Comstock Holding Companies, Inc.
Form 10-Q
May 16, 2018
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant To Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended March 31, 2018

or

Transition Report Pursuant To Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from __________ to __________

Commission File Number 1-32375

Comstock Holding Companies, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**20-1164345**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**

1886 Metro Center Drive, 4th Floor

Reston, Virginia 20190

(703) 883-1700

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

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 (Section 232.405) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
	Emerging growth company

If an emerging growth company, indicate by checkmark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of May 16, 2018, 3,674,461 shares of Class A common stock, par value $0.01 per share, and 220,250 shares of Class B common stock, par value $0.01 per share, of the registrant were outstanding.

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COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

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

	March 31, 2018 (unaudited)	December 31, 2017
ASSETS		
Cash and cash equivalents	$ 987	$ 1,806
Restricted cash	1,212	1,141
Trade receivables	634	491
Trade receivables - related party	3,976	145
Real estate inventories	43,010	44,711
Fixed assets, net	299	309
Goodwill and intangibles	1,922	1,939
Other assets, net	1,258	616
TOTAL ASSETS	$ 53,298	$ 51,158
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable and accrued liabilities	$ 8,486	$ 9,116
Deferred revenue	3,192	
Notes payable - secured by real estate inventories, net of deferred financing charges	22,890	23,215
Notes payable - due to affiliates, unsecured, net of discount and deferred financing charges	15,346	14,893
Notes payable - unsecured, net of deferred financing charges	1,220	1,285
Income taxes payable	45	39
TOTAL LIABILITIES	51,179	48,548
Commitments and contingencies (Note 13)		
STOCKHOLDERS EQUITY (DEFICIT)		
Series C preferred stock $0.01 par value, 3,000,000 shares authorized, 579,158 shares issued and liquidation preference of $2,896 at March 31, 2018 and December 31, 2017, respectively	$ 442	$ 442
Class A common stock, $0.01 par value, 11,038,071 shares authorized, 3,374,461 and 3,295,518 issued, and outstanding, respectively	34	33

Class B common stock, $0.01 par value, 220,250 shares authorized, issued, and outstanding, respectively	2	2
Additional paid-in capital	177,747	177,612
Treasury stock, at cost (85,570 shares Class A common stock)	(2,662)	(2,662)
Accumulated deficit	(190,526)	(189,803)
TOTAL COMSTOCK HOLDING COMPANIES, INC. DEFICIT	(14,963)	(14,376)
Non-controlling interests	17,082	16,986
TOTAL EQUITY	2,119	2,610
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	$ 53,298	$ 51,158

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

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COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

(Amounts in thousands, except per share data)

	Three Months Ended March 31, 2018	2017
Revenues		
Revenue homebuilding	$ 5,561	$ 10,064
Revenue asset management	2,791	
Revenue real estate services	447	204
Total revenue	8,799	10,268
Expenses		
Cost of sales homebuilding	5,495	9,101
Cost of sales asset management	2,541	
Cost of sales real estate services	177	224
Impairment charges	558	
Sales and marketing	219	381
General and administrative	360	1,246
Interest and real estate taxes	85	
Operating loss	(636)	(684)
Other income, net	14	20
Loss before income tax expense	(622)	(664)
Income tax expense	(6)	
Net loss	(628)	(664)
Net income (loss) attributable to non-controlling interests	95	(17)
Net loss attributable to Comstock Holding Companies, Inc.	(723)	(647)
Paid-in-kind dividends on Series B Preferred Stock		78
Extinguishment of Series B Preferred Stock		(1,011)
Net (loss) income attributable to common stockholders	$ (723)	$ 286
Basic net (loss) income per share	$ (0.21)	$ 0.09
Diluted net (loss) income per share	$ (0.21)	$ 0.08
Basic weighted average shares outstanding	3,448	3,343
Diluted weighted average shares outstanding	3,448	3,373

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

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COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands, except per share data)

