

Forestar Group Inc.
 Form 10-Q
 November 06, 2014
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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 September 30, 2014

or

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

For the transition period from _____ to _____

Commission File Number: 001-33662

FORESTAR GROUP INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware	26-1336998
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
6300 Bee Cave Road, Building Two, Suite 500, Austin, Texas 78746	
(Address of Principal Executive Offices, Including Zip Code)	
(512) 433-5200	
(Registrant's Telephone Number, Including Area Code)	

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

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

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

(Do not check if a smaller reporting company)

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

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

Title of Each Class	Number of Shares Outstanding as of November 3, 2014
Common Stock, par value \$1.00 per share	34,958,270

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PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

FORESTAR GROUP INC.

Consolidated Balance Sheets

(Unaudited)

	Third Quarter-End 2014	Year-End 2013
	(In thousands, except share data)	
ASSETS		
Cash and cash equivalents	\$ 170,606	\$ 192,307
Real estate, net	591,805	519,464
Oil and gas properties and equipment, net	259,755	232,641
Investment in unconsolidated ventures	53,709	41,147
Timber	9,216	10,947
Receivables, net	46,301	39,252
Prepaid expenses	4,613	5,136
Income taxes receivable	2,837	—
Property and equipment, net	11,547	6,112
Deferred tax asset, net	30,932	40,398
Goodwill and other intangible assets	67,440	66,646
Other assets	19,478	18,102
TOTAL ASSETS	\$ 1,268,239	\$ 1,172,152
LIABILITIES AND EQUITY		
Accounts payable	\$ 17,667	\$ 21,409
Accrued employee compensation and benefits	6,852	5,814
Accrued property taxes	7,044	3,822
Accrued interest	8,695	2,343
Income taxes payable	—	3,876
Earnest money deposits	8,466	10,854
Other accrued expenses	27,371	26,851
Other liabilities	17,418	24,379
Debt	429,295	357,407
TOTAL LIABILITIES	522,808	456,755
COMMITMENTS AND CONTINGENCIES		
EQUITY		
Forestar Group Inc. shareholders' equity:		
Preferred stock, par value \$0.01 per share, 25,000,000 authorized shares, none issued	—	—
Common stock, par value \$1.00 per share, 200,000,000 authorized shares, 36,946,603 issued at third quarter-end 2014 and year-end 2013	36,947	36,947
Additional paid-in capital	558,165	556,676
Retained earnings	178,801	150,418
Treasury stock, at cost, 1,988,333 shares at third quarter-end 2014 and 2,199,666 shares at year-end 2013	(31,154) (34,196
Total Forestar Group Inc. shareholders' equity	742,759	709,845
Noncontrolling interests	2,672	5,552
TOTAL EQUITY	745,431	715,397
TOTAL LIABILITIES AND EQUITY	\$ 1,268,239	\$ 1,172,152

Please read the notes to consolidated financial statements.

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FORESTAR GROUP INC.

Consolidated Statements of Income and Comprehensive Income
(Unaudited)

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands, except per share amounts)			
REVENUES				
Real estate sales and other	\$23,067	\$37,001	\$122,738	\$84,877
Commercial and income producing properties	9,378	13,355	30,360	85,387
Real estate	32,445	50,356	153,098	170,264
Oil and gas	24,145	22,095	66,076	53,430
Other natural resources	2,250	2,656	7,284	8,963
	58,840	75,107	226,458	232,657
COSTS AND EXPENSES				
Cost of real estate sales and other	(10,662)	(18,603)	(60,145)	(43,112)
Cost of commercial and income producing properties	(9,391)	(13,352)	(28,117)	(70,151)
Cost of oil and gas producing activities	(18,470)	(10,090)	(48,016)	(26,762)
Cost of other natural resources	(711)	(454)	(2,288)	(1,662)
Other operating	(12,860)	(16,051)	(43,187)	(45,039)
General and administrative	(5,140)	(5,945)	(17,141)	(22,245)
	(57,234)	(64,495)	(198,894)	(208,971)
GAIN ON ASSET PURCHASE, EXCHANGE AND SALES	11,110	—	27,977	—
OPERATING INCOME	12,716	10,612	55,541	23,686
Equity in earnings of unconsolidated ventures	2,016	3,125	3,965	6,604
Interest expense	(8,634)	(5,231)	(21,507)	(14,892)
Other non-operating income	1,896	1,459	6,459	3,711
INCOME BEFORE TAXES	7,994	9,965	44,458	19,109
Income tax (expense) benefit	(2,755)	2,932	(15,464)	28
CONSOLIDATED NET INCOME	5,239	12,897	28,994	19,137
Less: Net (income) attributable to noncontrolling interests	(12)	(1,067)	(611)	(2,815)
NET INCOME ATTRIBUTABLE TO FORESTAR GROUP INC.	\$5,227	\$11,830	\$28,383	\$16,322
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING				
Basic	35,498	35,410	35,437	35,341
Diluted	43,868	36,072	43,750	35,949
NET INCOME PER COMMON SHARE				
Basic	\$0.12	\$0.33	\$0.66	\$0.46
Diluted	\$0.12	\$0.33	\$0.65	\$0.45
TOTAL COMPREHENSIVE INCOME	\$5,227	\$11,830	\$28,383	\$16,322

Please read the notes to consolidated financial statements.

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FORESTAR GROUP INC.

Consolidated Statements of Cash Flows
(Unaudited)

	First Nine Months	
	2014	2013
	(In thousands)	
CASH FLOWS FROM OPERATING ACTIVITIES:		
Consolidated net income	\$28,994	\$19,137
Adjustments:		
Depreciation, depletion and amortization	29,109	21,698
Change in deferred income taxes	10,649	3,535
Change in unrecognized tax benefits	—	(6,251)
Equity in earnings of unconsolidated ventures	(3,965)	(6,604)
Distributions of earnings of unconsolidated ventures	2,817	869
Share-based compensation	4,523	15,367
Real estate cost of sales	59,251	71,324
Dry hole and leasehold abandonment costs	11,541	2,206
Real estate development and acquisition expenditures, net	(82,864)	(65,762)
Reimbursements from utility and improvement districts	8,554	4,540
Other changes in real estate	3,148	1,440
Changes in deferred income	102	(2,229)
Gain on asset purchase, exchange and sales	(27,977)	—
Other	1,697	154
Changes in:		
Notes and accounts receivable	(6,300)	(544)
Prepaid expenses and other	4,232	(373)
Accounts payable and other accrued liabilities	(3,249)	(11,268)
Income taxes	(3,876)	(2,156)
Net cash provided by operating activities	36,386	45,083
CASH FLOWS FROM INVESTING ACTIVITIES:		
Property, equipment, software, reforestation and other	(13,583)	(6,241)
Oil and gas properties and equipment	(65,661)	(56,482)
Acquisition of partner's interest in unconsolidated multifamily venture, net of cash	(20,155)	—
Investment in unconsolidated ventures	(5,016)	(819)
Proceeds from sales of oil and gas properties, net	17,017	—
Proceeds from sales of other assets, net	2,868	—
Return of investment in unconsolidated ventures	1,601	1,271
Other	—	(45)
Net cash used for investing activities	(82,929)	(62,316)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of convertible senior notes, net	—	120,795
Proceeds from issuance of senior secured notes, net	241,947	—
Payments of debt	(222,468)	(96,915)
Additions to debt	17,169	38,901
Deferred financing fees	(3,114)	(353)
Distributions to noncontrolling interests, net	(1,070)	(1,561)
Purchase of noncontrolling interests	(7,971)	—
Exercise of stock options	1,197	1,812
Payroll taxes on issuance of stock-based awards	(1,024)	(1,128)

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Excess income tax benefit from share-based compensation	176	90
Net cash provided by financing activities	24,842	61,641
Net increase (decrease) in cash and cash equivalents	(21,701) 44,408
Cash and cash equivalents at beginning of period	192,307	10,361
Cash and cash equivalents at end of period	\$170,606	\$54,769

Please read the notes to consolidated financial statements.

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FORESTAR GROUP INC.

Notes to Consolidated Financial Statements
(Unaudited)

Note 1—Basis of Presentation

Our consolidated financial statements include the accounts of Forestar Group Inc., all subsidiaries, ventures and other entities in which we have a controlling interest. We account for our investment in other entities in which we have significant influence over operations and financial policies using the equity method. We eliminate all material intercompany accounts and transactions. Noncontrolling interests in consolidated pass-through entities are recognized before income taxes. In our consolidated balance sheets we have reclassified prior year's earnest money deposits that were included in other accrued expenses and other liabilities as a separate line item to conform to the current year presentation.

