of Indemnification Agreement
10.4(1)	Form of Promissory Note to be issued to each of Christopher Clemente, Gregory Benson, James Keena and Lawrence Golub by each of Comstock Holding Company, Inc., Comstock Homes, Inc., Sunset Investment Corp., Inc. and Comstock Service Corp., Inc.
10.5(1)	Form of Tax Indemnification Agreement to be entered into by each of Christopher Clemente, Gregory Benson, James Keena and Lawrence Golub with each of Comstock Holding Company, Inc., Comstock Homes, Inc., Sunset Investment Corp., Inc. and Comstock Service Corp., Inc.
10.6(1)	2004 Long-Term Incentive Compensation Plan+
10.7(1)	Form Of Stock Option Agreement under the 2004 Long-Term Incentive Compensation Plan+
10.8(2)	Form Of Restricted Stock Grant Agreement under the 2004 Long-Term Incentive Compensation Plan+
10.9(1)	Employee Stock Purchase Plan+
10.10(2)	Purchase and Sale Agreement, dated as of November 9, 2004, as amended, with Fair Oaks Penderbrook Apartments L.L.C.
10.11(2)	Services Agreement, dated March 4, 2005, with Comstock Asset Management, L.C.
10.12(1)	Employment Agreement with Christopher Clemente+
10.13(1)	Employment Agreement with Gregory Benson+
10.14(1)	Confidentiality and Non-Competition Agreement with Christopher Clemente+
10.15(1)	Confidentiality and Non-Competition Agreement with Gregory Benson+
10.16(1)	Trademark License Agreement
10.17(2)	Purchase Agreement, dated as of November 12, 2004 with Comstock Asset Management, L.C.
10.18(4)	Description of Reimbursement and Indemnification Arrangement with Christopher Clemente and Gregory Benson

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

- 10.19(5) Stock Purchase Agreement with Parker-Chandler Homes, Inc. and the Selling Stockholders identified therein, dated as of January 19, 2006
- 10.20(6) Form of purchase agreement, dated as of May 5, 2006, as amended as of May 9, 2006, by and between the Company and the purchasers identified therein
- 10.21(6) Form of warrant
- 10.22(7) Note Purchase Agreement with Kodiak Warehouse LLC, dated as of May 4, 2006
- 10.23(7) Junior Subordinated Indenture with Wells Fargo Bank, N.A., dated as of May 4, 2006
- 10.24(7) Credit Agreement with Wachovia Bank, N.A., dated as of May 26, 2006
- 10.25(7) Stock Purchase Agreement with Capitol Homes, Inc. and the Selling Shareholders identified therein, dated as of May 1, 2006

**Table of Contents**

10.26(9)	Loan and Security Agreement, dated as of February 2008, by and between the Registrant and Stonehenge Funding, LC.
10.27(9)	Guaranty Agreement, dated as of February 2008, by Comstock Potomac Yard, L.C. in favor of Stonehenge Funding, LC.
10.28(9)	Supplement to Indenture, dated as of January 7, 2008, by and between the Registrant and Wells Fargo Bank, N.A.
10.29(9)	Amended and Restated Indenture, dated as of March 14, 2008, by and between the Registrant and Wells Fargo Bank, N.A.
10.30(10)	Forbearance and Conditional Release Agreement, dated as of November 25, 2008, by and among Highland Avenue Properties, LLC, Comstock Homes of Atlanta, LLC, the Registrant and Bank of American, N.A.
10.31(10)	Sixth Loan Modification Agreement, dated as of November 26, 2008, by and among the Registrant and Bank of America, N.A.
10.32(10)	Amended and Restated Promissory Note (Tribble Road Loan), dated as of December 10, 2008, by the Registrant in favor of Wachovia Bank, National Association.
10.33(10)	Loan Modification and Forbearance Agreement, dated as of December 10, 2008, by and among the Registrant, various wholly owned subsidiaries as guarantors and Wachovia Bank, National Association.
10.34(10)	Amended and Restated Promissory Note (Revolving Line of Credit), dated as of December 10, 2008, by the Registrant in favor of Wachovia Bank, National Association.
10.35(10)	Amended and Restated Promissory Note (Term Loan), dated as of December 10, 2008, by the Registrant in favor of Wachovia Bank, National Association.
10.36(11)	Consensual Foreclosure and Settlement Agreement, dated August 17, 2009, by and among the Registrant, et.al. and Wachovia Bank, National Association
10.37(11)	Third Amendment of Loan Agreement, dated September 16, 2009, by and among Comstock Penderbrook, L.C., the Registrant and Guggenheim Corporate Funding, LLC
10.38(11)	Settlement Agreement and Mutual Release, dated September 21, 2009, by and among Registrant, Mathis Partners, LLC and Cornerstone Bank
10.39(11)	Forbearance Agreement, dated September 28, 2009, by and among Comstock Cascades, L.C., the Registrant and Manufacturers and Traders Trust Company
10.40(11)	Forbearance and Conditional Release Agreement, dated September 28, 2009, by and among Comstock Belmont Bay 89, L.C., the Registrant and Manufacturers and Traders Trust Company
10.41(11)	First Amendment to Loan Agreement, dated October 30, 2009, by and among Comstock Station View, L.C., Comstock Potomac Yard, L.C., the Registrant and Key Bank National Association
10.42(11)	Forbearance and Conditional Release Agreement, dated November 10, 2009, by and among Comstock Homes of Raleigh, L.L.C., the Registrant and Fifth Third Bank, N.A.
10.43(12)	Forbearance Agreement and Second Amendment to Loan Agreement, dated January 27, 2009, by and among Comstock Penderbrook, L.C., the Registrant and Guggenheim Corporate Funding, LLC
10.44(12)	Fourth Amendment to Sublease Agreement and Services Agreement, dated February 26, 2009, with Comstock Asset Management
10.45(12)	Subordinated Deficiency Note, dated as of September 21, 2009, by the Registrant in favor of Cornerstone Bank., successor-in-interest to HavenTrust Bank.
10.46(12)	Amended and Restated Subordinated Deficiency Note, dated as of November 5, 2009, by the Registrant in favor of Wachovia Bank, National Association.
10.47(12)	Bankruptcy filing for Buckhead Overlook, LLC, filed November 2009 in the U.S. Bankruptcy Court, Northern District of Georgia, Atlanta Division
10.48(12)	Bankruptcy filing for Post Preserve, LLC filed November 2009 in the U.S. Bankruptcy Court, Northern District of Georgia, Atlanta Division
10.49(12)	Bankruptcy filing for Parker Chandler Homes, LLC f/k/a Comstock Homes of Atlanta, LLC filed November 2009 in the U.S. Bankruptcy Court, Northern District of Georgia, Atlanta Division
10.50(12)	

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Lease Agreement, dated on or about December 31, 2009, with Comstock Asset Management, L.C. by Comstock Property Management, L.C., a subsidiary of Registrant

10.51(12) License Agreement, effective January 1, 2010, with I-Connect

**Table of Contents**

10.52(12)	Letter of Intent, effective February 12, 2010, by and between Registrant and Stonehenge Funding, L.C. and Subordination and Standstill Agreements between Registrant and Guggenheim Corporate Funding, LLC and between Registrant and Key Bank, National Association
10.53(12)	Seventh Loan Modification Agreement, dated as of February 25, 2010, by and among the Registrant and Bank of America, N.A.
10.54(12)	Memorandum Opinion, filed February 23, 2010, by the US District Court in favor of Comstock Potomac Yard, L.C., a subsidiary of Registrant, against Balfour Beatty Construction, LLC
10.55(12)	Purchase Agreement, dated October 30, 2009, by and between Comstock Station View, L.C. and M/I Homes of DC, LLC
10.56(13)	Second Amended and Restated Indenture, dated as of February 12, 2010, by and among the Registrant and Comstock Asset Management, L.C.
10.57(13)	Amended and Restated Senior Note, effective February 12, 2010, by and among, Stonehenge Funding, LC, the Registrant and Comstock Asset Management, L.C.
10.58(13)	Employment Agreement with Joseph M. Squeri+
10.59(13)	Confidentiality and Non-Competition Agreement with Joseph M. Squeri+
10.60(14)	Loan Agreement, dated as of January 27, 2011, by and among Comstock Potomac Yard, L.C. and Eagle Bank
10.61(14)	Loan Agreement, dated as of February 11, 2011, by and among Comstock Cascades II, L.C. and Cardinal Bank
10.62(15)	Credit Enhancement and Indemnification Agreement, dated February 17, 2011, by and between Registrant and Christopher D. Clemente and Gregory V. Benson.
10.63(16)	Loan Agreement, dated as of July 12, 2011, by and among Comstock Potomac Eclipse, L.C. and BCL Eclipse, LLC.
10.64(16)	Guaranty, Pledge and Security Agreement, dated as of July 12, 2011, by Comstock Homebuilding Companies, Inc. and Comstock Emerald Farm, L.C. to and for the benefit of BCL Eclipse, LLC.
10.65(16)	Warrant, dated as of July 12, 2011, in the name of BridgeCom Development I, LLC.
10.66(16)	Registration Rights Agreement, dated as of July 12, 2011, between Comstock Homebuilding Companies, Inc. and BridgeCom Development I, LLC.
10.67(16)	Right of First Refusal and First Offer Agreement, dated as of July 12, 2011, between Comstock Homebuilding Companies, Inc. and BridgeCom Development I, LLC.
10.68(17)	Loan Agreement, dated as of October 5, 2011, by and among Comstock Penderbrook, L.C. and BCL Penderbrook, LLC.
10.69(17)	Contract of Sale Agreement, dated as of October 31, 2011, by and among Comstock Cascades II, L.C. and CAPREIT Acquisition Corporation.
10.70(17)	Loan Agreement, dated as of May 29, 2012, by and among Eagle Bank and Comstock Potomac Yard, L.C. and Comstock Penderbrook, L.C.
10.71(17)	Loan agreement, dated as of August 23, 2012, by and between Eagle Bank and New Hampshire Ave. Ventures, LLC.
10.72(17)	Loan agreement, dated as of September 27, 2012, by and between Cardinal Bank and Comstock Eastgate, L.C.
10.73(18)	Loan agreement, dated as of August 23, 2012, by and between Rosalie K. Stahl Trust and New Hampshire Ave. Ventures, LLC.
10.74(19)	Loan agreement, dated as of December 27, 2012, by and between Eagle Bank and Comstock Redland Road, L.C.
10.75(19)	Loan agreement, dated as of December 27, 2012, by and between TSR-Shady Grove, LLC and Comstock Redland Road, L.C.
10.76*	Loan agreement, dated as of March 25, 2013, by and between Eagle Commercial Ventures, LLC and Comstock Redland Road, L.C.
10.77*	Loan agreement, dated as of March 25, 2013, by and between Eagle Commercial Ventures, LLC and Comstock Redland Road, L.C.
10.78*	Loan agreement, dated as of March 25, 2013, by and between Eagle Bank and Comstock Redland Road, L.C.
10.79*	Loan agreement, dated as of March 25, 2013, by and between Eagle Bank and Comstock Redland Road, L.C.



## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

11	Statement of computation of per share earnings
14.1(2)	Code of Ethics
21.1*	List of subsidiaries
23.1*	Consent of PricewaterhouseCoopers LLP
31.1*	Certification of Chief Executive Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002
31.2*	Certification of Chief Financial Officer pursuant to Section 302 of Sarbanes-Oxley Act of 2002
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of Sarbanes-Oxley Act of 2002

**Table of Contents**

- \* Filed herewith.
- + Management contracts or compensatory plans, contracts or arrangements
- (1) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 31, 2005.
- (2) Incorporated by reference to an exhibit to the Registrant's Registration Statement on Form S-1, as amended, initially filed with the Commission on August 13, 2004 (No. 333-118193).
- (3) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on November 14, 2005.
- (4) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on August 9, 2005.
- (5) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 16, 2006.
- (6) Incorporated by reference to an exhibit to the Current Report on Form 8-K of the Registrant filed with the Commission on May 10, 2005.
- (7) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on August 9, 2006.
- (8) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 16, 2007.
- (9) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 24, 2008.
- (10) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 31, 2009.
- (11) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on November 13, 2009.
- (12) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 31, 2010.
- (13) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on November 12, 2010.
- (14) Incorporated by reference to an exhibit to the Registrant's Annual Report on Form 10-K filed with the Commission on March 31, 2011.
- (15) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on May 13, 2011.
- (16) Incorporated by reference to an exhibit to the Current Report on Form 8-K filed with the Securities and Exchange Commission on July 15, 2011.
- (17) Incorporated by reference to an exhibit to the Registrant's Quarterly Report on Form 10-Q filed with the Commission on November 14, 2012.
- (18) Incorporated by reference to the Current Report on Form 8-K filed with the Securities and Exchange Commission on August 27, 2012.
- (19) Incorporated by reference to the Current Report on Form 8-K filed with the Securities and Exchange Commission on January 3, 2013.