	Three Months Ended March 31, 2018	2017
Cash flows from operating activities:		
Net loss	$ (628)	$ (664)
Adjustment to reconcile net loss to net cash (used in) provided by operating activities		
Amortization of loan discount, loan commitment and deferred financing fees	150	210
Depreciation expense	57	37
Earnings from unconsolidated joint venture, net of distributions	4	18
Stock compensation	86	32
Impairment charges	558	
Changes in operating assets and liabilities:		
Trade receivables	(5,216)	469
Real estate inventories	1,157	524
Other assets	(655)	550
Accrued interest	592	253
Accounts payable and accrued liabilities	3,840	(754)
Income taxes payable	6	
Net cash (used in) provided by operating activities	(49)	675
Cash flows from investing activities:		
Purchase of fixed assets	(46)	(1)
Principal received on note receivable	9	9
Net cash (used in) provided by investing activities	(37)	8
Cash flows from financing activities:		
Proceeds from notes payable	2,853	5,499
Payments on notes payable	(3,458)	(5,981)
Loan financing costs	(57)	(71)
Distributions to non-controlling interests		(1,908)
Net cash used in financing activities	(662)	(2,461)
Net decrease in cash, restricted cash, and cash equivalents	(748)	(1,778)
Cash, restricted cash, and cash equivalents, beginning of period	2,947	6,999
Cash, restricted cash, and cash equivalents, end of period	$ 2,199	$ 5,221

Supplemental cash flow information:				
Interest paid, net of interest capitalized	$	605	$	243
Supplemental disclosure for non-cash activity:				
Seller s note payable	$		$	115
Accrued liability settled through issuance of stock	$		$	32
Increase in Series B preferred stock value in connection with dividends paid in-kind	$		$	24
Extinguishment of Series B Preferred Stock	$		$	1,011

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

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COMSTOCK HOLDING COMPANIES, INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Amounts are in thousands, except per share data, number of units, or as otherwise noted)

1. ORGANIZATION AND BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Comstock Holding Companies, Inc. and subsidiaries (Comstock or the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and in accordance with the instructions to Form 10-Q and Article 8 of Regulation S-X. Such financial statements do not include all of the disclosures required by GAAP for complete financial statements. In our opinion, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation have been included in the accompanying consolidated financial statements. For further information and a discussion of our significant accounting policies, other than discussed below, refer to our audited consolidated financial statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017.

Comstock Holding Companies, Inc., incorporated in 2004 as a Delaware corporation, is a multi-faceted real estate development and services company primarily focused in the mid-Atlantic region of the United States. In 2018, the Company has made a strategic decision to transform its operational platform from for sale production homebuilding to asset management, commercial development and complementary real estate related services. Moving forward, along with the buildout of the existing homebuilding pipeline, the Company will operate through two primary real estate focused platforms CDS Asset Management, LC (CAM) and Comstock Real Estate Services, LC (CRES). Concurrently, the Company will wind down its on-balance sheet production homebuilding. References in these consolidated financial statements on Form 10-Q to Comstock, Company , CAM , CRES , we, our and us ref Comstock Holding Companies, Inc. together in each case with our subsidiaries and any predecessor entities unless the context suggests otherwise.

The Company s Class A common stock is traded on the NASDAQ Capital Market under the symbol CHCI and has no public trading history prior to December 17, 2004.

Throughout this quarterly report on Form 10-Q, amounts are in thousands, except per share data, number of units, or as otherwise noted.

For the three months ended March 31, 2018 and 2017, comprehensive loss equaled net loss; therefore, a separate statement of comprehensive loss is not included in the accompanying consolidated financial statements.

Liquidity and Capital Resources

The Company requires capital to operate, manage assets, provide real estate services, develop land, construct homes, and fund carrying costs and overhead. These expenditures include payroll, engineering, entitlement, utilities and interest as well as the construction costs of our projects. Its sources of capital include fees generated from various asset management agreements, private equity and debt placements (which has included significant participation from Company insiders), funds derived from various secured and unsecured borrowings to finance acquisition, development and construction on acquired land, cash flow from operations, which includes fees generated from service agreements and the sale and delivery of constructed homes, and the potential sale of public debt and equity securities. The Company is involved in ongoing discussions with lenders and equity sources in an effort to provide additional growth capital to fund various new business opportunities.

The Company has outstanding borrowings with various financial institutions and other lenders that have been used to finance the acquisition of new service business opportunities, as well as acquisition, development and construction of real estate projects. It has generally financed its development and construction activities on a single or multiple project basis so it is not uncommon for each of our projects or collection of our projects to have a separate credit facility. Accordingly, the Company typically has had numerous credit facilities and lenders.