We prepare our unaudited interim financial statements in accordance with U.S. generally accepted accounting principles and Securities and Exchange Commission requirements for interim financial statements. As a result, they do not include all the information and disclosures required for complete financial statements. However, in our opinion, all adjustments considered necessary for a fair presentation have been included. Such adjustments consist only of normal recurring items unless otherwise noted. We make estimates and assumptions about future events. Actual results can, and probably will, differ from those we currently estimate including those principally related to allocating costs to real estate, measuring long-lived assets for impairment, oil and gas revenue accruals, capital expenditure and lease operating expense accruals associated with our oil and gas production activities, oil and gas reserves and depletion of our oil and gas properties. These interim operating results are not necessarily indicative of the results that may be expected for the entire year. For further information, please read the financial statements included in our 2013 Annual Report on Form 10-K.

Note 2—New and Pending Accounting Pronouncements

Accounting Standards Adopted in 2014

In first nine months 2014, we adopted ASU 2013-04 — Liabilities (Topic 405): Obligations Resulting from Joint and Several Liability Arrangements for Which the Total Amount of the Obligation Is Fixed at the Reporting Date, ASU 2014-12 — Compensation-Stock Compensation (Topic 718): Accounting for Share-Based Payments When the Terms of an Award Provide That a Performance Target Could Be Achieved after the Requisite Service Period and ASU 2014-08 — Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360), Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity. Adoption did not materially affect our earnings, financial position or disclosures.

Pending Accounting Standards

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606), requiring an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods or services to customers. The updated standard will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective and permits the use of either the retrospective or cumulative effect transition method. Early adoption is not permitted. The updated standard becomes effective for annual and interim periods beginning after December 15, 2016. We have not yet selected a transition method and we are currently evaluating the effect that the updated standard will have on our earnings, financial position and disclosures.

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Note 3—Real Estate

Real estate consists of:

	Third Quarter-End 2014 (In thousands)	Year-End 2013
Entitled, developed and under development projects	\$342,553	\$361,687
Undeveloped land (includes land in entitlement)	94,241	86,367
Commercial and income producing properties		
Carrying value	184,977	99,476
Less: accumulated depreciation	(29,966)	(28,066)
Net carrying value	155,011	71,410
	\$591,805	\$519,464

Included in entitled, developed and under development projects are the estimated costs of assets we expect to convey to utility and improvement districts of \$66,198,000 at third quarter-end 2014 and \$62,183,000 at year-end 2013, including \$40,045,000 at third quarter-end 2014 and \$41,795,000 at year-end 2013 related to our Cibolo Canyons project near San Antonio, Texas. These costs relate to water, sewer and other infrastructure assets we have submitted to utility or improvement districts for approval and reimbursement. We submitted for reimbursement to these districts \$7,118,000 and \$15,713,000 in first nine months 2014 and 2013. We collected reimbursements from these districts of \$4,504,000 and \$1,840,000 in first nine months 2014 and 2013. We expect to collect the remaining amounts billed when these districts achieve adequate tax basis or otherwise have funds available to support payment.

Also included in entitled, developed and under development projects is our investment in the resort development owned by third parties at our Cibolo Canyons project. We received \$4,050,000 and \$2,700,000 from the special improvement district in first nine months 2014 and 2013. At third quarter-end 2014, we have \$24,067,000 invested in the resort development.

In third quarter 2014, we acquired full ownership in CJUF III, RH Holdings partnership (the Eleven venture), owner of a 257-unit multifamily project in Austin in which we previously held a 25 percent interest, for \$21,500,000. The acquisition-date fair value was \$55,275,000, including debt of \$23,936,000. Our investment in the Eleven venture prior to acquiring our partner's interest was \$2,229,000. We accounted for this transaction as a business combination achieved in stages and as a result, we remeasured our equity method investment in the Eleven venture to its acquisition-date fair value of \$9,839,000 and recognized the resulting gain of \$7,610,000 in real estate segment earnings. The purchase price allocation related to the acquisition of our partner's interest in the Eleven venture is preliminary as it is subject to final valuation adjustments. At third quarter-end 2014, we recorded additions to real estate commercial and income producing properties of \$53,917,000 and other assets of \$992,000 primarily consisting of in-place tenant leases of \$865,000. In addition, we recorded a working capital deficit of \$979,000 and debt of \$23,936,000. In first nine months 2014, we also recorded a \$10,476,000 gain associated with a non-monetary exchange of leasehold timber rights on approximately 10,300 acres for 5,400 acres of undeveloped land with a partner in a consolidated venture.

In first nine months 2014, the increase in commercial and income producing properties was principally due to \$53,917,000 related to the Eleven multifamily project which is now wholly-owned after acquisition of our partner's interest in the Eleven venture, and \$26,110,000 from acquisition of three multifamily development sites. At third quarter-end 2014, commercial and income producing properties principally represents our investment in a 413 guest room hotel in Austin with a carrying value of \$29,002,000, our \$53,917,000 investment in our 257-unit multifamily property in Austin and our investment in multifamily development sites located in Austin, Charlotte, Dallas and Nashville with a combined carrying value of \$58,727,000.

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Note 4—Oil and Gas Properties and Equipment, net

Net capitalized costs, utilizing the successful efforts method of accounting, related to our oil and gas producing activities follows:

	Third Quarter-End 2014	Year-End 2013
	(In thousands)	
Unproved oil and gas properties	\$97,824	\$100,320
Proved oil and gas properties	201,905	155,262
Total capitalized costs	299,729	255,582
Less: accumulated depreciation, depletion and amortization	(39,974)	(22,941)
	\$259,755	\$232,641

In first nine months 2014, we recorded gains of \$9,041,000 principally related to the sale of 102 gross (7 net) producing oil and gas wells in Oklahoma for a gain of \$4,758,000 and the sale of 571 net mineral acres leased from others in North Dakota for a gain of \$4,283,000.

Note 5—Goodwill and Other Intangible Assets

Carrying value of goodwill and other intangible assets follows:

	Third Quarter-End 2014	Year-End 2013
	(In thousands)	
Goodwill	\$64,493	\$64,493
Identified intangibles, net	2,947	2,153
	\$67,440	\$66,646

Goodwill of \$60,619,000 represents the excess of the purchase price over the fair value of the tangible and intangible assets associated with acquisition of CREDO Petroleum Corporation (Credo) in 2012 and \$3,874,000 associated with a water resources company acquired in 2010.

Identified intangibles include \$1,681,000 in indefinite lived groundwater leases associated with a water resources company acquired in 2010, \$865,000 related to in-place tenant leases with definite lives associated with the purchase of our partner's interest in the Eleven venture and \$401,000 related to patents with definite lives associated with the Calliope Gas Recovery System, a process to increase natural gas production.

Note 6—Equity

A reconciliation of changes in equity at third quarter-end 2014 follows:

	Forestar Group Inc.	Noncontrolling Interests	Total
	(In thousands)		
Balance at year-end 2013	\$709,845	\$5,552	\$715,397
Net income	28,383	611	28,994
Distributions to noncontrolling interests	—	(2,093)	(2,093)
Contributions from noncontrolling interests	—	533	533
Dissolution of noncontrolling interests	—	1,342	1,342
Purchase of noncontrolling interests, net of deferred taxes of \$1,723,000	(2,975)	(3,273)	(6,248)
Other (primarily share-based compensation)	7,506	—	7,506
	\$742,759	\$2,672	\$745,431

In first quarter 2014, we acquired our partner's noncontrolling interests in the Lantana partnerships for \$7,971,000. Prior to acquisition of the noncontrolling interests, we were the primary beneficiary of all but one of the Lantana partnerships which were variable interest entities (VIEs) and consolidated in our financial statements. We adjusted the carrying amount of noncontrolling interests to reflect the change in our ownership interest in the partnerships. The

difference between the

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consideration paid and the carrying amount of the noncontrolling interests acquired is recognized as an adjustment to additional paid in capital attributable to Forestar, net of deferred taxes.

Note 7—Investment in Unconsolidated Ventures

At third quarter-end 2014, we have ownership interests in 14 ventures that we account for using the equity method. In third quarter 2014, we acquired full ownership in the Eleven venture for \$21,500,000. The acquisition-date fair value was \$55,275,000, including debt of \$23,936,000. Our investment in the Eleven venture prior to acquiring our partner's interest was \$2,229,000. At third quarter-end 2014, we no longer have an equity method investment in the Eleven venture.