**Table of Contents**

**SIGNATURES**

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

**COMSTOCK HOLDING COMPANIES, INC.**

Date: March 27, 2013

By: /s/ CHRISTOPHER CLEMENTE  
 Christopher Clemente  
 Chairman and Chief Executive Officer

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

Signature	Capacity	Date
/s/ CHRISTOPHER CLEMENTE Christopher Clemente	Chairman of the Board of Directors and Chief Executive Officer (Principal Executive Officer)	March 27, 2013
/s/ GREGORY V. BENSON Gregory V. Benson	President and Chief Operating Officer	March 27, 2013
/s/ JOSEPH M. SQUERI Joseph M. Squeri	Chief Financial Officer (Principal Financial Officer)	March 27, 2013
/s/ A. CLAYTON PERFALL A. Clayton Perfall	Director	March 27, 2013
/s/ DAVID M. GUERNSEY David M. Guernsey	Director	March 27, 2013
/s/ JAMES A. MACCUTCHEON James A. MacCutcheon	Director	March 27, 2013
/s/ NORMAN D. CHIRITE Norman D. Chirite	Director	March 27, 2013
/s/ ROBERT P. PINCUS Robert P. Pincus	Director	March 27, 2013
/s/ SOCRATES VERSES Socrates Verses	Director	March 27, 2013

**Table of Contents**

**INDEX TO CONSOLIDATED FINANCIAL STATEMENTS**

	<b>Page</b>
COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES	
<u>Report of Independent Registered Public Accounting Firm</u>	F-2
<u>Consolidated Balance Sheets at December 31, 2012 and 2011</u>	F-3
<u>Consolidated Statements of Operations for the Years Ended December 31, 2012 and 2011</u>	F-4
<u>Consolidated Statements of Changes in Shareholders' Equity for the Years Ended December 31, 2012 and 2011</u>	F-5
<u>Consolidated Statements of Cash Flows for the Years Ended December 31, 2012 and 2011</u>	F-6
<u>Notes to Consolidated Financial Statements</u>	F-8

F-1

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

To the Board of Directors and Shareholders of Comstock Holding Companies, Inc.:

In our opinion, the consolidated financial statements listed on page F-1 present fairly, in all material respects, the financial position of Comstock Holding Companies, Inc. and subsidiaries (the Company) at December 31, 2012 and 2011, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2012 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

/s/ PricewaterhouseCoopers LLP

McLean, Virginia

March 27, 2013

F-2

**Table of Contents****COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**

(Amounts in thousands, except per share data)

	December 31, 2012	December 31, 2011
<b>ASSETS</b>		
Cash and cash equivalents	\$ 3,539	\$ 5,639
Restricted cash	3,203	3,082
Trade receivables	1,611	2,228
Real estate held for development and sale	27,781	21,212
Operating real estate, net		12,095
Property, plant and equipment, net	222	105
Other assets	2,343	2,018
<b>TOTAL ASSETS</b>	<b>\$ 38,699</b>	<b>\$ 46,379</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
<b>LIABILITIES</b>		
Accounts payable and accrued liabilities	\$ 4,691	\$ 3,987
Notes payable secured by real estate held for development and sale, net of discount	19,492	10,541
Notes payable secured by operating real estate		9,957
Notes payable due to affiliates, unsecured	5,041	5,008
Notes payable unsecured	3,096	4,309
Income taxes payable		33
<b>TOTAL LIABILITIES</b>	<b>32,320</b>	<b>33,835</b>
<b>Commitments and contingencies (Note 15)</b>		
<b>SHAREHOLDERS EQUITY</b>		
Class A common stock, \$0.01 par value, 77,266,500 shares authorized, 17,627,826 and 17,944,503 issued and outstanding, respectively	176	179
Class B common stock, \$0.01 par value, 2,733,500 shares authorized, 2,733,500 issued and outstanding	27	27
Additional paid-in capital	170,070	168,620
Treasury stock, at cost (391,400 shares Class A common stock)	(2,480)	(2,439)
Accumulated deficit	(162,349)	(156,684)
<b>TOTAL COMSTOCK HOLDING COMPANIES, INC. EQUITY</b>	<b>5,444</b>	<b>9,703</b>
Non-controlling interests	935	2,841
<b>TOTAL EQUITY</b>	<b>6,379</b>	<b>12,544</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS EQUITY</b>	<b>\$ 38,699</b>	<b>\$ 46,379</b>

The accompanying notes are an integral part of these consolidated financial statements



**Table of Contents****COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS**

(Amounts in thousands, except per share data)

	Twelve Months Ended December 31,	
	2012	2011
<b>Revenues</b>		
Revenue homebuilding	\$ 11,633	\$ 14,062
Revenue other	2,669	7,871
<b>Total revenue</b>	<b>14,302</b>	<b>21,933</b>
<b>Expenses</b>		
Cost of sales homebuilding	9,692	12,160
Cost of sales other	3,484	7,434
Impairments and write-offs	2,358	
Selling, general and administrative	8,658	7,399
Interest, real estate taxes and indirect costs related to inactive projects	2,135	2,739
<b>Operating loss</b>	<b>(12,025)</b>	<b>(7,799)</b>
Gain on troubled debt restructuring		(219)
Gain on legal settlement, net		(9,434)
Other income, net	(18)	(304)
<b>(Loss) income before income tax benefit (expense)</b>	<b>(12,007)</b>	<b>2,158</b>
Income taxes benefit (expense)	2,484	(33)
<b>Net (loss) income from continuing operations</b>	<b>(9,523)</b>	<b>2,125</b>
<b>Discontinued operations:</b>		
Loss from discontinued operations	(98)	(527)
Gain on sale of the real estate from discontinued operations	6,466	
Income tax expense from discontinued operations	(2,484)	
<b>Net income (loss) from discontinued operations</b>	<b>3,884</b>	<b>(527)</b>
<b>Net (loss) income</b>	<b>(5,639)</b>	<b>1,598</b>
Less: Net loss from continuing operations attributable to non-controlling interests	(77)	
Less: Net income from discontinued operations attributable to non-controlling interests	103	491
<b>Net (loss) income attributable to Comstock Holding Companies, Inc.</b>	<b>\$ (5,665)</b>	<b>\$ 1,107</b>
<b>Basic (loss) income per share:</b>		
Continuing operations	\$ (0.47)	\$ 0.10
Discontinued operations	0.19	(0.05)
<b>Net (loss) income per share</b>	<b>\$ (0.28)</b>	<b>\$ 0.05</b>
<b>Diluted (loss) income per share:</b>		
Continuing operations	\$ (0.47)	\$ 0.10



Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Discontinued operations		0.19		(0.05)
Net (loss) income per share		\$ (0.28)	\$	0.05
Basic weighted average shares outstanding		19,970		20,287
Diluted weighted average shares outstanding		19,970		20,720
Net (loss) income attributable to Comstock Holding Companies, Inc.:				
(Loss) income from continuing operations		\$ (9,446)	\$	2,125
Income (loss) from discontinuing operations		3,781		(1,018)
Net (loss) income		\$ (5,665)	\$	1,107

The accompanying notes are an integral part of these consolidated financial statements.

F-4

**Table of Contents****COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CHANGES IN****SHAREHOLDERS EQUITY**

(Amounts in thousands, except per share data)

	Class A		Class B		Additional paid-in capital	Treasury stock	Retained earnings (deficit)	Non-controlling interest	Total
	Shares	Amount	Shares	Amount					
Balance at December 31, 2010	17,121	\$ 171	2,733	\$ 27	\$ 166,700	\$ (2,439)	\$ (157,791)	\$	\$ 6,668
Stock compensation and issuances	824	8			924				932
Warrants					996				996
Cascades Private Placement								2,350	2,350
Net income							1,107	491	1,598
Balance at December 31, 2011	17,945	\$ 179	2,733	\$ 27	\$ 168,620	\$ (2,439)	\$ (156,684)	\$ 2,841	\$ 12,544
Stock compensation and issuances (Note 2)	(317)	(3)			1,450				1,447
Net-settlement repurchases of stock compensation						(41)			(41)
Non-controlling interest contributions								1,012	1,012
Non-controlling interest distributions								(2,944)	(2,944)
Net income							(5,665)	26	(5,639)
Balance at December 31, 2012	17,628	\$ 176	2,733	\$ 27	\$ 170,070	\$ (2,480)	\$ (162,349)	\$ 935	\$ 6,379

The accompanying notes are an integral part of these consolidated financial statements.

**Table of Contents****COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS**

(Amounts in thousands, except per share data)

	Twelve Months Ended December 31,	
	2012	2011
Cash flows from operating activities:		
Net (loss) income	\$ (5,639)	\$ 1,598
Adjustment to reconcile net (loss) income to net cash (used in) provided by operating activities		
Amortization of loan discount and deferred financing fees	1,283	1,444
Depreciation expense	122	196
Provision for bad debt	60	1
Impairments and write-offs	2,358	
Amortization of stock compensation	1,447	932
Loss (gain) on extinguishment of notes payable	73	(219)
Gain on trade payable settlements		(161)
Gain on sale of operating real estate, net	(6,466)	
Loss on disposal of property, plant and equipment	1	
Changes in operating assets and liabilities:		
Restricted cash	(121)	19
Trade receivables	569	(1,837)
Real estate held for development and sale	(8,984)	10,292
Other assets	(433)	(678)
Accrued interest	(495)	752
Accounts payable and accrued liabilities	217	364
Income taxes payable	(33)	33
<b>Net cash (used in) provided by operating activities</b>	<b>(16,041)</b>	<b>12,736</b>
Cash flows from investing activities:		
Investment in Cascades Apartments operating real estate, net		(9,764)
Purchase of property, plant and equipment	(158)	(78)
Proceeds from sale of Cascades Apartments operating real estate, net	19,075	
<b>Net cash provided by (used in) investing activities</b>	<b>18,917</b>	<b>(9,842)</b>
Cash flows from financing activities:		
Proceeds from notes payable	24,986	38,908
Payments on notes payable	(27,512)	(38,436)
Loan financing costs	(518)	(1,548)
Proceeds from SunBridge warrant issuance		996
Distribution to non-controlling interest holders	(2,944)	
Contribution from non-controlling interest holders	1,012	2,350
<b>Net cash (used in) provided by financing activities</b>	<b>(4,976)</b>	<b>2,270</b>
<b>Net (decrease) increase in cash and cash equivalents</b>	<b>(2,100)</b>	<b>5,164</b>
Cash and cash equivalents, beginning of period	5,639	475

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Cash and cash equivalents, end of period	\$	3,539		\$	5,639
Supplemental disclosures:					
Interest paid, net of interest capitalized	\$	1,226		\$	522
Reduction in proceeds from sale of Cascades Apartments and increase in other assets related to amount placed in escrow upon settlement of Cascades Apartments sale	\$	275		\$	
Increase in class A common stock par value in connection with issuance of stock compensation	\$			\$	8
Increase in additional paid in capital in connection with SunBridge warrant	\$			\$	996
Increase in treasury stock and accrued liabilities for net-settlement of stock compensation	\$	41		\$	

The accompanying notes are an integral part of these consolidated financial statements.

---

**Table of Contents**

**COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Amounts in thousands, except per share data)**

**1. ORGANIZATION**

Comstock Holding Companies, Inc. is a multi-faceted real estate development and construction services company focused on the Washington, D.C. metropolitan area. The Company has substantial experience with building a diverse range of products including single-family homes, townhouses, mid-rise condominiums, high-rise multi-family condominiums, apartments and mixed-use (residential and commercial) developments. Since our founding in 1985, and as of December 31, 2012, we have built and delivered more than 5,500 homes generating total revenue in excess of \$1.4 billion. References in this Form 10-K to Comstock, Company, we, our and us refer to Comstock Holding Companies, Inc. together in each case with our subsidiaries and any predecessor entities unless the context suggests otherwise.

Our business was founded in 1985 as a residential land developer and home builder focused on the Northern Virginia suburbs of the Washington, D.C. area.

Comstock Companies, Inc. was incorporated on May 24, 2004 as a Delaware corporation. On June 30, 2004, the Company changed its name to Comstock Homebuilding Companies, Inc. On December 17, 2004, the Company completed an initial public offering ( IPO ) of its Class A common stock. On June 22, 2012, the Company changed its name to Comstock Holding Companies, Inc. which better reflects the Company's multi-faceted strategy and capabilities.

The Company's Class A common stock is traded on the Nasdaq Capital Market ( NASDAQ ) under the symbol CHCI and has no public trading history prior to December 17, 2004. The Company continues to be in compliance with all NASDAQ continued listing requirements.

***Liquidity Developments***

We require capital to operate, to post deposits on new deals, to purchase and develop land, to construct homes, to fund related carrying costs and overhead and to fund various advertising and marketing programs to generate sales. These expenditures include payroll, community engineering, entitlement, architecture, advertising, utilities and interest as well as the construction costs of our homes. Our sources of capital include, and will continue to include, funds derived from private placement equity raises, various secured and unsecured borrowings to finance construction on acquired land, cash flow from operations, which includes the sale and delivery of constructed homes, rental apartment projects, finished and raw building lots and the sale of equity and debt securities.