As of March 31, 2018, $29.4 million of the Company s outstanding credit facilities and project related loans mature at various periods through the end of 2018. Active discussions are taking place with our lenders to seek long term extensions and modifications to these loans. These debt instruments impose certain restrictions on our operations, including speculative unit construction limitations, curtailment obligations, and financial covenant compliance. If the Company fails to comply with any of these restrictions, an event of default could occur. Additionally, events of default could occur if we fail to make required debt service payments or if we fail to come to agreement on an extension on a certain facility prior to a given loan s maturity date. Any event of default would likely render the obligations under these instruments due and payable as of that event. Any such event of default would allow certain of our lenders to exercise cross default provisions in our loan agreements with them, such that all debt with that institution could be called into default. Refer to Note 12 *Debt* for further discussion regarding the Company s credit facilities and Note 23 *Subsequent Events* for other subsequent events impacting our credit facilities extensions.

At March 31, 2018, $15.3 million of the Company s notes payable to affiliates were set to mature prior to the end of 2018. These funds were primarily obtained from entities wholly owned by our Chief Executive Officer, who has unilateral ability to extend the maturity dates beyond 2018 as needed. The current performance of our projects has met all required servicing obligations required by the facilities. We are anticipating that with successful resolution of the debt extension discussions with our lenders, the recently completed capital raises from our private placements, 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 its operations through the next 12 months, though no assurances can be made that the Company will be successful in its efforts. See Note 18 *Related Party Transactions* in the accompanying consolidated financial statements for details on private placement offerings.

Recent Developments

Our business strategy to transition to a full-service asset manager and real estate services company involves the initial integration of our existing homebuilding operating platform with the commercial development operating platform of the Chief Executive Officer s private company and thereafter to grow our assets under management and expand our service based relationships. To anchor our new business focus, on March 30, 2018, the Company entered into an initial Master Asset Management Agreement (AMA) effective January 2, 2018, through its CAM subsidiary, with Comstock Development Services, LC (CDS), an entity wholly owned by the Chief Executive Officer of the Company. Under the AMA, CDS will pay CAM an annual cost-plus fee in an aggregate amount equal to the sum of (i) the employment expenses of personnel dedicated to providing services to CDS private portfolio pursuant to the AMA, (ii) the costs and expenses of the Company related to maintaining the listing of its shares on a securities exchange and complying with regulatory and reporting obligations as a public company, and (iii) a fixed annual payment of $1,000,000 (the Annual Fee). In connection with the execution of the AMA, CDS paid CAM a deposit in the aggregate amount of $2,500,000 pursuant to the Agreement that will be credited against the Annual Fee to be paid to CAM in accordance with the Agreement. The initial term of the Agreement will terminate on December 31, 2022 (Initial Term). The Agreement will automatically renew for successive additional one-year terms (each an Extension Term) unless CDS delivers written notice of non-renewal of the Agreement at least 180 days prior to the termination date of the Initial Term or any Extension Term.

Entering into the initial AMA is part of the Company s strategic plan to transform its business model from for-sale homebuilding to asset management and commercial development. In addition to the AMA, CRES continues to organically grow and pursue acquisitions of businesses and assets that provide supply chain services to assets under management pursuant to AMA as well as to unrelated third parties in the areas of environmental consulting, mortgage brokerage, and capital market services.

Use of Estimates

Our consolidated financial statements have been prepared in accordance with GAAP. The preparation of these consolidated financial statements requires us to make estimates and judgments that affect the reported amounts for the reporting periods. We base these estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances. We evaluate these estimates and judgements on an ongoing basis. Actual results may differ from those estimates under different assumptions or conditions. Material estimates are utilized in the valuation of real estate inventories, valuation of deferred tax assets, analysis of goodwill impairment, valuation of equity-based compensation, capitalization of costs, consolidation of variable interest entities and warranty reserves.

Reclassifications

Certain amounts in the prior year consolidated financial statements have been reclassified to the current year presentation. The impact of the reclassifications made to prior year amounts is not material and did not affect net loss.

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Recently Adopted Accounting Standards

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09, Revenue from Contracts with Customers (ASU 2014-09). ASU 2014-09 provides a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. ASU No. 2014-09 will require an entity to recognize revenue when it transfers promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. In August 2015, the FASB issued ASU 2015-14, which deferred the effective date of ASU 2014-09 for one year, which would make the guidance effective for the Company s first fiscal year beginning after December 15, 2017. The Company adopted this standard using the modified retrospective method effective January 1, 2018. There were no material adjustments to the financial statements as a result of this adoption. Refer to Note 9 *Revenue* for further information regarding revenue from contracts with customers.