On July 15, 2014, we entered into the FMF Littleton LLC venture with AIGGRE Littleton Common Investor LLC (AIGGRE), to develop a 385-unit multifamily property in Littleton, Colorado. We own a 25 percent interest and AIGGRE owns remaining 75 percent interest. We contributed \$4,900,000 of land and pre-development costs to the venture, net of \$9,852,000 of reimbursements received from the venture for land and pre-development costs we previously incurred. The venture obtained a senior secured construction loan in the amount of \$46,384,000 that bears interest at 30-day LIBOR plus 1.90% payable monthly, of which none was outstanding at third quarter-end 2014. We provided the lender a construction completion guaranty; a guaranty of repayment of 25 percent of the principal balance and unpaid accrued interest; and a nonrecourse carve-out guaranty. The principal guaranty will reduce from 25 percent of principal to ten percent upon achievement of certain conditions. At third quarter-end 2014, our investment in this venture is \$5,465,000.

In first quarter 2014, we entered into the CREA FMF Nashville LLC venture with Massachusetts Mutual Life Insurance Co. to develop a 320-unit multifamily property in Nashville, Tennessee. We contributed \$5,897,000 of land and pre-development costs to the venture, net of \$7,191,000 of reimbursements received from the venture for pre-development costs we previously incurred. The venture obtained a senior secured construction loan in the amount of \$51,950,000 that bears interest at 30-day LIBOR plus 2.50% per annum, of which \$20,289,000 was outstanding at third quarter-end 2014. We provided the lender a construction completion guaranty; a guaranty of repayment of 25 percent of the principal balance and unpaid accrued interest; and a nonrecourse carve-out guaranty. The principal guaranty will reduce from 25 percent of principal to zero upon achievement of certain conditions. At third quarter-end 2014, our investment in this venture is \$5,655,000.

Combined summarized balance sheet information for our ventures accounted for using the equity method follows:

	Venture Assets		Venture Borrowings ^(a)		Venture Equity		Our Investment	
	Third Quarter-End	Year-End	Third Quarter-End	Year-End	Third Quarter-End	Year-End	Third Quarter-End	Year-End
	2014	2013	2014	2013	2014	2013	2014	2013
	(In thousands)							
242, LLC ^(b)	\$26,139	\$23,751	\$2,934	\$921	\$19,286	\$19,838	\$8,819	\$9,084
CJUF III, RH Holdings	—	36,320	—	18,492	—	15,415	—	3,235
CL Ashton Woods ^(c)	11,671	10,473	—	—	10,277	9,704	4,370	3,544
CL Realty	8,085	8,298	—	—	7,916	8,070	3,958	4,035
CREA FMF Nashville ^(b)	28,962	—	20,289	—	6,126	—	5,655	—
FMF Littleton	21,599	—	—	—	21,148	—	5,465	—
FMF Peakview	40,137	30,673	21,088	12,533	17,617	16,620	3,605	3,406
HM Stonewall Estates ^(c)	3,367	3,781	286	63	3,081	3,718	1,751	2,128
LM Land Holdings ^(c)	32,824	33,298	9,502	9,768	19,349	13,347	9,843	8,283
PSW Communities	12,604	—	7,377	—	4,270	—	3,795	—
Temco	12,756	13,320	—	—	12,518	13,160	6,259	6,580

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Other ventures ^(d)	12,383	12,723	29,730	29,699	(32,022)	(31,357)	189	852
	\$210,527	\$172,637	\$91,206	\$71,476	\$89,566	\$68,515	\$53,709	\$41,147

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Combined summarized income statement information for our ventures accounted for using the equity method follows:

	Venture Revenues				Venture Earnings (Loss)				Our Share of Earnings (Loss)			
	Third Quarter		First Nine Months		Third Quarter		First Nine Months		Third Quarter		First Nine Months	
	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013
	(In thousands)											
242, LLC	\$88	\$37	\$1,563	\$3,168	\$(32)	\$(20)	\$448	\$817	\$(15)	\$(10)	\$236	\$438
CJUF III, RH Holdings	1,098	4	2,168	7	(305)	(133)	(956)	(357)	(305)	(133)	(956)	(357)
CL Ashton Woods (c)	790	1,355	1,859	4,246	277	477	573	1,027	373	677	826	1,817
CL Realty	413	445	1,240	1,246	294	350	846	802	147	175	423	401
CREA FMF Nashville	—	—	—	—	—	—	(25)	—	—	—	(25)	—
FMF Peakview	3	200	3	200	(109)	(98)	(261)	(137)	(21)	(19)	(52)	(27)
HM Stonewall Estates (c)	292	696	1,727	1,794	91	255	613	655	36	100	245	276
LM Land Holdings (c)	4,604	9,387	13,897	14,651	3,397	5,515	10,368	9,274	1,200	2,344	3,097	3,998
PSW Communities	—	—	—	—	(11)	—	(231)	—	(9)	—	(204)	—
Temco	79	162	793	437	42	42	158	48	21	21	79	24
Other ventures	1,329	21	1,378	5,171	691	(120)	502	(642)	589	(30)	296	34
	\$8,696	\$12,307	\$24,628	\$30,920	\$4,335	\$6,268	\$12,035	\$11,487	\$2,016	\$3,125	\$3,965	\$6,604

(a) Total includes current maturities of \$61,936,000 at third quarter-end 2014, of which \$40,697,000 is non-recourse to us, and \$37,966,000 at year-end 2013, of which \$37,822,000 is non-recourse to us.

(b) Includes unamortized deferred gains on real estate contributed by us to ventures. We recognize deferred gains as income as real estate is sold to third parties. Deferred gains of \$1,648,000 are reflected as a reduction to our investment in unconsolidated ventures at third quarter-end 2014.

(c) Includes unrecognized basis difference of \$2,011,000 which is reflected as a reduction of our investment in unconsolidated ventures at third quarter-end 2014. The difference will be accreted as income or expense over the life of the investment and included in our share of earnings (loss) from the respective ventures.

(d) Our investment in other ventures reflects our ownership interests, excluding venture losses that exceed our investment where we are not obligated to fund those losses. Please read Note 16—Variable Interest Entities for additional information.

In first nine months 2014, we contributed cash of \$5,016,000 to these ventures and received \$4,418,000 in cash distributions, and in first nine months 2013, we contributed cash of \$819,000 to these ventures and received \$2,140,000 in cash distributions. Distributions include both return of investments and distribution of earnings. From time to time, we provide performance bonds and letters of credit on behalf of certain ventures that could be drawn on due to failure to satisfy construction obligations as general contractor or for failure to timely deliver streets and utilities in accordance with local codes and ordinances. At third quarter-end 2014, we have no outstanding performance bonds or letters of credit.

Note 8—Receivables

Receivables consist of:

Year-End

	Third Quarter-End 2014	2013
	(In thousands)	
Loan secured by real estate	\$4,236	\$7,610
Other loans secured by real estate, average interest rates of 4.40% at third quarter-end 2014 and 5.00% at year-end 2013	8,234	7,987
Oil and gas joint interest billing receivables	11,220	3,896
Oil and gas revenue accruals	18,753	8,137
Other receivables and accrued interest	3,884	11,648
	46,327	39,278
Allowance for bad debts	(26) (26
	\$46,301	\$39,252

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At third quarter-end 2014, we have \$4,236,000 invested in a loan which was acquired from a financial institution in second quarter 2011 when it was non-performing and is secured by a lien on developed and undeveloped real estate located near Houston designated for single-family residential and commercial development. Interest accrues at nine percent the first three years escalating to ten percent in April 2015 and 12 percent in April 2016, with interest above 6.25 percent to be forgiven if the loan is prepaid by certain dates. In first nine months 2014, we received principal payments of \$8,912,000 and interest payments of \$530,000. At third quarter-end 2014, the outstanding principal balance was \$6,787,000.

Estimated accretable yield follows:

	Third Quarter-End 2014 (In thousands)
Beginning of period (year-end 2013)	\$8,908
Change in accretable yield due to change in timing of estimated cash flows	(347)
Interest income recognized (in first nine months 2014)	(6,068)
End of period	\$2,493

Other loans secured by real estate generally are secured by a deed of trust and due within three years.

Note 9—Debt

Debt consists of:

	Third Quarter-End 2014 (In thousands)	Year-End 2013
Senior secured credit facility		
Term loan facility — average interest rate of 4.17% at year-end 2013	\$—	\$200,000
8.50% senior secured notes due 2022	250,000	—
3.75% convertible senior notes due 2020, net of discount	102,368	99,890
6.00% tangible equity unit notes, net of discount	19,192	25,619
Secured promissory notes — average interest rates of 3.15% at third quarter-end 2014 and 3.17% at year-end 2013	15,400	15,400
Other indebtedness — interest rates ranging from 2.19% to 5.50% at third quarter-end 2014	42,335	16,498
	\$429,295	\$357,407

Our debt agreements contain financial covenants customary for such agreements including minimum levels of interest coverage and limitations on leverage. At third quarter-end 2014, we were in compliance with the financial covenants of these agreements.