The Company is involved in ongoing discussions with lenders in an effort to provide additional growth capital to fund various new business opportunities. In addition, on March 14, 2013, the Company, through its wholly-owned subsidiary Comstock Investors VII, L.C., entered into subscription agreements with certain accredited investors ( Comstock VII Investors ), pursuant to which the Comstock VII Investors purchased membership interests in the subsidiary for an initial aggregate principal amount of \$6,925, of an up to \$7,000 capital raise. Further, we have executed extensions and obtained new facilities to significantly reduce the debt obligations maturing in 2013. As of December 31, 2012, the maturities and curtailment obligations for 2013 was \$14,027, of which, the new facilities and extensions resulted in \$13,291 of the obligations with revised maturities beginning in 2015 and beyond. Refer to Note 20 for more details on the capital raise and changes to our credit facilities. We are anticipating that through a combination of the capital raised through the aforementioned private placement, current available cash on hand and additional cash from settlement proceeds at existing and under development communities, the Company will have sufficient financial resources to sustain our operations through the next 12 months, though no assurances can be made that we will be successful in our efforts.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

A summary of the significant accounting policies and practices used in the preparation of the consolidated financial statements is as follows:

***Basis of presentation***

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

The accompanying consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles ( GAAP ) and include the accounts of Comstock Holding Companies, Inc., a Delaware corporation, and all of its majority-owned and controlled subsidiaries. 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 control of the entity, in which case the entity would be consolidated. The Company had no investments accounted for using the equity method as of December 31, 2012 and 2011.

F-7

**Table of Contents*****Cash and cash equivalents and restricted cash***

Cash and cash equivalents are comprised of cash and short-term investments with maturities of three months or less when purchased. At times, the Company may have deposits with institutions in excess of federally insured limits. Banking institutions with which the Company does business are considered credit worthy; therefore, credit risk associated with cash and cash equivalents is considered low. At December 31, 2012 and 2011, the Company had restricted cash of \$3.2 million and \$3.1 million, respectively, which includes a \$3.0 million deposit with an insurance provider, to which we have no access currently, as security for future claims.

***Real estate held for development and sale***

Real estate held for development and sale includes land, land development costs, construction and other costs. Real estate held for development and use is stated at cost, or when circumstances or events indicate that the real estate is impaired, at estimated fair value. Real estate held for sale is carried at the lower of cost or fair value less estimated costs to sell. Land, land development and indirect land development costs are accumulated by specific project and allocated to various units within that project using specific identification and allocation based upon the relative sales value, unit or area methods. Direct construction costs are assigned to units based on specific identification. Construction costs primarily include direct construction costs and capitalized field overhead. Other costs are comprised of fees, capitalized interest and real estate taxes. Costs incurred to sell real estate are capitalized to the extent they are reasonably expected to be recovered from the sale of the project and are tangible assets or services performed to obtain regulatory approval of sales. Other selling costs are expensed as incurred.

If the project is considered held for sale, it is valued at the lower of cost or fair value less estimated selling costs. For assets held for development and use, estimated fair value is based on comparable sales of real estate in the normal course of business under existing and anticipated market conditions. The evaluation takes into consideration the current status of the property, various restrictions, carrying costs, costs of disposition and any other circumstances that may affect fair value including management's plans for the property. A write-down to estimated fair value is recorded when the net carrying value of the property exceeds its estimated undiscounted future cash flows. These evaluations are made on a property-by-property basis whenever events or changes in circumstances indicate that the net book value may not be recoverable.

***Capitalized interest and real estate taxes***

Interest and real estate taxes incurred relating to the development of lots and parcels are capitalized to real estate held for development and sale during the active development period, which generally commences when borrowings are used to acquire real estate assets and ends when the properties are substantially complete or the property becomes inactive. A project becomes inactive when development and construction activities have been suspended indefinitely. Interest is capitalized based on the interest rate applicable to specific borrowings or the weighted average of the rates applicable to other borrowings during the period. Interest and real estate taxes capitalized to real estate held for development and sale are expensed as a component of cost of sales as related units are sold. The following table is a summary of interest and real estate taxes incurred and capitalized and interest and real estate taxes expensed for units settled:

	<b>Years ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Total interest incurred and capitalized	\$ 351	\$ 320
Total real estate taxes incurred and capitalized	150	13
<b>Total interest and real estate taxes incurred and capitalized</b>	<b>\$ 501</b>	<b>\$ 333</b>
Interest expensed as a component of cost of sales	\$ 2,065	\$ 2,329
Real estate taxes expensed as a component of cost of sales	189	198
<b>Interest and real estate taxes expensed as a component of cost of sales</b>	<b>\$ 2,254</b>	<b>\$ 2,527</b>

When a project becomes inactive, its interest, real estate taxes and indirect production overhead costs are no longer capitalized but rather expensed in the period in which they are incurred. Following is a breakdown of the interest, real estate taxes and indirect costs related to inactive projects reported in real estate held for development and sale:

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

	Years ended December 31,	
	2012	2011
Total interest incurred and expensed for inactive projects	\$ 1,940	\$ 2,507
Total real estate taxes incurred and expensed for inactive projects	170	381
Total production overhead incurred and expensed for inactive projects	179	214
	2,289	3,102
Amounts reclassified to discontinued operations	(154)	(363)
	\$ 2,135	\$ 2,739

F-8



**Table of Contents*****Property, plant and equipment***

Property, plant and equipment are carried at cost less accumulated depreciation and are depreciated on the straight-line method over their estimated useful lives as follows:

Furniture and fixtures	7 years
Office equipment	5 years
Computer equipment and capitalized software	3 years
Leasehold improvements	Life of related lease

When assets are retired or otherwise disposed of, the cost and accumulated depreciation are removed from their separate accounts and any gain or loss on sale is reflected in operations. Expenditures for maintenance and repairs are charged to expense as incurred.

***Warranty reserve***

Warranty reserves for units settled are established to cover potential costs for materials and labor with regard to warranty-type claims expected to arise during the typical one-year warranty period provided by the Company or within the two-year statutorily mandated structural warranty period for condominiums. Since the Company typically subcontracts its homebuilding work, subcontractors are required to provide the Company with an indemnity and a certificate of insurance prior to receiving payments for their work. Claims relating to workmanship and materials are generally the primary responsibility of the subcontractors and product manufacturers. The warranty reserve is established at the time of closing, and is calculated based upon historical warranty cost experience and current business factors. This reserve is an estimate and actual warranty costs could vary from these estimates. Variables used in the calculation of the reserve, as well as the adequacy of the reserve based on the number of homes still under warranty, are reviewed on a periodic basis. Warranty claims are directly charged to the reserve as they arise. The following table is a summary of warranty reserve activity which is included in accounts payable and accrued liabilities:

	Years ended December 31,	
	2012	2011
Balance at beginning period	\$ 1,009	\$ 1,110
Additions	52	110
Releases and/or charges incurred	(98)	(211)
Balance at end of period	\$ 963	\$ 1,009

***Revenue recognition***

The Company recognizes revenues and related profits or losses from the sale of residential properties, including multiple units to the same buyer, finished lots and land sales when closing has occurred, full payment has been received, title and possession of the property has transferred to the buyer and the Company has no significant continuing involvement in the property. Other revenues include revenue from land sales, rental revenue from leased apartments which is recognized over the terms of the respective leases, revenue from construction services which is recognized under the percentage-of-completion method, and revenue earned from management and administrative support services provided to related parties which is recognized as the services are provided.

***Advertising costs***

The total amount of advertising costs charged to selling, general and administrative expense was \$168 and \$64 for the years ended December 31, 2012 and 2011, respectively.

***Stock compensation***

As discussed in Note 14, the Company sponsors stock option plans and restricted stock award plans. The Company accounts for its share-based awards pursuant to Accounting Standards Codification ( ASC ) 718, *Share Based Payments*. ASC 718 requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements over the vesting period based on their fair

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

values at the date of grant. For the year ended December 31, 2012 and 2011, total stock-based compensation cost was \$1,447 and \$932, respectively. Of this amount, \$1,447 and \$925 was charged to selling, general and administration expenses for the years ended December 31, 2012 and 2011, respectively.

### *Out-of-period adjustment*

During the fourth quarter of 2012, we identified an error in the consolidated financial statements for the year ended December 31, 2011 and the first three quarters of 2012. This error related to accounting for non-cash stock compensation expense. We concluded that this adjustment was not material to any prior periods' consolidated financial statements. We also concluded that the out-of-period correction of this error in 2012 was not material to the consolidated financial statements for the year ended December 31, 2012. As such, the cumulative effect of the error was recorded in the 2012 Consolidated Statement of Operations and the 2012 Consolidated Statement of Changes in Shareholders' Equity as an out-of-period adjustment. The effect of this adjustment was to increase the Company's net loss by \$176 for the year ended December 31, 2012 and to reduce the Class A Common Stock shares outstanding by \$3, or 317 shares.

F-9

**Table of Contents****Income taxes**

Income taxes are accounted for under the asset and liability method in accordance with ASC 740, Accounting for Income Taxes (ASC 740). Deferred tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on the deferred tax assets and liabilities is recognized in income in the period that includes the enactment date.

**Income (Loss) per share**

The weighted average shares and share equivalents used to calculate basic and diluted (loss) income per share for the year ended December 31, 2012 and 2011, are presented on the consolidated statement of operations. Stock options and warrants for the year ended December 31, 2012 and 2011 are included in the diluted earnings per share calculation using the treasury stock method and average market prices during the period, unless the stock option and warrants would be anti-dilutive. As a result of net losses from continuing operations for the year ended December 31, 2012, approximately 388 restricted stock awards, 196 stock options and 428 warrants were excluded from the computation of diluted earnings per share because their inclusion would have been anti-dilutive. For the year ended December 31, 2011, approximately 170 and 263 of stock options and warrants, respectively, were included in the computation of diluted earnings per share. The computation of basic and diluted shares outstanding is as follows:

	<b>Year Ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
<b>Computation of weighted-average basic shares outstanding:</b>		
Weighted average basic shares outstanding	19,970	20,287
<b>Computation of weighted average diluted shares outstanding:</b>		
Weighted-average basic shares outstanding	19,970	20,287
Dilutive effect of stock options		170
Dilutive effect of restricted stocks		
Dilutive effect of warrants		263
Weighted average common shares outstanding    diluted	19,970	20,720

**Comprehensive income**

For the years ended December 31, 2012 and 2011, comprehensive income equaled net income; therefore, a separate statement of comprehensive income is not included in the accompanying consolidated financial statements.

**Segment reporting**

We operate our business through three segments: Homebuilding, Apartment Buildings and Real Estate Services. We are currently focused on the Washington, D.C. market.

For our Homebuilding operations, we develop properties with the intent that they be sold either as fee-simple properties or condominiums to individual unit buyers or as investment properties sold to private or institutional investors. Our for-sale products are designed to attract first-time, early move-up, and secondary move-up buyers. We focus on products that we are able to offer for sale in the middle price points within the markets where we operate, avoiding the very low-end and high-end products.

For our Apartment Buildings segment we focus on projects ranging from approximately 75 to 200 units in locations that are supply constrained with demonstrated demand for stabilized assets. We seek opportunities in the multi-family rental market where our experience and core capabilities can be leveraged. We will either position the assets for sale when completed or operate the asset within our own portfolio. Operating the asset for our own account affords us the flexibility of converting the units to condominiums in the future.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Our Real Estate Services segment pursues projects in all aspects of real estate management including strategic planning, land development, entitlement, property management, sales and marketing, workout and turnaround strategies, financing and general construction. We are able to provide a wide range of construction management and general contracting services to other property owners.

F-10

**Table of Contents**

The following disclosure includes the Company's three reportable segments of Homebuilding, Apartment Buildings and Real Estate Services. Each of these segments operates within the Company's single Washington, D.C. reportable geographic segment. The information for 2011 has been reclassified to conform to current year business segment presentation and to reflect the reclassification of operations derived from the Cascades II sale as discontinued operations. Refer to Note 16 for further discussion.

	(in thousands)			
	Homebuilding	Apartment Buildings	Real Estate Services	Total
<b>Twelve Months Ended December 31, 2012</b>				
Gross revenue (1)	\$ 12,043	\$	\$ 2,259	\$ 14,302
Gross income	724		402	1,126
Net (loss) income from continuing operations	(12,285)		278	(12,007)
Net income from discontinued operations		6,368		6,368
Net (loss) income	(12,285)	6,368	278	(5,639)
Total assets	36,378	278	2,043	38,699
Depreciation and amortization	1,487			1,487
Interest expense	1,775			1,775
Capital expenditures	158			158
<b>Twelve Months Ended December 31, 2011</b>				
Gross revenue (1)	\$ 15,354	\$	\$ 6,579	\$ 21,933
Gross income	1,686		653	2,339
Net income from continuing operations	1,729		429	2,158
Net loss from discontinued operations		(527)		(527)
Net income (loss)	1,696	(527)	429	1,598
Total assets	31,964	12,695	1,720	46,379
Depreciation and amortization	955	173		1,128
Interest expense	2,180	327		2,507
Capital expenditures	55	9,764	23	9,842

(1) Gross revenue includes Revenue homebuilding and Revenue other as described in the consolidated income statement for assets included in each segment.

The Company allocates selling general and administrative expenses to the individual segments based upon specifically allocable costs and, in the absence of direct allocations, based upon its estimate of time allocable to the segment or based upon overall pro rata revenue generation.