In August 2016, the FASB issued ASU 2016-15, *Statement of Cash Flows (Topic 230), Classification of Certain Cash Receipts and Cash Payments* (ASU 2016-15). ASU 2016-15 reduces the existing diversity in practice in financial reporting across all industries by clarifying certain existing principles in ASC 230, *Statement of Cash Flows*, including providing additional guidance on how and what an entity should consider in determining the classification of certain cash flows. Additionally, in November 2016, the FASB issued ASU 2016-18, *Statement of Cash Flows (Topic 230), Restricted Cash* (ASU 2016-18). ASU 2016-18 clarifies certain existing principles in ASC 230, *Statement of Cash Flows*, including providing additional guidance related to transfers between cash and restricted cash and how entities present, in their statement of cash flows, the cash receipts and cash payments that directly affect the restricted cash accounts. Both ASU 2016-15 and ASU 2016-18 were adopted for the Company s fiscal year beginning January 1, 2018. The adoption resulted in presentation reclassification of cash and restricted cash for the three months ended March 31, 2018 and 2017 of $1.2 million and $1.5 million, respectively, in its consolidated statement of cash flows.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805), Clarifying the Definition of a Business , which provides a more robust framework to use in determining when a set of assets and activities (collectively referred to as a set) is a business. The standard requires that when substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single identifiable asset or a group of similar identifiable assets, the set is not a business. ASU 2017-01 is effective for public business entities for annual periods beginning after December 15, 2017, including interim periods within those periods. The amendments in ASU 2017-01 will be applied prospectively beginning January 1, 2018. The adoption of ASU 2017-01 did not have a material effect on our consolidated financial statements.

In May 2017, the FASB issued ASU 2017-09, Compensation Stock Compensation (Topic 718) Scope of Modification Accounting. The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. ASU 2017-09 is effective for fiscal years, including interim periods within those fiscal years, beginning after December 15, 2017. The amendments in this update will be applied prospectively to an award modified on or after the adoption date, January 1, 2018. The adoption of ASU 2017-09 did not have a material effect on our consolidated financial statements.

Recently Issued Accounting Standards

In March 2018, the FASB issued ASU 2018-05, Income Taxes (Topic 740), Amendments to SEC Paragraphs Pursuant to SEC Staff Accounting Bulletin No. 118. The Tax Cuts and Jobs Act (the Act) changes existing United States tax law and includes numerous provisions that will affect businesses. The Act, for instance, introduces changes that impact U.S. corporate tax rates, business-related exclusions, and deductions and credits. ASC Topic 740 provides accounting and disclosure guidance regarding the recognition of taxes payable or refundable for the current year and the recognition of deferred tax liabilities and deferred tax assets for the future tax consequences of events that have been recognized in an entity s financial statements or tax returns. In accordance with SEC Staff Accounting Bulletin (SAB) 118, entities that elect to record provisional amounts must base them on reasonable estimates and may adjust those amounts for a period of up to a year after the December 22, 2017 enactment date. We do not expect the amendments of ASU 2018-05 to have a material effect on our consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, Simplifying the Test for Goodwill Impairment, which removes Step 2 from the goodwill impairment test and replaces the qualitative assessment. Impairment will be measured using the difference between the carrying amount and the fair value of the reporting unit. Under this revised guidance, failing Step 1 will always result in a goodwill impairment. The amendments in this update should be applied prospectively for annual and interim periods in fiscal years beginning after December 15, 2019. Early adoption is permitted for goodwill impairment tests with measurement dates after January 1, 2017. We do not expect the adoption of ASU 2017-04 to have a material effect on our consolidated financial statements.

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In February 2016, the FASB issued ASU 2016-02, Leases . The core principle of the standard is that a lessee should recognize the assets and liabilities that arise from leases. A lessee should recognize in its statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term. ASU 2016-02 is effective for public companies for annual reporting periods beginning after December 15, 2018 and interim periods within those fiscal years. Early adoption is permitted. We are currently evaluating the impact this new standard will have on our consolidated financial statements.

We assessed other accounting pronouncements issued or effective during the three months ended March 31, 2018 and deemed they were not applicable to us and are not anticipated to have a material effect on our consolidated financial statements.

2. TRADE RECEIVABLES

Trade receivables include amounts due from real estate services, asset management, commercial development, home sales transactions and amounts due from related parties with whom we have service arrangements.

	March 31, 2018	December 31, 2017
Trade	$ 332	$ 432
Due from settlement attorneys	120	
Other	182	59
	634	491
Less : allowance for doubtful accounts		
	$ 634	$ 491

3. REAL ESTATE INVENTORIES

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