In second quarter 2014, we amended our senior secured credit facility in order to consolidate previous amendments and to effect the following:

- increase the revolving loan commitment from \$200,000,000 to \$300,000,000;
- extend the maturity date to May 15, 2017 (with two one-year extension options);
- increase the minimum interest coverage ratio from 1.50x to 2.50x;
- eliminate the collateral value to loan commitment ratio covenant; and
- increase the maximum total leverage ratio from 40% to 50%.

We incurred fees of \$3,068,000 related to this amendment. At third quarter-end 2014, our senior secured credit facility provides for a \$300,000,000 revolving line of credit maturing May 15, 2017. The revolving line of credit may be prepaid at any time without penalty. The revolving line of credit includes a \$100,000,000 sublimit for letters of credit, of which \$10,118,000 is outstanding at third quarter-end 2014. Total borrowings under our senior secured credit facility (including the face amount of letters of credit) may not exceed a borrowing base formula. At third quarter-end 2014, we had \$289,882,000 in net unused borrowing capacity under our senior secured credit facility.

Under the terms of our senior secured credit facility, at our option we can borrow at LIBOR plus 4.0 percent or at the alternate base rate plus 3.0 percent. The alternate base rate is the highest of (i) KeyBank National Association's base rate, (ii) the federal funds effective rate plus 0.5 percent or (iii) 30 day LIBOR plus 1 percent. Borrowings under the senior secured credit facility are or may be secured by (a) mortgages on the timberland, high value timberland and portions of raw entitled

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land, as well as pledges of other rights including certain oil and gas operating properties, (b) assignments of current and future leases, rents and contracts, (c) a security interest in our primary operating account, (d) a pledge of the equity interests in current and future material operating subsidiaries and most of our majority-owned joint venture interests, or if such pledge is not permitted, a pledge of the right to distributions from such entities, and (e) a pledge of reimbursements, hotel occupancy and other revenues payable to us from special improvement district tax collections in connection with our Cibolo Canyons project. The senior secured credit facility provides for releases of real estate and other collateral provided that borrowing base compliance is maintained.

On May 12, 2014, we issued \$250,000,000 aggregate principal of 8.5% Senior Secured Notes due 2022 (Notes). The Notes will mature on June 1, 2022 and interest on the Notes is payable semiannually at a rate of 8.5 percent per annum in arrears. We incurred debt issuance costs of approximately \$8,053,000, including the underwriters discount of \$6,250,000. Net proceeds from issuance of the Notes were used to repay our \$200,000,000 senior secured term loan. We intend to use the remaining amount for general corporate purposes, which may include investments in strategic growth opportunities.

At third quarter-end 2014, secured promissory notes represent a \$15,400,000 loan collateralized by a 413 guest room hotel located in Austin with a carrying value of \$29,002,000. Other indebtedness principally represents \$38,033,000 of senior secured construction loans for two multifamily properties, of which \$23,936,000 is related to the third quarter 2014 acquisition of our partner's interest in the 257-unit multifamily project in Austin. The combined carrying value of these two multifamily properties is \$82,715,000 at third quarter-end 2014. The remaining other indebtedness is collateralized by entitled, developed and under development projects with a carrying value of \$19,239,000.

At third quarter-end 2014 and year-end 2013, we have \$16,072,000 and \$7,896,000 in unamortized deferred financing fees which are included in other assets. Amortization of deferred financing fees was \$3,089,000 and \$2,282,000 in first nine months 2014 and 2013 and is included in interest expense.

Note 10—Fair Value

Fair value is the exchange price that would be the amount received for an asset or paid to transfer a liability in an orderly transaction between market participants. In arriving at a fair value measurement, we use a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable. The three levels of inputs used to establish fair value are the following:

Level 1 — Quoted prices in active markets for identical assets or liabilities;

Level 2 — Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Non-financial assets measured at fair value on a non-recurring basis principally include real estate assets, oil and gas properties, assets held for sale, goodwill and other intangible assets, which are measured for impairment. In third quarter 2014, we recognized non-cash asset impairment charges of \$94,000 associated with a real estate project in Austin. We had no non-cash impairment charges in third quarter 2013.

We elected not to use the fair value option for cash and cash equivalents, accounts receivable, other current assets, variable debt, accounts payable and other current liabilities. The carrying amounts of these financial instruments approximate their fair values due to their short-term nature or variable interest rates. We determine the fair value of fixed rate financial instruments using quoted prices for similar instruments in active markets.

Information about our fixed rate financial instruments not measured at fair value follows:

	Third Quarter-End 2014		Year-End 2013		Valuation Technique
	Carrying Amount	Fair Value	Carrying Amount	Fair Value	
	(In thousands)				
Loan secured by real estate	\$4,236	\$7,524	\$7,610	\$18,025	Level 2
Fixed rate debt ^(a)	(371,560)	(381,619)	(126,640)	(118,634)	Level 2

(a) Third quarter-end 2014 includes our \$250,000,000 of 8.50% senior secured notes due 2022, issued May 12, 2014.

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Note 11—Capital Stock

Pursuant to our stockholder rights plan, each share of common stock outstanding is coupled with one-quarter of a preferred stock purchase right (Right). Each Right entitles our stockholders to purchase, under certain conditions, one one-hundredth of a share of newly issued Series A Junior Participating Preferred Stock at an exercise price of \$100. Rights will be exercisable only if someone acquires beneficial ownership of 20 percent or more of our common shares or commences a tender or exchange offer, upon consummation of which they would beneficially own 20 percent or more of our common shares. We will generally be entitled to redeem the Rights at \$0.001 per Right at any time until the 10th business day following public announcement that a 20 percent position has been acquired. The Rights will expire on December 11, 2017.

Please read Note 17—Share-Based Compensation for information about additional shares of common stock that could be issued under terms of our share-based compensation plans.

At third quarter-end 2014, personnel of former affiliates held options to purchase 706,000 shares of our common stock. The options have a weighted average exercise price of \$26.11 and a weighted average remaining contractual term of one year. At third quarter-end 2014, the options have an aggregate intrinsic value of \$54,300.

Note 12—Net Income per Share

Basic and diluted earnings per share is computed using the two-class method. The two-class method is an earnings allocation formula that determines net income per share for each class of common stock and participating security. We have determined that our 6.00% tangible equity units (Units) are participating securities. Per share amounts are computed by dividing earnings available to common shareholders by the weighted average shares outstanding during each period.

The computations of basic and diluted earnings per share are as follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Numerator:				
Consolidated net income	\$5,239	\$12,897	\$28,994	\$19,137
Less: Net loss (income) attributable to noncontrolling interest	(12)	(1,067)	(611)	(2,815)
Earnings available for diluted earnings per share	\$5,227	\$11,830	\$28,383	\$16,322
Less: Undistributed net income allocated to participating securities	(947)	—	(5,151)	—
Earnings available to common shareholders for basic earnings per share	\$4,280	\$11,830	\$23,232	\$16,322
Denominator:				
Weighted average common shares outstanding — basic	35,498	35,410	35,437	35,341
Weighted average common shares upon conversion of participating securities ^(a)	7,857	—	7,857	—
Dilutive effect of stock options, restricted stock and equity-settled awards	513	662	456	608
Total weighted average shares outstanding — diluted	43,868	36,072	43,750	35,949
Anti-dilutive awards excluded from diluted weighted average shares	1,959	1,764	2,171	2,022

^(a) Our earnings per share calculation reflects the weighted average shares issuable upon settlement of the prepaid stock purchase contract component of our 6.00% tangible equity units, issued November 27, 2013.

The actual number of shares we may issue upon settlement of the stock purchase contract will be between 6,547,800 shares (the minimum settlement rate) and 7,857,000 shares (the maximum settlement rate) based on the applicable market value, as defined in the purchase contract agreement associated with issuance of the Units.

We intend to settle the principal amount of our convertible senior notes (Convertible Notes) in cash upon conversion with only the amount in excess of par value of the Convertible Notes to be settled in shares of our common stock. Therefore, our calculation of diluted net income per share using the treasury stock method includes only the amount, if any, in excess of par value of the Convertible Notes. As such, the Convertible Notes have no impact on diluted net income per share until the price of our common stock exceeds the \$24.49 conversion price of the Convertible Notes. The average price of our common stock in third quarter 2014 did not exceed the conversion price which resulted in no additional diluted outstanding shares.