The table below reconciles the segment information to the corresponding amounts in the Consolidated Statements of Operations:

	Twelve Months Ended December 31,	
	2012	2011
Segment operating (loss) income from continuing operations	\$ (12,007)	\$ 2,158
Income tax benefit (expense)	2,484	(33)
Income (loss) from continuing operations	\$ (9,523)	\$ 2,125
Segment operating income (loss) from discontinued operations	\$ 6,368	\$ (527)
Income tax expense	(2,484)	

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Income (loss) from discontinued operations	\$ 3,884	\$ (527)
--	----------	----------

F-11

---

## **Table of Contents**

### ***Use of estimates***

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts in the financial statements and accompanying notes. Actual results could differ from those estimates. Material estimates are utilized in the valuation of real estate held for development and sale, valuation of deferred tax assets, capitalization of costs, consolidation of variable interest entities and warranty reserves.

### ***Recent accounting pronouncements***

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standard (IFRS), which provides a consistent definition of fair value and ensures that the fair value measurement and disclosure requirements are similar between U.S. GAAP and IFRS. The guidance changes certain fair value measurement principles and expands the disclosure requirements, particularly for Level 3 fair value measurements. The guidance was effective for the Company beginning February 1, 2012 and is applied prospectively. The adoption of this guidance, which relates primarily to disclosure, did not have a material impact on our Consolidated Financial Statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, Statement of Comprehensive Income (ASU2011-05), which requires entities to present net income and other comprehensive income in either a single continuous statement or in two separate, but consecutive, statements of net income and other comprehensive income. The guidance was effective for the Company beginning January 1, 2012 and is applied prospectively. The adoption of this guidance did not have a material impact on our Consolidated Financial Statements.

### **3. CONSOLIDATION OF VARIABLE INTEREST ENTITIES**

GAAP requires a variable interest entity (VIE) to be consolidated by the company that is the primary beneficiary. The primary beneficiary of a VIE is the entity that has both of the following characteristics: (a) the power to direct the activities of a VIE that most significantly impact the VIE's economic performance and (b) the obligation to absorb losses of the VIE that could potentially be significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE. Entities determined to be VIEs, for which we are not the primary beneficiary, are accounted for under the equity method. Comstock's variable interests in VIEs may be in the form of (1) equity ownership, (2) contracts to purchase assets and/or (3) loans provided and or guaranteed to a VIE. We examine specific criteria and use judgment when determining if Comstock is the primary beneficiary of a VIE. Factors considered in determining whether we are the primary beneficiary include risk and reward sharing, experience and financial condition of other partner(s), voting rights, involvement in day-to-day capital and operating decisions and contracts to purchase assets from VIEs.

#### **Consolidated Real Estate Held for Development and Sale**

Included within the Company's real estate held for development and sale at December 31, 2012 are four wholly-owned entities that are VIEs and for which the Company is the primary beneficiary; Penderbrook, Potomac Yard, Yorkshire and Redland Road. These entities have been established to own and operate real estate property and were deemed VIEs primarily based on the fact that the equity investment at risk is not sufficient to permit the entities to finance their activities without additional financial support. The Company determined that it was the primary beneficiary of these VIEs as a result of its majority voting and complete operational control of the entities.

On August 23, 2012, the Company formed New Hampshire Ave. Ventures, LLC, a joint venture of its subsidiary, Comstock Ventures XVI, L.C, and 6000 New Hampshire Avenue, LLC, for the purpose of acquiring, developing and constructing a 111-unit project (the NHA Project) in Washington, D.C. The Company evaluated the joint venture and determined that it was a VIE concluding that the equity investment at risk is not sufficient to permit the entity to finance its activities without additional financial support. The Company determined that it was the primary beneficiary of the VIE as a result of its shared voting interests, complete operational control of the activities that most significantly impact the VIE's economic performance and its obligation to absorb losses, or receive benefits, from the VIE that could be significant to the VIE.

On September 27, 2012, the Company formed Comstock Eastgate, L.C., a joint venture of Comstock Holding Companies, Inc. and BridgeCom Development II, LLC, for the purpose of acquiring, developing and constructing 66 condominium units (the Eastgate Project) in Loudoun County, Virginia. The Company evaluated the joint venture and determined that it was a VIE concluding that the equity investment at risk is not sufficient to permit the entity to finance its activities without additional financial support. The Company determined that it was the primary beneficiary of the VIE as a result of its complete operational control of the activities that most significantly impact the VIE's economic performance and its obligation to absorb losses, or receive benefits, from the VIE that could be significant to the VIE.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

At December 31, 2012 and December 31, 2011, total assets of these VIEs were approximately \$29.4 million and \$22.0 million, respectively, and total liabilities were approximately \$17.4 million and \$11.1 million, respectively. The classification of these assets is primarily within real estate held for development and sale and the classification of liabilities are primarily within notes payable secured by real estate held for development and sale in the Company's consolidated balance sheets.

F-12



---

**Table of Contents**

**Consolidated Operating Real Estate, Net**

On January 31, 2011, Comstock Cascades II, L.C., a subsidiary of the Company ( Cascades II ), entered into a private placement for the sale of membership interests in Cascades II whereby Cascades II raised working capital in the amount of \$2.35 million (the Private Placement ) related to the planned construction of a 103 unit apartment project located in the Cascades master planned community in Loudoun County, Virginia (the Cascades Apartments ). Proceeds of the Private Placement were utilized (i) to provide sufficient capital needed to secure project financing for the Cascades Apartments, (ii) to retire a portion of the existing indebtedness, and (iii) to reimburse the Company for prior expenditures incurred on behalf of the project. Participants in the Private Placement included unrelated third party investors along with several members of the Company s Board of Directors, as well as the Chief Operating Officer, Chief Financial Officer and General Counsel of the Company.

On February 11, 2011, Comstock closed its loan agreement with Cardinal Bank (see Note 9) which provided the necessary construction financing for the development of the Cascades Apartments and concurrent with that closing, the Company utilized the proceeds of the Private Placement offering as described above. The Company fully guaranteed the loan and accordingly, Comstock concluded that Cascades II was a VIE. As part of the Cascades II operating agreement, the Company had majority voting and complete operational control of the subsidiary. The Company concluded that it was the primary beneficiary of the VIE and therefore the financial condition, results of operations and cash flows of Cascades II were consolidated in the accompanying financial statements.

The investors in the Private Placement (the Priority Members ) were entitled to a cumulative, compounded, preferred return, subject to the performance of Cascades II, of 20% per annum, compounded annually on their capital account balances. Comstock had the right to repurchase the interest of the Priority Members provided that i) all of the Priority Members interests were acquired, ii) the purchase was made in cash and iii) the purchase price shall equal the Priority Members capital account plus an amount necessary to cause the preferred return to equal a cumulative cash on cash return equal to 20% per annum. The equity contribution related to the Private Placement is reflected as a Non-Controlling Interest as a component of consolidated shareholders equity. The Company s investment was subordinate to the Priority Members investment and gains from the operating activity and distributions of cash flow (if any) of Cascades II would allocate to the Priority Members (in advance of Comstock) up to their capital account plus the required preferred return of 20% as outlined above. For the year ended December 31, 2012 and 2011, the priority returns were approximately \$103 and \$491, respectively. The priority returns are reflected in the accompanying consolidated statement of operations as net income from discontinued operations attributable to non-controlling interests to properly account for the preferred return due the Priority Members upon liquidation of their interest in Cascades II.

On March 7, 2012, the Company completed the sale of the Cascades Apartments (the Project ) to an affiliate of CAPREIT Acquisition Corporation ( Purchaser ), a Maryland corporation, pursuant to a Contract of Sale Agreement, as amended, dated October 31, 2011. The Project was sold for \$19.35 million. In connection with the closing of the transaction, Cascades II placed in escrow \$300 (the Warranty Escrow ) to secure performance of certain post-closing warranty work and \$650 (the Claims Escrow ) to secure Cascades II s indemnification and other obligations set forth in the Agreement. The Warranty Escrow was agreed to be released to Cascades upon completion of the post-closing warranty work and the Claims Escrow was agreed to be released to Cascades in three equal installments at six, eight and twelve months from the date of settlement provided that no claims have been made against Cascades by the Purchaser. On September 6, 2012, the Purchaser released the \$300 Warranty escrow, net of \$2 in settlement costs, and one-third of the Claims Escrow, \$217, net of \$35 of post-closing warranty claims. On November 26, 2012, the Purchaser released the second installment, one-third of the remaining Claims Escrow, \$143. As detailed in Note 9, the historical operations of Cascades Apartments are included within discontinued operations.

Concurrent with the execution of the sale transaction, Cascades II settled the secured financing of \$10.1 million with Cardinal Bank, including all principal and interest due at the time of settlement, and retired the non-controlling equity investment, including all preferred returns due. The Company realized a loss on the extinguishment of the secured financing with Cardinal Bank of \$0.3 million, including the prepayment penalty fees of \$0.2 million. At settlement, the Company received net proceeds of approximately \$4.7 million from the transaction after repayment of the existing loan from Cardinal Bank secured by the Project and the retirement of the non-controlling equity investment related to the Project.

Concurrent with the settlement of the secured financing, retirement of non-controlling equity investment holders and the release of the Company s corporate guaranty, the Company determined a reconsideration event under ASC 810 had occurred and concluded the entity no longer met the definition of a VIE as defined by the standard. The Company further noted that the Company has retained the controlling financial interest in Cascades II and has continued to consolidate the subsidiary.

**Land purchase options**

The Company typically acquires land for development at market prices under fixed price purchase agreements. The purchase agreements require deposits that may be forfeited if the Company fails to perform under the agreements. The deposits required under the purchase agreements are in the form of cash or letters of credit in varying amounts. The Company may, at its option, choose for any reason and at any time not to perform under these purchase agreements by delivering notice of its intent not to acquire the land under contract. The Company s sole legal obligation and

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

economic loss for failure to perform under these purchase agreements is typically limited to the amount of the deposit pursuant to the liquidated damages provision contained within the purchase agreement. As a result, none of the creditors of any of the entities with which the Company enters into forward fixed price purchase agreements have recourse to the general credit of the Company.

F-13

**Table of Contents**

The Company does not share in an allocation of either the profit earned or loss incurred by any of these entities with which the Company has fixed price purchase agreements. The Company has concluded that whenever it options land or lots from an entity and pays a significant non-refundable deposit as described above, a variable interest entity is created under the provisions of ASC 810-10, *Consolidation*. This is because the Company has been deemed to have provided subordinated financial support, which creates a variable interest which limits the equity holder's returns and may absorb some or all of an entity's expected theoretical losses if they occur. The Company, therefore, examines the entities with which it has fixed price purchase agreements for possible consolidation by the Company under the provision of ASC 810-10. The Company does not have any contractual or ownership interests in the entities with which it contracts to buy the land. The Company concluded that it does not have the power to direct the activities that most significantly impact the economic performance of the VIEs, including the power to site plan and engineer the developments, finance the parcels under option contract, and develop the raw parcels under option contract into finished lots. The third party retains these rights under the fixed purchase price agreements until title is transferred to the Company upon settlement of the transaction, or a portion of the transactions as defined. Therefore, the Company has not consolidated these VIEs in the consolidated balance sheet.

**4. REAL ESTATE HELD FOR DEVELOPMENT AND SALE**

Real estate held for development and sale includes land, land development costs, construction and other costs. Real estate held for development and use is stated at cost, or when circumstances or events indicate that the real estate is impaired, at estimated fair value. Real estate held for sale is carried at the lower of cost or fair value less estimated costs to sell. Land, land development and indirect land development costs are accumulated by specific project and allocated to various units within that project using specific identification and allocation based upon the relative sales value, unit or area methods. Direct construction costs are assigned to units based on specific identification. Construction costs primarily include direct construction costs and capitalized field overhead. Other costs are comprised of fees, capitalized interest and real estate taxes. Costs incurred to sell real estate are capitalized to the extent they are reasonably expected to be recovered from the sale of the project and are tangible assets or services performed to obtain regulatory approval of sales. Other selling costs are expensed as incurred.

If the project is considered held for sale, it is valued at the lower of cost or fair value less estimated selling costs. For assets held for development and use, estimated fair value is based on comparable sales of real estate in the normal course of business under existing and anticipated market conditions. The evaluation takes into consideration the current status of the property, various restrictions, carrying costs, costs of disposition and any other circumstances that may affect fair value including management's plans for the property. A write-down to estimated fair value is recorded when the net carrying value of the property exceeds its estimated undiscounted future cash flows. These evaluations are made on a property-by-property basis whenever events or changes in circumstances indicate that the net book value may not be recoverable.

The Company has classified its Eclipse and Penderbrook projects as held for sale and accordingly, carries the projects at fair value less costs to sell as determined by discounted cash flow models, by reference to comparable market transactions, or relevant purchase offers. Discounted cash flow models are dependent upon several subjective factors, including estimated average sales prices, estimated sales pace, and the selection of an appropriate discount rate. The estimates of sales prices, sales pace and discount rates used by the Company are based on the best information available at the time the estimates are made.