Note 13—Income Taxes

Our effective tax rate was 35 percent in third quarter and first nine months 2014, which includes a one percent benefit for noncontrolling interests. Our effective tax rate was a 29 percent benefit in third quarter 2013 and less than a one percent benefit in first nine months 2013, which included a four percent benefit for noncontrolling interests. Our third quarter and first nine months 2013 effective tax rates include a benefit from recognition of \$6,326,000 of previously unrecognized tax benefits upon lapse of the statute of limitations for a previously reserved tax position. Our effective tax rates in third quarter and first nine months 2013 would have been 33 percent excluding the impact of the foregoing tax benefits.

Our 2014 and 2013 effective tax rates also include the effect of state income taxes, nondeductible items and benefits of percentage depletion.

We have not provided a valuation allowance for our federal deferred tax asset because we believe it is likely it will be recoverable in future periods.

Note 14—Commitments and Contingencies

Litigation

We are involved in various legal proceedings that arise from time to time in the ordinary course of doing business and believe that adequate reserves have been established for any probable losses. We do not believe that the outcome of any of these proceedings should have a significant adverse effect on our financial position, long-term results of operations or cash flows. However, it is possible that charges related to these matters could be significant to our results or cash flows in any one accounting period.

Environmental

Environmental remediation liabilities arise from time to time in the ordinary course of doing business, and we believe we have established adequate reserves for any probable losses that we can reasonably estimate. We own 288 acres near Antioch, California, portions of which were sites of a former paper manufacturing operation that are in remediation. We have received certificates of completion on all but one 80 acre tract, a portion of which includes subsurface contamination. We estimate the remaining cost to complete remediation activities will be approximately \$810,000, which is included in other accrued expenses. It is possible that remediation or monitoring activities could be required in addition to those included within our estimate, but we are unable to determine the scope, timing or extent of such activities.

We have asset retirement obligations related to the abandonment and site restoration requirements that result from the acquisition, construction and development of oil and gas properties. We record the fair value of a liability for an asset retirement obligation in the period in which it is incurred and a corresponding increase in the carrying amount of the related long-lived asset. Accretion expense related to the asset retirement obligation and depletion expense related to capitalized asset retirement cost is included in cost of oil and gas producing activities on our consolidated statements of income and comprehensive income. At third quarter-end 2014, our asset retirement obligation was \$1,667,000, which is included in other liabilities.

Note 15—Segment Information

We manage our operations through three segments: real estate, oil and gas and other natural resources. Real estate secures entitlements and develops infrastructure on our lands for single-family residential and mixed-use communities, and manages our undeveloped land, commercial and income producing properties, primarily a hotel and our multifamily investments. Oil and gas is an independent oil and gas exploration, development and production operation and manages our owned and leased mineral interests. Other natural resources manages our timber, recreational leases and water resource initiatives.

Total assets allocated by segment are as follows:

Year-End

	Third Quarter-End 2014	2013
	(In thousands)	
Real estate	\$664,642	\$582,802
Oil and gas	355,501	312,553
Other natural resources	23,502	23,478
Assets not allocated to segments ^(a)	224,594	253,319
	\$1,268,239	\$1,172,152

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Assets not allocated to segments at third quarter-end 2014 principally consist of cash and cash equivalents of (a) \$170,606,000 and a net deferred tax asset of \$30,932,000. Assets not allocated to segments at year-end 2013 principally consist of cash and cash equivalents of \$192,307,000 and a net deferred tax asset of \$40,398,000. We evaluate performance based on segment earnings (loss) before unallocated items and income taxes. Segment earnings (loss) consist of operating income, equity in earnings (loss) of unconsolidated ventures, gain on sales of assets, interest income on loans secured by real estate and net (income) loss attributable to noncontrolling interests. Items not allocated to our business segments consist of general and administrative expense, share-based compensation, gain on sale of strategic timberland, interest expense and other corporate non-operating income and expense. The accounting policies of the segments are the same as those described in Note 1—Basis of Presentation. Our revenues are derived from U.S. operations and all of our assets are located in the U.S. In third quarter and first nine months 2014, no single customer accounted for more than ten percent of our total revenues.

Segment revenues and earnings are as follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Revenues:				
Real estate	\$32,445	\$50,356	\$153,098	\$170,264
Oil and gas	24,145	22,095	66,076	53,430
Other natural resources	2,250	2,656	7,284	8,963
Total revenues	\$58,840	\$75,107	\$226,458	\$232,657
Segment earnings:				
Real estate	\$15,987	\$13,197	\$66,859	\$40,747
Oil and gas	6,002	8,499	16,331	17,869
Other natural resources	669	549	2,220	2,792
Total segment earnings	22,658	22,245	85,410	61,408
Items not allocated to segments (a)	(14,676)	(13,347)	(41,563)	(45,114)
Income before taxes attributable to Forestar Group Inc.	\$7,982	\$8,898	\$43,847	\$16,294

(a) Items not allocated to segments consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
General and administrative expense	\$(5,190)	\$(4,648)	\$(15,924)	\$(14,935)
Shared-based compensation expense	(991)	(3,492)	(4,523)	(15,367)
Interest expense	(8,634)	(5,231)	(21,507)	(14,892)
Other corporate non-operating income	139	24	391	80
	\$(14,676)	\$(13,347)	\$(41,563)	\$(45,114)

Note 16—Variable Interest Entities

We participate in real estate ventures for the purpose of acquiring and developing residential, multifamily and mixed-use communities in which we may or may not have a controlling financial interest. Generally accepted accounting principles require consolidation of VIEs in which an enterprise has a controlling financial interest and is the primary beneficiary. A controlling financial interest will have both of the following characteristics: (a) the power to direct the VIE activities that most significantly impact economic performance and (b) the obligation to absorb the VIE losses and right to receive benefits that are significant to the VIE. We examine specific criteria and use judgment when determining whether we are the primary beneficiary and must consolidate a VIE. We perform this review initially at the time we enter into venture agreements and continuously reassess to see if we are the primary beneficiary of a VIE.

At third quarter-end 2014, we have four VIEs. We account for these VIEs using the equity method and we are not the primary beneficiary. Although we have certain rights regarding major decisions, we do not have the power to direct

the activities that are most significant to the economic performance of these VIEs. At third quarter-end 2014, these VIEs have total assets of \$53,747,000, substantially all of which represent developed and undeveloped real estate, and total liabilities of \$75,575,000, which includes \$31,060,000 of borrowings classified as current maturities. These amounts are included in the

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summarized balance sheet information for ventures accounted for using the equity method in Note 7—Investment in Unconsolidated Ventures. At third quarter-end 2014, our investment in these VIEs is \$9,507,000 and is included in investment in unconsolidated ventures. In first nine months 2014, we contributed \$4,378,000 to these VIEs. Our maximum exposure to loss related to one of these VIEs is estimated at \$3,627,000, which exceeds our investment as we have a nominal general partner interest and could be held responsible for its liabilities. The maximum exposure to loss represents the maximum loss that we could be required to recognize assuming all the ventures' assets (principally real estate) are worthless, without consideration of the probability of a loss or of any actions we may take to mitigate any such loss.

Note 17—Share-Based Compensation

Share-based compensation expense consists of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Cash-settled awards	\$(801)	\$1,823	\$(1,996)	\$7,498
Equity-settled awards	1,307	899	4,897	3,565
Restricted stock	22	85	101	541
Stock options	463	685	1,521	3,763
	\$991	\$3,492	\$4,523	\$15,367

Share-based compensation expense is included in:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
General and administrative expense	\$(50)	\$1,297	\$1,217	\$7,310
Other operating expense	1,041	2,195	3,306	8,057
	\$991	\$3,492	\$4,523	\$15,367

In first nine months 2014, we granted 92,800 cash-settled awards and 467,200 equity-settled awards. Equity-settled awards granted to employees in the first nine months 2014 include restricted stock units (RSUs), market-leveraged stock units (MSUs) and performance stock units (PSUs). Cash-settled RSUs vest ratably over three years from the date of grant. Equity-settled RSUs, MSUs and PSUs vest after three years from the date of grant upon achievement of market conditions for MSUs and upon achievement of performance goals for PSUs. Equity-settled awards in the form of RSUs granted to our directors are fully vested at the time of grant and are issued upon retirement. There were no restricted stock awards or stock options granted in first nine months 2014.

The fair value of awards granted to retirement eligible employees and expensed at the date of grant was \$760,000 and \$590,000 in first nine months 2014 and 2013. Unrecognized share-based compensation expense related to non-vested equity-settled awards, restricted stock and stock options is \$10,950,000 at third quarter-end 2014.

In first nine months 2014 and 2013, we issued 211,333 and 118,472 shares out of our treasury stock associated with vesting of stock-based awards or exercise of stock options, net of 54,272 and 59,172 shares withheld having a value of \$1,024,000 and \$1,128,000 for payroll taxes in connection with vesting of stock-based awards or exercise of stock options.

Note 18—Subsequent Event

Cibolo Canyons—San Antonio, Texas

On October 24, 2014, we received \$46,500,000 from the Cibolo Canyons Special Improvement District (CCSID) under 2007 economic development agreements in connection with development of the JW Marriott Hill Country Resort & Spa at our Cibolo Canyons project near San Antonio. CCSID funded payment to us from its issuance of \$48,900,000 Hotel Occupancy Tax (HOT) and Sales and Use Tax Revenue Bonds. These bonds are obligations solely of CCSID and are payable from HOT and sales and use taxes levied by CCSID.

The resort hotel owner, SA Real Estate, LLLP (SARE), previously had senior rights to certain payments from CCSID to be funded by HOT and sales and use taxes. To facilitate issuance of the bonds by CCSID, SARE assigned these rights to us so that we could subordinate the rights to the rights of bondholders. In return, we provided SARE a

\$10,000,000 surety bond

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securing the entire obligation. The surety bond will decrease as CCSID satisfies its payment obligation to SARE, which is scheduled to be retired in full by 2020.

In addition, we provided a \$6,846,000 letter of credit to the bond trustee as security for certain debt service fund obligations in the event CCSID tax collections are not sufficient to support payment of the bonds in accordance with their terms. The letter of credit must be maintained until the earlier of redemption of the bonds or scheduled bond maturity in 2034. If the letter of credit is drawn upon in part or in full, we are not required to replenish the letter of credit.

At third quarter-end 2014, we had \$24,067,000 invested in the resort development against which we expect to apply proceeds resulting in a recovery of our full investment in fourth quarter 2014.

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Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

Management’s Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with the financial statements and Management’s Discussion and Analysis of Financial Condition and Results of Operations in our 2013 Annual Report on Form 10-K. Unless otherwise indicated, information is presented as of third quarter-end 2014, and references to acreage owned includes all acres owned by ventures regardless of our ownership interest in a venture.

Forward-Looking Statements

This Quarterly Report on Form 10-Q and other materials we have filed or may file with the Securities and Exchange Commission contain “forward-looking statements” within the meaning of the federal securities laws. These forward-looking statements are identified by their use of terms and phrases such as “believe,” “anticipate,” “could,” “estimate,” “likely,” “intend,” “may,” “plan,” “expect,” and similar expressions, including references to assumptions. These statements reflect our current views with respect to future events and are subject to risks and uncertainties. We note that a variety of factors and uncertainties could cause our actual results to differ significantly from the results discussed in the forward-looking statements. Factors and uncertainties that might cause such differences include, but are not limited to: general economic, market or business conditions in Texas or Georgia, where our real estate activities are concentrated;

- our ability to achieve some or all of our strategic initiatives;
- the opportunities (or lack thereof) that may be presented to us and that we may pursue;
- our ability to hire and retain key personnel;
- significant customer concentration;
- future residential, multifamily or commercial entitlements, development approvals and the ability to obtain such approvals;
- obtaining approvals of reimbursements and other payments from special improvement districts and the timing of such payments;
- accuracy of estimates and other assumptions related to investment in and development of real estate, the expected timing and pricing of land and lot sales and related cost of real estate sales, impairment of long-lived assets, income taxes, share-based compensation, oil and gas reserves, revenues, capital expenditures and lease operating expense accruals associated with our oil and gas working interests, and depletion of our oil and gas properties;
- the levels of resale housing inventory and potential impact of foreclosures in our mixed-use development projects and the regions in which they are located;
- fluctuations in costs and expenses, including impacts from shortages in materials or labor;
- demand for new housing, which can be affected by a number of factors including the availability of mortgage credit;
- demand for multifamily communities, which can be affected by a number of factors including local markets and economic conditions;
- competitive actions by other companies;
- changes in governmental policies, laws or regulations and actions or restrictions of regulatory agencies;
- risks associated with oil and gas exploration, drilling and production activities;
- fluctuations in oil and gas commodity prices;
- government regulation of exploration and production technology, including hydraulic fracturing;
- the results of financing efforts, including our ability to obtain financing with favorable terms, or at all;
- our ability to make interest and principal payments on our debt and satisfy the other covenants contained in our senior credit facility, indentures and other debt agreements;
- our partners’ ability to fund their capital commitments and otherwise fulfill their operating and financial obligations;
- the effect of limitations, restrictions and natural events on our ability to harvest and deliver timber;
- inability to obtain permits for, or changes in laws, governmental policies or regulations affecting, water withdrawal or usage;
- the final resolutions or outcomes with respect to our contingent and other liabilities related to our business; and

our ability to execute our growth strategy and deliver acceptable returns from acquisitions and other investments.

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Other factors, including the risk factors described in Item 1A of our 2013 Annual Report on Form 10-K, may also cause actual results to differ materially from those projected by our forward-looking statements. New factors emerge from time to time and it is not possible for us to predict all such factors, nor can we assess the impact of any such factor on our business or the extent to which any factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement.

Any forward-looking statement speaks only as of the date on which such statement is made, and, except as required by law, we expressly disclaim any obligation or undertaking to disseminate any updates or revisions to any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events.

Strategy

Our strategy is:

Recognizing and responsibly delivering the greatest value from every acre; and

Growing through strategic and disciplined investments.

2014 Strategic Initiatives

On February 13, 2014, we announced Growing FORward, new strategic initiatives designed to further enhance shareholder value by:

Growing segment earnings through strategic and disciplined investments,

Increasing returns, and

Repositioning non-core assets.

Results of Operations

A summary of our consolidated results by business segment follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Revenues:				
Real estate	\$32,445	\$50,356	\$153,098	\$170,264
Oil and gas	24,145	22,095	66,076	53,430
Other natural resources	2,250	2,656	7,284	8,963
Total revenues	\$58,840	\$75,107	\$226,458	\$232,657
Segment earnings:				
Real estate	\$15,987	\$13,197	\$66,859	\$40,747
Oil and gas	6,002	8,499	16,331	17,869
Other natural resources	669	549	2,220	2,792
Total segment earnings	22,658	22,245	85,410	61,408
Items not allocated to segments:				
General and administrative expense	(5,190)	(4,648)	(15,924)	(14,935)
Share-based compensation expense	(991)	(3,492)	(4,523)	(15,367)
Interest expense	(8,634)	(5,231)	(21,507)	(14,892)
Other corporate non-operating income	139	24	391	80
Income before taxes	7,982	8,898	43,847	16,294
Income tax (expense) benefit	(2,755)	2,932	(15,464)	28
Net income attributable to Forestar Group Inc.	\$5,227	\$11,830	\$28,383	\$16,322

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Significant aspects of our results of operations follow:

Third Quarter and First Nine Months 2014

Third quarter 2014 real estate segment earnings were up compared with third quarter 2013 due principally to a gain of \$7,610,000 associated with the acquisition of our partner's interest in the Eleven multifamily venture, which more than offset lower undeveloped land sales, commercial acre tract sales, and residential lot sales activity. First nine months 2014 real estate segment earnings were up compared with first nine months 2013 principally due to increased undeveloped land sales, a \$10,476,000 gain associated with a non-monetary exchange of leasehold timber rights for 5,400 acres of undeveloped land with a partner in a consolidated venture and higher residential lot sales activity. First nine months 2013 real estate segment earnings benefited from sale of Promesa, a 289-unit multifamily property we developed in Austin, for \$41,000,000, which generated approximately \$10,881,000 in segment earnings.

Third quarter 2014 oil and gas segment earnings were down compared with third quarter 2013 principally due to higher exploration costs and lower production volumes, lease bonus and delay rental revenues associated with our owned mineral interests, which were partially offset by a gain of \$3,335,000 related to the sale of oil and gas properties in North Dakota and Oklahoma and higher working interest oil production volume. First nine months 2014 oil and gas segment earnings were down compared with first nine months 2013 principally due to higher exploration costs, lower production volumes, lease bonus and delay rental revenues associated with our owned mineral interests and higher operating expenses, which were partially offset by gains of \$9,041,000 related to sale of oil and gas properties in North Dakota and Oklahoma and higher working interest production volumes.

Third quarter 2014 other natural resources segment earnings benefited from lower operating costs, a groundwater reservation agreement which generated \$250,000 in segment revenues and a \$165,000 gain associated with sale of water rights associated with a real estate project in Colorado, partially offset by lower fiber volumes compared with third quarter 2013. First nine months 2014 other natural resources segment earnings declined compared to first nine months 2013 principally due to lower fiber volumes, partially offset principally due to a groundwater reservation agreement which generated \$1,000,000 in segment revenues, lower operating costs and a \$685,000 gain from a partial termination of a timber lease.