In 2012, management evaluated its strategic alternatives with respect to its real estate projects classified as held for sale with the objective of creating additional near term liquidity. As a result, a decision was made to market the Potomac Yard project in a bulk sale transaction, rather than by selling directly to prospective home buyers, significantly accelerating absorption. The impairment charge of \$2,358 for the year ended December 31, 2012, reflects the write down to estimated fair value less costs to sell under the revised disposition strategy, however, there can be no assurance that the Company will be successful in the sale of the Potomac Yard project in a bulk sale and in the absence thereof, the Company will continue selling to prospective home buyers. The Company recorded an impairment charge of \$2,358 during the year ended December 31, 2012, to properly record its for sale projects at fair market value less costs to sell, consistent with the provisions of ASC 360. There were no impairment charges recorded during the year ended December 31, 2011.

After impairments and write-offs, real estate held for development and sale consists of the following:

	<b>December 31,</b>	
	<b>2012</b>	<b>2011</b>
Land and land development costs	\$ 19,378	\$ 4,693
Cost of construction (including capitalized interest and real estate taxes)	8,403	16,519

\$ 27,781      \$ 21,212

F-14

**Table of Contents****5. OPERATING REAL ESTATE, NET**

In February 2011, the Company began construction on a 103-unit apartment rental project located in the Cascades master planned community in Loudoun County, Virginia (the Cascades Apartments). Accordingly, upon the initiation of construction, the value of the existing land upon which the project was constructed (approximately \$2.5 million) was reclassified from real estate held for development and sale to operating real estate, net. The total construction costs capitalized in addition to the land and land development costs were approximately \$9.8 million. The apartment project consisted of two buildings, the first of which was placed into service in July 2011 and the second of which was placed in service in September 2011. As further discussed in Note 9, the Cascades Apartments were sold on March 7, 2012 and accordingly, the results of operations are included in Net income (loss) on discontinued operations in 2012 and 2011.

Depreciation was calculated on buildings and improvements at the Cascades Apartments using the straight-line method over estimated useful lives, which ranged from seven to thirty years. Furniture, fixtures and equipment were depreciated using the straight-line method over estimated useful lives, which range from three years (primarily computer-related equipment) to seven years. Depreciation of \$82 was recorded for the year ended December 31, 2012 and depreciation of \$173 was recorded for the year ended December 31, 2011 and is reflected in segment reporting Note 2 and in discontinued operations on the Consolidated Statement of Operations. Operating real estate consisted of the following:

	December 31,	
	2012	2011
Land	\$	\$ 2,815
Building and improvements		9,453
		12,268
Less: accumulated depreciation		(173)
	\$	\$ 12,095

**6. PROPERTY, PLANT AND EQUIPMENT, NET**

Property, plant and equipment consist of the following:

	December 31,	
	2012	2011
Computer equipment and capitalized software	\$ 199	\$ 1,840
Furniture and fixtures	106	82
Office equipment	58	84
Leasehold improvements		15
	363	2,021
Less: accumulated depreciation	(141)	(1,916)
	\$ 222	\$ 105

Depreciation and amortization expense, included in selling, general, and administrative in the consolidated financial statements of operations, amounted to \$41 and \$23 for the years ended December 31, 2012 and 2011, respectively.

**7. OTHER ASSETS**

Other assets consist of the following:

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

	<b>December 31,</b>	
	<b>2012</b>	<b>2011</b>
Restricted escrow deposits	\$ 570	\$ 483
Deferred financing costs	1,148	1,679
Deposits on land purchase options	820	420
Other	106	48
	<b>2,644</b>	<b>2,630</b>
Less: accumulated amortization	(301)	(612)
	<b>\$ 2,343</b>	<b>\$ 2,018</b>

F-15

**Table of Contents****8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

Accounts payable and accrued liabilities consist of the following:

	December 31,	
	2012	2011
Trade payables	\$ 3,511	\$ 2,910
Warranty	963	1,009
Customer deposits	206	63
Other	6	5
	\$ 4,686	\$ 3,987

**9. MORTGAGES AND CREDIT FACILITIES**

The Company generally finances its development and construction activities on a single or multiple project basis so it is not uncommon for each project or collection of projects the Company develops and builds to have a separate credit facility. Accordingly, the Company typically has had numerous credit facilities and lenders. As described in more detail below, our outstanding debt by lender was as follows:

<b>Bank</b>	<b>Balance as of 12/31/12</b>	<b>Balance as of 12/31/11</b>	<b>Recourse</b>
SunBridge, net of \$0.0 million and \$0.6 million discount, respectively	\$	\$ 10,178	Secured
Cardinal Bank	636	9,957	Secured
Bank of America	3,096	3,751	Unsecured
Cornerstone (Haven Trust)		400	Unsecured
Branch Banking & Trust	263	263	Secured
Wachovia		133	Unsecured
Seller Emerald Farm	100	100	Secured
Fifth Third		25	Unsecured
Eagle Bank Potomac Yard / Penderbrook	4,084		Secured
Eagle Bank New Hampshire Ave.	3,159		Secured
Eagle Bank Redland Road	2,500		Secured
Rosalie K. Stahl Trust	3,000		Secured
TSR-Shady Grove, LLC.	5,750		Secured
	22,588	24,807	
Due to affiliates Stonehenge Funding	5,041	5,008	Unsecured
Total	\$ 27,629	\$ 29,815	

The material loan agreements are discussed below.

*Eagle Bank*

On May 29, 2012, the Company, through its Comstock Potomac Yard, L.C. and Comstock Penderbrook, L.C. subsidiaries, entered into a loan agreement with Eagle Bank pursuant to which the Company secured a \$9.96 million loan with a twenty-seven months term (the Eagle Bank Loan ) to refinance the Company's Eclipse condominium project and Penderbrook Square condominium project. Proceeds from the Eagle Bank

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Loan were primarily utilized (i) to pay off existing indebtedness of approximately \$7.97 million, (ii) set up an interest reserve escrow pursuant to the term of agreement in the amount \$0.5 million, (iii) pay approximately \$0.1 million in settlement charges and closing costs, and (iv) for general corporate purpose. The interest reserve escrow is held in the name of the bank and if the borrower defaults under the loan agreement, the bank has sole discretion to apply the funds or portion of the funds to pay off the indebtedness. Commencing thirty days after closing, the Company is required to make monthly payments of interest only on outstanding principal balance, principal curtailment payments upon settlements at the two subsidiaries and a minimum principal curtailment payment of \$4.98 million no later than 12 months following the closing of the Eagle Bank Loan. There is no prepayment penalty associated with the Eagle Bank Loan. The balance outstanding at December 31, 2012 was \$4.08 million.

F-16



## Table of Contents

On August 23, 2012, the Company, through New Hampshire Ave. Ventures, LLC, a consolidated joint venture of its subsidiary Comstock Ventures XVI, L.C. and 6000 New Hampshire Avenue, LLC, entered into a three-year loan agreement and related documents with Eagle Bank securing a \$6.0 million revolving development loan and a \$4.0 million revolving construction loan (collectively, the Eagle NHA Revolver ) to finance The Hampshires, the Company's 111-unit project located in Washington, D.C. Proceeds from the Eagle NHA Revolver will primarily be utilized to (i) pay for expenses associated with the Eagle NHA Revolver; (ii) reimburse the Company for development costs previously expended and (iii) to pay for the future development and construction related expenses. Under the terms of the Loan Agreement, the Eagle NHA Revolver provides for an initial floating interest rate of LIBOR plus 3% with an interest rate floor of 5.75%. The New Hampshire Ave. Ventures, LLC is required to make monthly interest payments on the Eagle NHA Revolver to the extent not offset by a \$400 interest reserve initially set aside for the benefit of the Borrower and is required to make a minimum principal curtailment under the development portion of the Eagle NHA Revolver of \$3.22 million by December 31, 2013 and additional curtailments on a quarterly basis thereafter. There is no prepayment penalty associated with the Eagle NHA Revolver, which is secured by a first deed of trust and is fully guaranteed by the Company. The balance outstanding at December 31, 2012 was \$3.16 million.

On December 27, 2012, the Company, through Comstock Redland Road, L.C. subsidiary, entered into acquisition bridge loan (the Bridge Loan ) with Eagle Bank, pursuant to which the Company secured \$2.5 million to finance the Company's acquisition of the property directly adjacent to the Shady Grove Metro in Rockville, Montgomery County, Maryland. The Company utilized the proceeds from the Eagle Bank Loan (the Bridge Loan ) to (i) pay for the acquisition of land planned for development of 36 townhomes, 3 single family, and a 117-unit multi-family apartments and (ii) to pay for expenses associated with settlement charges and closing costs. Under the terms of the loan agreement, the Bridge Loan provides for an interest rate of 5% per annum. The Company is expected to make monthly interest payments commencing thirty days after closing, with entire principal balance due March 27, 2013. The loan is secured by a promissory note, second deed of trust and security agreement on the property, second deed of trust and security agreement on the Potomac Yard project, a guaranty of Comstock Holding Companies, Inc., Comstock Potomac Yard, L.C. and Christopher Clemente, the Chief Executive Officer of Comstock Holding Companies, Inc. and other ancillary documents (collectively, the Bridge Loan Documents ). There is no prepayment penalty associated with the Bridge Loan. The amount outstanding at December 31, 2012 was \$2.5 million. The Bridge Loan was repaid in full on March 25, 2012 as further described in Note 20 to the consolidated financial statements.

### *SunBridge*

On July 12, 2011, the Company, through its Comstock Potomac Yard, L.C. subsidiary, entered into a loan agreement with BCL Eclipse, LLC, an affiliate of SunBridge Capital Management, LLC ( SunBridge ), pursuant to which the Company secured a \$13.8 million loan with a three year term (the SunBridge Eclipse Loan ) to refinance the Company's Eclipse condominium project. Proceeds from the SunBridge Eclipse Loan were primarily utilized to (i) pay off existing indebtedness of approximately \$9.0 million, (ii) pay approximately \$0.8 million for expenses associated with the SunBridge Eclipse Loan (which were classified in Other assets in the accompanying balance sheet), and (iii) for general corporate purposes. The SunBridge Eclipse Loan provided for a 1% origination fee and an interest rate of 12.5%. There was no prepayment penalty associated with the SunBridge Eclipse Loan, which was secured by a first deed of trust on the Eclipse property. The loan was subject to minimum sales and release requirements.

On July 12, 2011, SunBridge also issued a binding commitment letter to the Company, through its Comstock Penderbrook, L.C. subsidiary, for a cash out refinance of the Company's Penderbrook Square condominium projected in an amount of up to \$7.0 million with a three-year term (the SunBridge Penderbrook Loan ). This commitment was drawn upon on October 5, 2011 and the loan was funded for approximately \$5.4 million. Proceeds from this loan were primarily utilized to (i) pay off existing indebtedness of approximately \$3.9 million, (ii) pay for expenses associated with the loan of approximately \$0.7 million, and (iii) for general corporate purposes.

As a condition of the loan agreement, the Company also entered into a cross-collateralization agreement whereby the Penderbrook project and the Eclipse project each secured payment and performance of the covenants and agreements of the October 5, 2011 SunBridge Penderbrook Loan and the loan funded on July 12, 2011 with respect to the Eclipse project as described above. The SunBridge Penderbrook Loan provided for a 1% origination fee and an interest rate of 12.5%. There was no prepayment penalty associated with the SunBridge Penderbrook Loan, which was secured by a first deed of trust on the property. The loan was subject to minimum sales and release requirements.

On October 5, 2011, the Company and a subsidiary of the Company, Comstock Emerald Farm, L.C., as guarantors, also entered into a guaranty agreement for the benefit of SunBridge. Pursuant to the guaranty agreement, (i) the guarantors jointly and severally guaranteed the payment of principal and interest and any other amounts due under the SunBridge Penderbrook Loan Agreement, (ii) the Company pledged its equity interest in Comstock Penderbrook, L.C., and (iii) each guarantor granted SunBridge a security interest in all of its unencumbered assets, all as additional security for the SunBridge Penderbrook Loan.

On May 29, 2012, the Company repaid the SunBridge loans in full. All cash paid to satisfy the extinguishment of the SunBridge Loans is classified as a financing activity in the consolidated statement of cash flows.



**Table of Contents***Cardinal Bank*

On February 11, 2011, the Company, through Cascades II entered into a loan agreement with Cardinal Bank pursuant to which the Company obtained an \$11.0 million multi-family construction loan and mortgage with a five-year term (the Cardinal Bank Loan ). Proceeds from the Cardinal Bank Loan (i) funded the construction of the Company's Cascades apartment project and (ii) retired existing indebtedness of the Company owed to M&T Bank having a maturity date of February 14, 2011 and which was secured by a first deed of trust on the real property upon which the Cascades project was constructed. The Cardinal Bank Loan, secured by a new first deed of trust on the property, had an initial interest rate of Prime plus two percent (2%), with an interest rate floor of 6.5%. The Cardinal Bank Loan was amortized in accordance with a 5.5%, 25-year schedule, with amortization to begin 18 months after the loan closing and had a 2% prepayment penalty if paid within the first or second year and a 1% prepayment penalty if retired in the third or fourth year. The Company had fully guaranteed the Cardinal Bank Loan. The Chief Executive Officer of the Company and the Chief Operating Officer of the Company also provided a limited guaranty in connection with the Cardinal Bank Loan of up to \$6.8 million, subject to further reduction upon the satisfaction of certain enumerated conditions set forth in the loan agreement (see Note 12). On March 7, 2012, the Company sold the Cascades Apartments and the Cardinal Bank Loan was repaid in full. A prepayment penalty of \$0.2 million was incurred in connection with the early repayment and is included in discontinued operations gain on sale of real estate in the consolidated statement of operations. All cash paid to satisfy the extinguishment of the Cardinal Bank Loan is classified as a financing activity in the statement of cash flows.

On September 27, 2012, the Company, through Comstock Eastgate, L.C. ( Eastgate ), a consolidated joint venture of Comstock Holding Companies, Inc. and BridgeCom Development I, LLC, entered into a loan agreement with Cardinal Bank to which the Company secured a \$2.5 million revolving construction loan (the Cardinal Bank Revolver ) to finance The Villas at Eastgate, the Company's 66-unit project located in Loudoun County, VA. The loan maturity is twelve months from origination, with an automatic extension of twelve months subject to the Company meeting sales conditions, which include (i) entering into binding contracts for the sale of eighteen units and (ii) settling twelve units, each by the one year anniversary of the loan. The proceeds of Cardinal Bank Revolver will be primarily utilized to pay expenses associated with the loan and future construction expenses of the project. The Cardinal Bank Revolver provides for a variable interest rate of Prime plus 0.5%, with an interest rate floor of 4.75%. Commencing thirty days after loan close, the Company is required to make monthly payments of interest only and upon the closing of the sale of a unit, make principal curtailment payments of 100% of unit costs borrowed. There is no prepayment penalty associated with the Cardinal Bank Revolver.

*Bank of America*

At December 31, 2012, the Company had \$3.10 million outstanding to Bank of America under a 10-year unsecured note. On February 25, 2010 the Company entered into a Seventh Loan Modification Agreement with Bank of America regarding the modification of the terms of this loan. In connection therewith the Company agreed to pay an extension fee of \$100 and Bank of America agreed to delay until January 2011 the commencement of repayments of all previously unpaid interest accruing since the date of the Company's previously reported modification of the line of credit in November 2008. On February 1, 2011, the Company entered into the Eighth Loan Modification Agreement with Bank of America. The modification required payments of past interest and modification fees of approximately \$175 on February 1, 2011, which were paid in accordance with the agreement. The maturity date remains December 28, 2018. Comstock is required to make monthly interest payments beginning on February 28, 2011 through loan maturity. Commencing January 28, 2012 and continuing on each and every month through November 28, 2018, Comstock is also required to make monthly principal payments of approximately \$37.

*Rosalie K. Stahl Trust*

On August 23, 2012, the Company, through New Hampshire Ave. Ventures, LLC, a consolidated joint venture of its subsidiary Comstock Ventures XVI, L.C. and 6000 New Hampshire Avenue, LLC, also entered into a \$3.0 million mezzanine loan (the NHA Mezzanine Loan ) in connection with the The Hampshires project with the Rosalie K. Stahl Trust. Proceeds from the NHA Mezzanine Loan, which has a three-year maturity date, were utilized to acquire the land for development of the project. The NHA Mezzanine Loan provides for an interest rate of 13.5% per annum, interest to be paid current on a monthly basis, with the full principal balance being due at maturity. The NHA Mezzanine Loan is secured by a second deed of trust which is fully subordinate to the Eagle NHA Revolver and is non-recourse to the Company. There is no prepayment penalty associated with the NHA Mezzanine Loan.

*TSR-Shady Grove, LLC*

On December 27, 2012, the Company, through the Comstock Redland Road, L.C. subsidiary, entered into a Deferred Purchase Money Promissory Note with TSR-Shady Grove, LLC, a Maryland Limited liability company, pursuant to which the Company secured \$5.75 million for the acquisition of land planned for development of 36 town houses, 3 single family and a 117-unit multi-family apartments. The TSR-Shady Grove Loan provides for an interest rate of 6% per annum, interest is payable commencing thirty days after closing, with entire principal balance due March 28, 2013. However, pursuant to the Purchase and Sale Agreement (the Purchase Agreement ), no interest shall accrue until the

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

property is vacated. The TSR-Shady Grove Loan is secured by a deferred purchase money first deed of trust. There is no prepayment penalty associated with Redland Grove Loan. The balance outstanding at December 31, 2012 was \$5.75 million. The Deferred Purchase Money Promissory Note was repaid in full on March 25, 2012 as further described in Note 20 to the consolidated financial statements.

F-18

**Table of Contents**

*Stonehenge*

On December 23, 2009, Stonehenge Funding, LC ( Stonehenge ), an entity wholly-owned by the Chief Executive Officer of the Company, completed the purchase of a senior unsecured note (the JP Morgan Debt ) from JP Morgan Ventures ( JPMV ) in the then outstanding amount of approximately \$9.0 million, plus accrued and unpaid interest. The purchase of the JP Morgan Debt resulted in the transfer to Stonehenge of a warrant previously issued to JPMV for the purchase of 1.5 million shares of the Company s Class A Common Stock with a strike price of \$0.07 per share (the JP Morgan Warrant ). The Company s Chief Operating Officer subsequently purchased a participation interest in the JP Morgan Debt and the JP Morgan Warrant from Stonehenge. On February 12, 2010 the Company entered into a modification agreement to modify the terms of the Company s senior unsecured note with Stonehenge (the Modification Agreement ). Under the terms of the Modification Agreement, Stonehenge agreed to forgive \$4.5 million of the principal balance due from the Company under the JP Morgan Debt, reducing the principal balance by 50% to \$4.5 million. Stonehenge also agreed to forgive an additional amount due from the Company of approximately \$875, representing all past due interest, late fees and penalties accruing through December 31, 2009 under the JP Morgan Debt. Stonehenge further agreed to reduce the interest rate, effective January 1, 2010, by 50% to 300 basis points above the one year LIBOR on a floating basis. In addition, to ensure the Company s ability to comply with certain restrictions placed upon the Company by KeyBank and Guggenheim in connection with previously announced loan modifications enhancing cash flow to the Company, Stonehenge agreed to allow all future interest payments due from the Company under the JP Morgan Debt to accrue until at least 90 days after KeyBank and Guggenheim have been fully repaid. In connection therewith, Stonehenge may, on a quarterly basis, elect to accept stock of the Company (or warrants for the purchase thereof) with a cumulative value equal to the value of the scheduled interest payment in lieu of accruing a future quarterly interest payment. For the year ended December 31, 2011, no elections were made and no warrants were issued under the agreement. The KeyBank debt was fully repaid on February 2, 2011. The Guggenheim debt was fully repaid upon funding of the SunBridge Penderbrook Loan on October 5, 2011.

Further, the Modification Agreement provided for the elimination or forbearance upon the enforcement of all financial covenants contained in the JP Morgan Debt and all previously reported covenant violations by the Company. Stonehenge, as a condition of the new financing arrangement with SunBridge, agreed to subordinate its loan and delay principal and interest payments until the SunBridge loans on both Eclipse and Penderbrook are fully repaid. Concurrent with the repayment of the Sunbridge loans on May 29, 2012, the subordination agreement expired. On July 24, 2012, the Company and Stonehenge entered into an agreement extending the maturity of the debt to July 20, 2013.

On March 14, 2013, Stonehenge entered into an extension agreement of the Amended and Restated Senior Note with the Company to extend the maturity date of the financing arrangement to January 1, 2016. Under the terms of the extension agreement, the Company is required to pay \$50 monthly to Stonehenge, to be allocated first to accrued and unpaid interest and then to unpaid principal outstanding, beginning on April 1, 2013. The extension agreement was subject to the approval by the Company s board of directors and approval was obtained on March 21, 2013.

*Wachovia*

On August 17, 2009, the Company entered into a foreclosure agreement ( Agreement ) with Wachovia Bank with respect to approximately \$17.8 million of secured debt, accrued interest and fees. Under the terms of the Agreement, the Company agreed to cooperate with Wachovia with respect to its foreclosure on certain of the Company s real estate assets. In return, Wachovia agreed to release the Company from their obligations and guarantees relating to the \$17.8 million of indebtedness contemporaneous with the execution by the Company of a non-interest bearing, unsecured deficiency note payable to Wachovia in the amount of approximately \$1.8 million. The deficiency note was reduced by the principal payments related to certain homes sold by the Company. As of December 31, 2011, the deficiency note balance was \$132. On September 27, 2012, the Company repaid the outstanding balance of the deficiency note in full.

*Cornerstone*

On September 21, 2009 the Company entered into a settlement and mutual release agreement with Cornerstone Bank ( Cornerstone ) with respect to approximately \$5.1 million debt secured by its Gates of Luberon project in Atlanta, Georgia. Under the terms of the agreement, Cornerstone released the Company, and its subsidiary Mathis Partners, LLC, from their respective obligations and guarantees relating to \$5.1 million of debt owed by the Company to Cornerstone in exchange for a non-interest bearing unsecured subordinate note in the amount of \$0.4 million with a three year term. On October 15, 2012, the Company repaid the outstanding balance of the deficiency note in full.

As of December 31, 2012, maturities and/or curtailment obligations of all of our borrowings are as follows:

2013	\$ 14,027
2014	4,084

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

2015	6,422
2016	
2017 and thereafter	3,096
Total	\$ 27,629

As of December 31, 2012, the maturities and curtailment obligations for 2013 was \$14,027, of which, the new facilities and extensions resulted in \$13,291 of the obligations with revised maturities beginning in 2015 and beyond. Refer to Note 20 for more details on changes to our credit facilities.

F-19

**Table of Contents****10. SUNBRIDGE WARRANT AND STRATEGIC AGREEMENT**

In connection with entering into the SunBridge Loans, on July 12, 2011, the Company agreed to issue BridgeCom Development I, LLC, an affiliate of SunBridge ( BridgeCom ), an immediately exercisable warrant to purchase 1.0 million shares of the Company's Class A common stock at an exercise price equal to the average closing price of the stock for the preceding twenty days (\$1.03) (the SunBridge Warrant ). The exercise period is ten years from July 12, 2011. The Company calculated the fair value of the SunBridge Warrant and the SunBridge Loans and allocated the proceeds of the SunBridge Loans on a relative fair value basis. The fair value of the SunBridge Warrant was calculated using a Black Scholes option pricing model and the fair value of the SunBridge Loans was calculated using a discounted cash flow model. The Black Scholes option pricing model considered risk-free interest rates, volatility factors and current market and contractual prices. The fair value of the SunBridge Loans was estimated based on interest rates available to the Company for debt with similar terms. The amount allocated to the SunBridge Warrant was approximately \$1.0 million and is reflected as an addition to additional paid-in capital and a corresponding discount on the SunBridge Loans. The Company is amortizing this discount over the term of the SunBridge Loans using the effective interest method. The remaining discount at December 31, 2011 was approximately \$0.6 million. On May 29, 2012, the Company repaid the SunBridge loans in full and the SunBridge warrants remain unexercised as of December 31, 2012.

In addition, the Company agreed to enter into a right of first offer and refusal ( Strategic Agreement ) with SunBridge to jointly pursue certain homebuilding and multi-family projects in the Washington, D.C. metropolitan area. Under the general terms of the Strategic Agreement, the Company will offer material future investment opportunities to SunBridge and if mutually agreed upon, the Company and SunBridge will enter into specific joint venture arrangements for each identified opportunity. The Strategic Agreement terminates at the earlier of three years from the date of the agreement or until each party funds a minimum of \$25.0 million in identified investment opportunities.

**11. COMMON STOCK AND WARRANTS**

On May 12, 2006, the Company completed a private placement (the PIPE ) to institutional and other accredited investors of 2,121 shares of Class A common stock and warrants exercisable into 636 shares of Class A common stock. The Company sold the securities for \$9.43 per share for total proceeds of approximately \$20.0 million and net proceeds of approximately \$18.7 million. The per share price of \$9.43 represented a premium of approximately 14.6% to the closing price of the Company's common stock on the date the purchase was completed. The net proceeds were used for general corporate purposes. The warrants issued in connection with the PIPE were five-year warrants exercisable at any time after November 10, 2006 with an exercise price of \$11.32 per share. The fair value of the warrants issued under the PIPE have been reported as equity instruments because the liquidated damages, which are capped at 10%, reasonably represent the difference between the value of a registered share and an unregistered share of the Company's common stock. All unexercised warrants were forfeited as of November 10, 2011.

As part of the Private Placement referred to in Note 20, the Company also issued warrants to purchase shares of the Company's Class A Common Stock ( Class A Common stock )( Warrants, and each a Warrant ) to Purchasers who are not officers, directors or affiliates of the Company that purchased Interests that equaled or exceeded an initial investment amount of \$250. The Warrants represent the right to purchase an aggregate amount of up to 224 shares of Class A Common Stock. The Warrants have an initial exercise price which is equal to the average of the closing price of the Class A Common Stock of the 20 trading days preceding the issuance of the Warrant. The Warrants contain a cashless exercise provision. In the event the Purchasers exercise the Warrants on a cashless basis, the Company will not receive any proceeds. Warrants may be exercised at any time prior to March 14, 2023.