Share-based compensation expense decreased principally as result of a 17 percent decrease in our stock price since year-end 2013, compared with a 24 percent increase in our stock price in first nine months 2013 since year-end 2012, which impacted the value of vested cash-settled awards.

Third quarter and first nine months 2014 interest expense increased primarily due to higher average borrowing rates and increased debt outstanding.

Third Quarter and First Nine Months 2013

Third quarter and first nine months 2013 real estate segment earnings increased due to higher average prices for lots and commercial acres sold, higher lot sales volume and higher undeveloped land sales from our retail land sales program offset partially by lower commercial acres sold as compared with third quarter 2012. First nine months 2013 real estate segment earnings benefited from sale of Promesa, a 289-unit multifamily property we developed in Austin, for \$41,000,000, which generated approximately \$10,881,000 in segment earnings. In addition, first nine months 2013 segment earnings also benefited from increased residential lot sales activity, undeveloped land sales from our retail program and commercial tract sales.

Oil and gas segment earnings for the third quarter and first nine months 2013 increased principally due to higher working interest production volume and earnings attributable to our exploration and production operations on leased mineral interests as result of our acquisition of Credo in third quarter 2012 and higher average oil and natural gas prices, partially offset by lower oil and gas production volumes and reduced lease bonus and delay rental payments received related to our owned mineral interests.

Third quarter 2013 other natural resources segment earnings remained flat. Higher average fiber prices were offset by lower volumes primarily due to scheduled maintenance outages taken by our customers in the quarter. First nine months 2013 other natural resources segment earnings benefited from higher levels of timber harvesting activity driven by increased customer demand compared to first nine months 2012.

Share-based compensation expense fluctuations are primarily driven by changes in our stock price. First nine month 2013 share-based compensation expense increased principally as result of a 24 percent increase in our

stock price since year-end 2012, compared with a 10 percent increase in our stock price in first nine months 2012 since year-end 2011, which impacted the value of vested cash-settled awards.

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Current Market Conditions

Sales of new U.S. single-family homes rose to a six-year high in September 2014, on a seasonally adjusted basis, but a sharp downward revision to August's sales pace indicates the housing recovery remains tentative. Inventories of new homes are at historically low levels in many areas. In addition, declining finished lot inventories and supply of economically developable raw land is increasing demand for our developed lots. However, national and global economic weakness and uncertainty, and a restrictive mortgage lending environment continue to threaten a robust recovery in the housing market, despite low interest rates. Multifamily market conditions continue to be strong, with many markets experiencing healthy occupancy levels and positive rent growth. This improvement has been driven primarily by limited housing inventory, reduced single-family mortgage credit availability, and the increased propensity to rent among the 18 to 34 year old demographic of the U.S. population.

Oil prices posted their biggest one-day drop in nearly two years on October 14, 2014 due to weakening global demand and the strength of U.S. domestic oil production. The International Energy Agency cut its full-year oil-demand growth forecast to the lowest level in five years. Exploration and development activity continues to be oil focused due to the premium price of oil over gas when comparing energy equivalency and current estimates of domestic gas producing supplies are believed to be sufficient. However, the impact of lower oil prices on well economics could impact future exploration and development activity.

Gas prices are up nearly 12 percent from year ago levels, but are significantly lower than realized prices over the last decade. Prolonged cold weather throughout the 2013 - 2014 heating season has taken working gas in storage below the previous five year average (2009 - 2013) causing gas prices to recover from their lows of a year ago.

Business Segments

We manage our operations through three business segments:

Real estate,

Oil and gas, and

Other natural resources.

We evaluate performance based on segment earnings (loss) before unallocated items and income taxes. Segment earnings (loss) consist of operating income, equity in earnings (loss) of unconsolidated ventures, gain on sales of assets, interest income on loans secured by real estate and net (income) loss attributable to noncontrolling interests. Items not allocated to our business segments consist of general and administrative expense, share-based compensation, gain on sale of strategic timberland, interest expense and other corporate non-operating income and expense. The accounting policies of the segments are the same as those described in the accounting policy note to the consolidated financial statements.

We operate in cyclical industries. Our operations are affected to varying degrees by supply and demand factors and economic conditions including changes in interest rates, availability of mortgage credit, consumer and home builder sentiment, new housing starts, real estate values, employment levels, changes in the market prices for oil, gas and timber, and the overall strength or weakness of the U.S. economy.

Real Estate

We own directly or through ventures approximately 120,000 acres of real estate located in ten states and 13 markets. Our real estate segment secures entitlements and develops infrastructure on our lands, primarily for single-family residential and mixed-use communities. We own approximately 98,000 acres in a broad area around Atlanta, Georgia, with the balance located primarily in Texas. We target investments principally in our strategic growth corridors, regions across the southern half of the United States that possess key demographic and growth characteristics that we believe make them attractive for long-term real estate investment. We own and manage our projects either directly or through ventures. Our real estate segment revenues are principally derived from the sales of residential single-family lots and tracts, undeveloped land and commercial real estate, and from the operation of income producing properties, primarily a hotel and multifamily properties we may develop and sell as a merchant builder.

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A summary of our real estate results follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Revenues	\$32,445	\$50,356	\$153,098	\$170,264
Cost of sales	(20,053)	(31,955)	(88,262)	(113,263)
Operating expenses	(7,604)	(8,498)	(24,994)	(23,179)
	4,788	9,903	39,842	33,822
Interest income on loan secured by real estate	1,757	1,435	6,068	3,631
Gain on asset purchase and non-monetary exchange	7,610	—	18,086	—
Equity in earnings of unconsolidated ventures	1,844	2,926	3,474	6,109
Less: Net income attributable to noncontrolling interests	(12)	(1,067)	(611)	(2,815)
Segment earnings	\$15,987	\$13,197	\$66,859	\$40,747

In first nine months 2014, revenues were principally driven by increased residential real estate and undeveloped land sales. First nine months 2013 revenues include \$41,000,000 as a result of the first quarter 2013 sale of Promesa, a 289-unit multifamily property in Austin which we developed and sold as a merchant builder.

In third quarter and first nine months 2014, cost of sales includes \$4,649,000 and \$13,690,000 related to multifamily construction contract costs we incurred as general contractor and paid to subcontractors associated with our development of two multifamily venture properties. We incurred charges of \$1,784,000 and \$4,131,000 in third quarter and first nine months 2014 reflecting estimated cost increases associated with our fixed fee contracts as general contractor for these two multifamily venture properties. Cost of sales associated with multifamily construction contracts for third quarter and first nine months 2013 were \$9,583,000 and \$27,189,000. First nine months 2013 cost of sales also included \$29,707,000 in carrying value related to Promesa, a 289-unit multifamily property we developed as a merchant builder and sold.

Interest income principally represents earnings from a loan we hold which is secured by a mixed-use real estate community in Houston.

In third quarter 2014, we acquired full ownership in CJUF III, RH Holdings partnership (the Eleven venture), owner of a 257-unit multifamily project in Austin in which we previously held a 25 percent interest, for \$21,500,000. The acquisition-date fair value was \$55,275,000, including debt of \$23,936,000. Our investment in the Eleven venture prior to acquiring our partner's interest was \$2,229,000. We accounted for this transaction as a business combination achieved in stages and as a result, we remeasured our equity method investment in the Eleven venture to its acquisition-date fair value of \$9,839,000 and recognized the resulting gain of \$7,610,000 in real estate segment earnings. Also in first nine months 2014, we recorded a \$10,476,000 gain associated with a non-monetary exchange of leasehold timber rights on approximately 10,300 acres for 5,400 acres of undeveloped land with a partner in a consolidated venture.

In first nine months 2014, the decrease in net income attributable to noncontrolling interests compared with first nine months 2013 is principally due to the purchase of noncontrolling interests in the Lantana ventures for \$7,971,000 in March 2014.