**12. RELATED PARTY TRANSACTIONS**

On December 31, 2009, the Company, through an affiliate, Comstock Property Management, L.C., entered into a three-year lease for approximately 7,620 square feet of office space for its corporate headquarters at 1886 Metro Center Drive, Reston, Virginia from Comstock Asset Management, L.C., an affiliate wholly-owned by our Chief Executive Officer. On September 19, 2012, the Company amended the lease for an additional 2,436 square feet of office space, or a total 10,056 square feet, for its corporate headquarters, with an effective date of July 1, 2012. Concurrent with the amendment, the Company agreed to extend the lease for five-years from the effective date and future minimum annual lease payments are as follows:

2013	\$ 301
2014	310
2015	320
2016	329

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

2017

167

Total

\$ 1,427

For the year ended December 31, 2012 and 2011, total payments made under this lease agreement were \$246 and \$203, respectively. As of December 31, 2012, the Company recorded a straight line rent payable of \$9, which is included in Accounts payable and accrued liabilities .

F-20



---

## **Table of Contents**

During the second quarter of 2009, the Company began deferring a portion of the base salary payments to our Chief Executive Officer and our Chief Operating Officer. These deferrals ended on May 1, 2011 and the deferred balance of \$842 was paid during the third quarter of 2011.

On February 11, 2011, Comstock Contracting, L.C., a subsidiary of the Company, entered into an Owner-Contractor Agreement with CRS Construction Services, L.C., an entity wholly-owned by the Chief Executive Officer of the Company, to perform paving and certain site improvement work to property in Reston, Virginia which is owned by Fairfax County, Virginia. The contract sum was for approximately \$1.0 million and the work was completed in April 2011.

Comstock Contracting, L.C., a subsidiary of the Company, entered into a Subcontract Agreement with Davis Construction, LLC to perform site work and land development for a project known as Loudoun Station in Loudoun County, Virginia. Comstock Partners, L.C., an entity wholly-owned by the Chief Executive Officer of the Company, is the owner of the Loudoun Station project. The total contract value is estimated to be approximately \$5 million and the project was completed in October 2012. The revenue associated with this project is included in Revenue other in the consolidated statement of operations. For the year ended December 31, 2012 and 2011, the Company recognized \$1.4 million and \$3.8 million of revenue, respectively, under this contract. The Company was owed \$1.3 million and \$1.0 million at December 31, 2012 and 2011, respectively, under this contract, which is included in Trade receivables in the consolidated balance sheet.

On January 31, 2011, Comstock Cascades II, L.C., a subsidiary of the Company ( Cascades II ) entered into a private placement for the sale of membership interests in Cascades II whereby Cascades II raised working capital in the amount of \$2.35 million (the Private Placement ) related to the planned construction of the Cascades Apartments. Proceeds of the Private Placement were utilized (i) to provide sufficient capital needed to secure project financing for the Cascades Apartments, (ii) to retire a portion of the existing indebtedness, and (iii) to reimburse the Company for prior expenditures incurred on behalf of the project. Participants in the Private Placement included unrelated third party investors along with several members of the Company's Board of Directors, as well as the Chief Operating Officer, Chief Financial Officer and General Counsel of the Company. In March 2012, upon completion of the sale of the Cascades Apartments, the Company repaid the participants in the Private Placement \$2.94 million, including the preferred returns, in full.

Pursuant to a Credit Enhancement Agreement by and between Comstock and the Chief Operating Officer and Chief Executive Officer of the Company (each, a Guarantor ), the Guarantors agreed to provide credit enhancement and the personal guarantee of loans with Cardinal Bank and Eagle Bank in exchange for payment by the Company of a credit enhancement fee. As a result of this credit enhancement the Guarantors on an aggregate basis were entitled to a credit enhancement fee calculated at a rate of four percent (4%) per annum based on an agreed upon formula more fully discussed in Note 9. During the year ended December 31, 2012 and 2011, the Company made guarantee payments under this agreement of approximately \$130 and \$254. The financing with SunBridge Capital Management, LLC, as discussed fully in Note 9, eliminated the need for personal guarantees on the applicable projects and accordingly this agreement was terminated on July 12, 2011 with respect to the fees paid on the Eagle Bank loan. On March 7, 2012, the Cardinal Bank loan was repaid and, accordingly, the agreement was terminated with respect to the fees paid on the Cardinal Bank loan and the accrued fees were paid in full.

On February 23, 2009, Comstock Homes of Washington, L.C., a wholly-owned subsidiary of the Company, entered into a Services Agreement with Comstock Asset Management, L.C., an entity wholly-owned by the Chief Executive Officer, to provide services related to real estate development and improvements, legal, accounting, marketing, information technology and additional support services. Pursuant to the Services Agreement, the Company shall not be responsible for any out-of-pocket or third party costs associated with the services provided. For the years ended December 31, 2012 and 2011, the Company billed Comstock Asset Management, L.C. \$525 and \$92, respectively, for services and out-of-pocket expenses incurred. Revenues from this arrangement are included within Revenue other within the statement of operations.

### **13. EMPLOYEE BENEFIT PLANS**

The Company maintains a defined contribution retirement savings plan pursuant to Section 401(k) of the Internal Revenue Code (the Code ). Eligible participants may contribute a portion of their compensation to their respective retirement accounts in an amount not to exceed the maximum allowed under the Code. In January 2006, the Company began matching employee contributions. The total amount matched for the twelve months 2012 and 2011 was \$37 and \$28 respectively.

### **14. RESTRICTED STOCK, STOCK OPTIONS AND OTHER STOCK PLANS**

On December 14, 2004 the Company adopted the 2004 Long-Term Compensation Plan ( The Plan ). The Plan provides for the issuance of stock options, stock appreciation rights, or SARs, restricted stock, deferred stock, dividend equivalents, bonus stock and awards in lieu of cash compensation, other stock-based awards and performance awards. Any shares issued under the Plan typically vest over service periods that

range from one to five years. Stock options issued under the plan expire 10 years from the date they are granted.

## Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

The Plan provided an initial authorization of 2,550 shares of Class A common stock for issuance and allows an automatic annual increase equal to the lesser of (i) 3% of the Class A common stock outstanding (ii) 750 shares or (iii) such lesser amount as may be determined by the Company's Board of Directors. On April 27, 2012, the Company authorized an increase in the number of shares of our class A common stock reserve to 7.1 million. On June 22, 2012, the Company's shareholders approved the Amended and Restated 2004 Long-Term Incentive Compensation Plan, including an increase in the reserve, with an automatic annual increase on January 1 of each successive year of the lesser of (i) 3% of the Class A Common Stock outstanding, or (ii) 750 shares. As of December 31, 2012, there were 7.1 million shares available for issuance under the Plan.

F-21

**Table of Contents**

The fair value of each option award is calculated on the date of grant using the Black-Scholes option pricing model and certain subjective assumptions. Because the Company does not have sufficient trading history, expected volatilities are based on historical volatilities of comparable companies within our industry. We estimate forfeitures using a weighted average historical forfeiture rate. Our estimates of forfeitures will be adjusted over the requisite service period based on the extent to which actual forfeitures differ, or are expected to differ, from their estimate. The risk-free rate for the periods is based on the U.S. Treasury rates in effect at the time of grant. The expected term of options is based on the simplified method which assumes that the option will be exercised midway between the vesting date and the contractual term of the option. The Company is able to use the simplified method as the options qualify as plain vanilla options as defined by ASC 718 Stock Compensation. The following table summarizes the assumptions used to calculate the fair value of options during 2012 and 2011.

	2012	2011
Weighted average fair value of options granted	\$ 1.26	\$ 0.99
Dividend yields		
Expected volatility	106.3%-165.6%	107.3%-164.5%
Weighted average expected volatility	137.0%	137.00%
Risk free interest rates	0.78%	0.96%
Weighted average expected term (in years)	6.25	6.25

The following table summarizes information about stock option activity:

	Shares	Weighted average exercise price
Outstanding at December 31, 2010	664	\$ 0.94
Granted	100	1.08
Exercised		
Forfeited or expired		
Outstanding at December 31, 2011	764	\$ 0.96
Granted	140	1.81
Exercised		
Forfeited or expired	(1)	1.00
Outstanding at December 31, 2012	903	1.09
Exercisable at December 31, 2012	688	\$ 0.95

As of December 31, 2012 and 2011, the weighted-average remaining contractual term of unexercised stock options was 7.3 years and 7.8 years, respectively.

A summary of the Company's restricted share activity is presented below:

	Shares	Weighted average fair value at date of grant
Restricted shares outstanding at December 31, 2010	94	\$ 1.24
Granted	1,471	1.31
Vested	(602)	1.27
Forfeited		

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Restricted shares outstanding at December 31, 2011	963	\$	1.31
Granted	706		1.73
Vested	(615)		1.36
Forfeited	(4)		1.31
Restricted shares outstanding at December 31, 2012	1,050	\$	1.56

F-22

---

## **Table of Contents**

As of December 31, 2012 and 2011, \$1.0 million and \$0.9 million, respectively, of unrecognized compensation cost related to stock options and restricted stock issuances granted under the Plan. The Company intends to issue new shares of its common stock upon vesting of restricted stock grants or the exercise of stock options.

## **15. COMMITMENTS AND CONTINGENCIES**

### ***Litigation***

On July 29, 2008, Balfour Beatty Construction, LLC, successor in interest to Centex Construction ( Balfour ), the general contractor for a subsidiary of the Company, filed liens totaling approximately \$552 at The Eclipse on Center Park Condominium project ( Project ) in connection with its claim for amounts allegedly owed under the Project contract documents. In September 2008, the Company s subsidiary filed suit against Balfour to invalidate the liens and for its actual and liquidated damages in the approximate amount of \$17.1 million due to construction delays and additional costs incurred by the Company s subsidiary with respect to the Project. In October 2008, Balfour filed counterclaims in the approximate amount of \$2.8 million. Subsequent to an expedited hearing filed by the Company s subsidiary to determine the validity of the liens that was ultimately heard in February 2009, the Company received an order of the court in April 2009 invalidating the liens. On March 19, 2010, the Company s subsidiary received a judgment against Balfour in an amount of \$11.96 million. On March 25, 2010, the Company s subsidiary received notice of Balfour s intention to appeal the judgment and post a supersedeas bond in the amount of \$12.5 million. On July 21, 2011, the Company and Balfour reached a settlement for all claims related to this matter for approximately \$9.4 million, net of closing costs of approximately \$900. The Company received the proceeds of the settlement on August 4, 2011.

Currently, we are not subject to any material legal proceedings. From time to time, however, we are named as a defendant in legal actions arising from our normal business activities. Although we cannot accurately predict the amount of our liability, if any, that could arise with respect to legal actions pending against us, we do not expect that any such liability will have a material adverse effect on our financial position, operating results and cash flows. We believe that we have obtained adequate insurance coverage, rights to indemnification, or where appropriate, have established reserves in connection with these legal proceedings.

### ***Letters of credit and performance bonds***

The Company has commitments as a result of contracts entered into with certain third parties, primarily local governmental authorities, to meet certain performance criteria as outlined in such contracts. The Company is required to issue letters of credit and performance bonds to these third parties as a way of ensuring that such commitments entered into are met by the Company. The letters of credit and performance bonds issued in favor of the Company and/or its subsidiaries mature on a revolving basis, and if called into default, would be deemed material if assessed against the Company and/or its subsidiaries for the full amounts claimed. In some circumstances we have negotiated with our lenders in connection with foreclosure agreements for the lender to assume certain liabilities with respect to the letters of credit and performance bonds. We cannot accurately predict the amount of any liability that could be imposed upon the Company with respect to maturing or defaulted letters of credit or performance bonds and it is anticipated that any such liability would likely have a material adverse effect on our financial position, operating results or cash flows. At December 31, 2012 and 2011, the Company had issued \$66 and \$528 in letters of credit, respectively, and \$1,610 and \$2,133 in performance and payment bonds, respectively, to these third parties. No amounts have been drawn against these letters of credit or performance bonds.

## **16. DISCONTINUED OPERATIONS**

As described in Note 3, on March 7, 2012, the Company s subsidiary sold the Cascades Apartments. As the Cascades Apartments represented a component of the Company s business, the consolidated financial statements have been reclassified for all periods presented to appropriately reflect the discontinued operations of the Cascades Apartments and the continuing operations of the Company. Revenues, costs and expenses directly associated with the Cascades Apartments have been reclassified as discontinued operations in the consolidated statements of operations. Corporate expenses, such as general corporate overhead, have not been allocated to discontinued operations. The guidance in ASC 740-20-45-7 requires that the income recorded in discontinued operations be considered when determining the amount of benefit allocable to continuing operations in circumstances when continuing operations result in a net loss position for the period presented. Accordingly, the Company has allocated a tax benefit of \$2,484 to continuing operations and a tax expense of \$2,484 to discontinued operations for the year ended December 31, 2012.



**Table of Contents**

Summarized financial information for the Cascades Apartments, is set forth below:

	<b>Years ended December 31,</b>	
	<b>2012</b>	<b>2011</b>
Revenue	\$ 171	\$ 276
Cost of sales	128	391
Selling, general and administrative	9	44
Interest, real estate taxes and indirect costs related to inactive projects	154	363
Other (income) expenses, net	(22)	5
Loss from discontinued operations before gain on sale of real estate and income tax expense	(98)	(527)
Net gain on sale of real estate	6,466	
Net (loss) income from discontinued operations before income tax expense	6,368	(527)
Income tax expense	(2,484)	
Net (loss) income from discontinued operations	\$ 3,884	\$ (527)

Discontinued operations have not been segregated in the consolidated statement of cash flows. Therefore, amounts for certain captions will not agree with the respective data in the consolidated statement of operations.

**17. FAIR VALUE OF FINANCIAL INSTRUMENTS**

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

The carrying amounts reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities are reasonable estimates of their fair values based on their short maturities.

The fair value of fixed and floating rate debt is based on observable market rates (Level 2 inputs) for similar instruments, which ranged from 4.75% - 13.5% as of December 31, 2012 and 6.5% - 12.5% as of December 31, 2011. The following table summarizes the fair value of fixed and floating rate debt and the corresponding carrying value as of:

	<b>December 31,</b>	<b>December 31,</b>
	<b>2012</b>	<b>2011</b>
Carrying amount	\$ 27,629	\$ 30,378
Fair value	\$ 24,881	\$ 26,927

Fair value estimates are made at a specific point in time, based on relevant market information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matters of significant judgment and therefore, cannot be determined with precision. Changes in assumptions could significantly affect the estimates.

The Company may also value its real estate held for development and sale at fair value on a nonrecurring basis if it is determined that an impairment has occurred. Such fair value measurements use significant unobservable inputs and are classified as Level 3. See Note 2 for a further discussion of the valuation techniques and the inputs used.



**18. INCOME TAXES**

The effective tax rate for the years ended December 31, 2012 and 2011 was 0% and 3%, respectively. This resulted in zero and \$33 in tax expense for the twelve month periods ended December 31, 2012 and 2011, respectively.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. The Company recorded valuation allowances for certain tax attributes and other deferred tax assets. At this time, sufficient uncertainty exists regarding the future realization of these deferred tax assets through future taxable income. If, in the future, the Company believes that it is more likely than not that these deferred tax benefits will be realized, the valuation allowances will be reversed. With a full valuation allowance, any change in the deferred tax asset or liability is fully offset by a corresponding change in the valuation allowance.

**Table of Contents**

The Company currently has approximately \$116 million in federal and state NOLs, which based on current statutory tax rates, has a potential fair value of approximately \$45 million in tax savings. If unused, these NOLs will begin expiring in 2028. Under Internal Revenue Code Section 382 ( Section 382 ) rules, if a change of ownership is triggered, the Company's NOL assets and possibly certain other deferred tax assets may be impaired. We estimate that as of December 31, 2012, the cumulative shift in ownership of the Company's stock would not cause an impairment of our NOL asset. However, if an ownership change were to occur, the Section 382 limitation would not be expected to materially impact the Company's financial position or results of operations as of December 31, 2012, because of the Company's full valuation allowance on its net deferred tax assets.

The Company's ability to use its NOLs (and in certain circumstances, future built-in losses and depreciation deductions) can be negatively affected if there is an ownership change as defined under Section 382. In general, an ownership change occurs whenever there is a shift in ownership by more than 50 percentage points by one or more 5% shareholders over a specified time period (generally three years). Given Section 382's broad definition, an ownership change could be the unintended consequence of otherwise normal market trading in the Company's stock that is outside of the Company's control. In an effort to preserve the availability of these NOLs, Comstock adopted a Section 382 stockholder rights plan (the Rights Plan). The Rights Plan was adopted to reduce the likelihood of such an unintended ownership change and thus assist in preserving the value of these tax benefits. Similar plans have been adopted by a number of companies holding similar significant tax assets over the past several years. This plan was submitted to a vote of the Company's shareholders on June 17, 2011 and the plan was approved at that meeting.

The Company has not recorded any accruals for tax uncertainties as of December 31, 2012 and 2011, respectively. We file U.S. and state income tax returns in jurisdictions with varying statutes of limitations. The 2009 through 2011 tax years generally remain subject to examination by federal and most state tax authorities.

Income tax provision consists of the following as of December 31:

	2012	2011
<b>Current:</b>		
Federal	\$	\$ 33
State		
		33
<b>Deferred:</b>		
Federal	(1,013)	731
State	(185)	136
	(1,198)	867
Valuation allowance	1,198	(867)
Total income tax expense (benefit)	\$	\$ 33

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Components of the Company's deferred tax assets and liabilities at December 31 are as follows:

	2012	2011
<b>Deferred tax assets:</b>		
Inventory	\$ 1,051	\$ 3,480
Warranty	282	320
Net operating loss and tax credit carryforwards	45,330	41,562
Cancellation of debt gain	1	760
Accrued expenses	112	(63)

Edgar Filing: Comstock Holding Companies, Inc. - Form 10-K

Stock based compensation	397	303
	47,173	46,362
Less - valuation allowance	(47,013)	(45,815)
Net deferred tax assets	160	547
Deferred tax liabilities:		
Investments in affiliates	(136)	
Depreciation and amortization	(24)	(547)
Net deferred tax liabilities	(160)	(547)
Net deferred tax assets (liabilities)	\$	\$

F-25

**Table of Contents**

We file U.S. and state income tax returns in jurisdictions with varying statutes of limitations. The 2009 through 2011 tax years generally remain subject to examination by federal and most state tax authorities.

A reconciliation of the statutory rate and the effective tax rate follows:

	2012	2011
Federal statutory rate	(35.00)%	(35.00)%
State income taxes - net of federal benefit	(3.90)%	(3.97)%
Permanent differences	%	%
Return to provision adjustments	3.24%	(14.19)%
Change in valuation allowance	21.23%	53.16%
Other, net	14.43%	%
<b>Tax benefit</b>	<b>%</b>	<b>%</b>

**19. QUARTERLY RESULTS (unaudited)**

Quarterly results for the years ended December 31, 2012 and 2011 follow (in thousands, except per share amounts):

	March 31, 2012	Three months ended		December 31, 2012
		June 30, 2012	September 30, 2012	
Revenues	\$ 3,935	\$ 4,244	\$ 3,483	\$ 2,640
Operating loss	(2,369)	(3,089)	(4,485)	(2,082)
Net loss from continuing operations	(1,428)	(1,879)	(4,166)	(2,050)
Net income (loss) from discontinued operations	5,482	(1,236)	(370)	8
Pretax income (loss)	4,054	(3,115)	(4,536)	(2,042)
Net income (loss)	4,054	(3,115)	(4,536)	(2,042)
Net income (loss) attributable to Comstock Holding Companies, Inc.	3,951	(3,115)	(4,496)	(2,005)
Basic earnings (loss) per share	0.19	(0.15)	(0.22)	(0.10)
Diluted earnings (loss) per share	0.19	(0.15)	(0.22)	(0.10)

	March 31, 2011	Three months ended		December 31, 2011
		June 30, 2011	September 30, 2011	
Revenues	\$ 4,586	\$ 5,903	\$ 5,308	\$ 6,136
Operating loss	(1,119)	(1,793)	(2,256)	(2,631)
Net (loss) income from continuing operations	(843)	(1,506)	6,895	(2,421)
Net loss from discontinued operations	(50)	(52)	(234)	(191)
Pretax (loss) income	(893)	(1,558)	6,661	(2,612)
Net (loss) income	(893)	(1,558)	6,661	(2,612)
Net (loss) income attributable to Comstock Holding Companies, Inc.	(1,025)	(1,676)	6,541	(2,733)
Basic (loss) earnings per share	(0.05)	(0.09)	0.33	(0.14)
Diluted (loss) earnings per share	(0.05)	(0.09)	0.33	(0.14)

Quarterly and year-to-date computations of per share amounts are made independently. Therefore, the sum of per share amounts for the quarters may not agree with per share amounts for the year due to rounding.



**Table of Contents****20. SUBSEQUENT EVENTS**

On March 14, 2013, Comstock Investors VII, L.C. ( Investors VII ), a subsidiary of the Company entered into subscription agreements (each a Subscription Agreement ) with certain accredited investors (the Purchasers, and each a Purchaser ), pursuant to which the Purchasers purchased membership interests ( Interests ) in Investors VII for an initial aggregate principal amount of \$6,925 of an up to \$7,000 capital raise (the Private Placement ). Purchasers included unrelated third-party accredited investors along with members of the Company s Board of Directors and the Chief Operating Officer, Chief Financial Officer and General Counsel of the Company. The Subscription Agreement provides that the Purchasers are entitled to a cumulative, compounded, preferred return of 20% per annum, compounded annually on their capital account balances. After six months, the Company has the right to repurchase the Interests of the Purchasers, provided that (i) all of the Purchasers Interests are acquired, (ii) the purchase is made in cash and (iii) the purchase price equals the Purchasers capital account plus an amount necessary to cause the preferred return to equal a cumulative cash on cash return equal to 20% per annum. The Private Placement provides capital related to the current and planned construction of the Company s following projects: The Residences at Shady Grove in Rockville, Maryland consisting of 36 townhomes, The Hampshires project in Washington, D.C. consisting of 38 single family residences and 73 townhomes, and the Falls Grove project in Prince William County, Virginia consisting of 110 townhomes and 19 single family homes (collectively, the Projects ). Proceeds of the Private Placement are to be utilized (i) to provide capital needed to complete the Projects in conjunction with project financing for the Projects, (ii) to reimburse the Company for prior expenditures incurred on behalf of the Projects, and (iii) for general corporate purposes of the Company.

As part of the Private Placement, the Company also issued warrants to purchase shares of the Company s Class A Common Stock ( Class A Common stock ) ( Warrants, and each a Warrant ) to Purchasers who are not officers, directors or affiliates of the Company that purchased Interests that equaled or exceeded an initial investment amount of \$250. The Warrants represent the right to purchase up to 224 shares of Class A Common Stock, the maximum aggregate amount of warrants approved for issuance under the Private Placement. The Warrants have an initial exercise price which is equal to the average of the closing price of the Class A Common Stock of the 20 trading days preceding the issuance of the Warrant. The Warrants contain a cashless exercise provision. In the event the Purchasers exercise the Warrants on a cashless basis, the Company will not receive any proceeds. Warrants may be exercised at any time prior to March 14, 2023.

On March 25, 2013, Comstock Redland Road, L.C., a subsidiary of the Company ( Redland ), entered into a Revolving Credit Line Deed of Trust, Security Agreement, and Fixture Filing, Loan Agreement, Revolving Construction Loan Promissory Note, Development Loan Promissory Note, and related documents (the TH Loan Documents ) with EagleBank ( Primary Lender ) pursuant to which Redland secured a Twelve Million Eight Hundred Thirty Thousand Dollar (\$12,830,000) acquisition, development and construction loan and letter of credit facility ( TH Loan ) for a mix of 39 townhomes and single family homes at the Residences at Shady Grove project in Rockville, Montgomery County, Maryland (the TH Project ) and a Two Million Four Hundred Thousand Dollar (\$2,400,000) acquisition and development loan ( Apt Loan ) for a 117-unit multi-family residential building known as BLVD Shady Grove, in Rockville, Montgomery County, Maryland (the Apt Project ). Under the terms of the TH Loan Documents, there is a twenty-four month maturity date, and an interest rate at LIBOR plus three percent (3%). Under the Apt Loan Documents, there is a twelve month maturity date and an interest rate at LIBOR plus three percent (3%). The TH Loan and Apt Loan are secured by the TH Project, Apt Project, and fully guaranteed by the Company.

In addition, on March 25, 2013, the Company, through Redland, entered into a Loan Agreement, Deed of Trust, Security Agreement and Fixture Filing, and Promissory Note, and related documents (the Secondary Loan Documents ) with Eagle Commercial Ventures, LLC ( Secondary Lender ) for acquisition and development of the TH Project and the Apt. Project totaling Three Million One Hundred and Ninety Thousand Dollars (\$3,190,000). Under the terms of the Secondary Loan Documents, there is a twenty-four month maturity date for the TH Loan, and a one year maturity date for the Apt Loan, and both loan provides for an interest rate at twelve percent (12%), with payment of interest only at six percent (6%) and accrual of the remaining six percent until maturity. The Secondary Loan is secured by a second trust on the TH Project, Apt Project, and fully guaranteed by the Company and the Company s Chief Executive Officer.

On March 14, 2013, Stonehenge Funding, LC ( Stonehenge ), an entity wholly-owned by the Chief Executive Officer of the Company, entered into an Extension Agreement of the Amended and Restated Senior Note with the Company to extend the maturity date of the financing arrangement to January 1, 2016. Under the terms of the Extension Agreement, the Company is required to pay \$50 monthly to Stonehenge, to be allocated first to accrued and unpaid interest and then to unpaid principal outstanding, beginning on April 1, 2013. The Extension Agreement was subject to the approval by the Company s board of directors and approval was obtained on March 21, 2013.

On March 22, 2013, the Company, through Comstock Eastgate, L.C., a consolidated joint venture of Comstock Holding Companies, Inc. and BridgeCom Development I, LLC, executed the third lot takedown, of eleven total, under the Building and Purchase Agreement with M/I Homes of DC, LLC, for the purchase price of \$554.