Revenues in our owned and consolidated ventures consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Residential real estate	\$20,714	\$28,298	\$89,876	\$65,748
Commercial real estate	166	1,083	946	4,521
Undeveloped land	2,021	6,571	29,031	11,858
Commercial and income producing properties	9,378	13,355	30,361	85,387
Other	166	1,049	2,884	2,750
	\$32,445	\$50,356	\$153,098	\$170,264

Residential real estate revenues principally consist of the sale of single-family lots to national, regional and local homebuilders. Revenues decreased in third quarter 2014 compared with third quarter 2013 primarily due to lower residential lot and undeveloped land sales activity, which was somewhat offset by higher average price per lot sold. Revenues increased in first nine months 2014 compared with first nine months 2013 due to increased lot sales volume offset by lower average price

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per lot sold and higher undeveloped land sales. In addition, in first nine months 2014, we sold 918 undeveloped residential tract acres for \$6,617,000 which generated segment earnings of \$2,689,000, compared with the sale of 486 undeveloped residential acres of which 440 were the remaining undeveloped residential tract acres from a project in Florida for \$3,536,000, which generated approximately \$687,000 in segment earnings in first nine months 2013. In first nine months 2014, undeveloped land sales increased as compared with first nine months 2013 principally due to first quarter sale of 9,329 acres for \$19,713,000, or approximately \$2,100 per acre, generating approximately \$16,233,000 in segment earnings.

In addition, third quarter and first nine months 2014 commercial and income producing properties revenues include construction revenues of \$2,865,000 and \$9,559,000 associated with our multifamily fixed fee contracts as general contractor. We are reimbursed for costs paid to subcontractors plus we may earn a development and construction fee on certain projects, both of which are included in commercial and income producing properties revenue. Revenues associated with multifamily construction contracts for third quarter and first nine months 2013 were \$9,029,000 and \$26,635,000.

In first nine months 2014, commercial and income producing properties revenue decreased compared with first nine months 2013 as a result of the first quarter 2013 sale of Promesa, a 289-unit multifamily property in Austin which we developed and sold as a merchant builder for \$41,000,000 generating segment earnings of \$10,881,000.

In first nine months 2014, revenues related to our 413 guest room hotel in Austin were up \$3,007,000 when compared with first nine months 2013, primarily due to a higher average room rates and increased food and beverage sales.

Units sold in our owned and consolidated ventures consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
Owned and consolidated ventures:				
Residential Lots Sold	286	414	1,603	1,028
Revenue per Lot Sold	\$72,352	\$56,866	\$52,052	\$55,417
Commercial Acres Sold	—	2	3	37
Revenue per Commercial Acre Sold	\$—	\$426,554	\$96,774	\$115,892
Undeveloped Acres Sold	637	1,314	12,916	3,233
Revenue per Acre Sold	\$3,179	\$5,001	\$2,248	\$3,668
Ventures accounted for using the equity method:				
Residential Lots Sold	37	133	231	325
Revenue per Lot Sold	\$83,711	\$55,251	\$70,325	\$54,752
Commercial Acres Sold	4	17	4	19
Revenue per Commercial Acre Sold	\$589,203	\$239,710	\$589,203	\$277,739
Undeveloped Acres Sold	—	26	258	68
Revenue per Acre Sold	\$—	\$2,650	\$2,306	\$2,650

Operating expenses consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Employee compensation and benefits	\$2,605	\$2,434	\$8,118	\$5,708
Property taxes	1,558	1,669	5,043	5,714
Professional services	807	871	4,218	2,997
Depreciation and amortization	725	721	2,068	2,463
Other	1,909	2,803	5,547	6,297
	\$7,604	\$8,498	\$24,994	\$23,179

The increase in employee compensation and benefits in first nine months 2014 is principally related to increase in staffing and incentive compensation. The increase in professional services in first nine months 2014 is primarily associated with conveyance of land in payment of management fees in a consolidated venture associated with non-monetary exchange of leasehold timber rights for undeveloped land.

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Information about our real estate projects and our real estate ventures follows:

	Third Quarter-End 2014	2013
Owned and consolidated ventures:		
Entitled, developed and under development projects		
Number of projects	65	65
Residential lots remaining	14,772	19,378
Commercial acres remaining	1,722	2,020
Undeveloped land and land in the entitlement process		
Number of projects	11	13
Acres in entitlement process	24,430	25,830
Acres undeveloped	78,918	87,714
Ventures accounted for using the equity method:		
Ventures' entitled, developed and under development projects		
Number of projects	8	7
Residential lots remaining	2,984	3,380
Commercial acres remaining	236	289
Ventures' undeveloped land and land in the entitlement process		
Acres undeveloped	5,073	5,587

We underwrite development projects based on a variety of assumptions incorporated into our development plans, including the timing and pricing of sales and leasing and costs to complete development. Our development plans are periodically reviewed in comparison to our return projections and expectations, and we may revise our plans as business conditions warrant. If as a result of changes to our development plans the anticipated future net cash flows are reduced such that our basis in a project is not fully recoverable, we may be required to recognize a non-cash impairment charge for such project.

Our net investment in owned and consolidated real estate by geographic location follows:

State	Entitled, Developed, and Under Development Projects (In thousands)	Undeveloped Land and Land in Entitlement Process	Commercial and Income Producing Properties	Total
Texas	\$273,534	\$6,000	\$132,882	\$412,416
Georgia	17,502	65,074	—	82,576
Colorado	25,368	—	—	25,368
California	8,915	22,645	—	31,560
North Carolina	—	35	14,678	14,713
Tennessee	9,932	371	7,451	17,754
Other	7,302	116	—	7,418
	\$342,553	\$94,241	\$155,011	\$591,805

Oil and Gas

Our oil and gas segment is focused on the exploration, development and production of oil and gas on our mineral and leasehold interests.

We are an independent oil and gas exploration, development and production company. We have approximately 358,000 net mineral acres of leasehold interests principally located in Nebraska, Kansas, Oklahoma, Texas and North Dakota. At third quarter-end 2014, our working interest investments are principally targeting the Bakken and Three Forks, Lansing-Kansas City and Tonkawa and Cleveland formations. Our leasehold interests include 46,000 net acres held by production and 414 gross oil and gas wells with working interest ownership, of which 202 are operated by us.

These leasehold interests include about 8,000 net mineral acres in North Dakota focused on the Bakken and Three Forks formations.

In addition, we lease portions of our 590,000 owned net mineral acres located principally in Texas, Louisiana, Georgia and Alabama to other oil and gas companies in return for a lease bonus, delay rentals and a royalty interest. At third quarter-end 2014, we have about 20,000 net acres leased to others, about 36,000 net acres leased to others that are held by production and

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547 gross productive wells operated by others on our owned mineral acres. Most leases are for a three to five year term although all or a portion of a lease may be extended as long as actual production is occurring.

A summary of our oil and gas results follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Revenues	\$24,145	\$22,095	\$66,076	\$53,430
Cost of oil and gas producing activities	(18,470)	(10,090)	(48,016)	(26,762)
Operating expenses	(3,164)	(3,683)	(11,235)	(9,253)
	2,511	8,322	6,825	17,415
Gain on sale of assets	3,335	—	9,041	—
Equity in earnings of unconsolidated ventures	156	177	465	454
Segment earnings	\$6,002	\$8,499	\$16,331	\$17,869

In third quarter 2014, we recorded gains of \$3,335,000 principally related to sale of 348 net mineral acres leased from others in North Dakota for a gain of \$3,065,000 and sale of 5 gross (1 net) producing oil and gas wells in Oklahoma for a gain of \$270,000.

In first nine months 2014, we recorded gains of \$9,041,000 principally related to sale of 102 gross (7 net) producing oil and gas wells in Oklahoma for a gain of \$4,758,000 and sale of 571 net mineral acres leased from others in North Dakota for a gain of \$4,283,000.

Revenues consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Oil production ^(a)	\$22,053	\$18,120	\$59,057	\$45,496
Gas production	1,913	1,782	5,694	4,966
Other	179	2,193	1,325	2,968
	\$24,145	\$22,095	\$66,076	\$53,430

^(a) Oil production includes revenues from oil, condensate and natural gas liquids (NGLs).

In third quarter 2014, oil and gas production revenues increased principally as a result of higher production volumes. Increased oil production volume contributed \$7,022,000, partially offset by decreased oil prices which negatively impacted revenues by \$3,089,000. Decreased gas production volume negatively impacted revenues by \$112,000, offset by higher gas prices increasing revenues by \$243,000 as compared with third quarter 2013.

In first nine months 2014, oil and gas production revenues increased principally as a result of higher production volumes. Increased oil production volume contributed \$15,280,000, partially offset by decreased oil prices which negatively impacted revenues by \$1,719,000. Decreased gas production volume negatively impacted revenues by \$540,000, offset by higher gas prices increasing revenues by \$1,268,000 as compared with first nine months 2013.

In first nine months 2014, other revenues include \$1,236,000 in lease bonuses received from leasing approximately 3,900 net mineral acres owned in Texas and Louisiana compared to \$2,233,000 in lease bonuses received from leasing approximately 8,400 net mineral acres owned in Texas and Louisiana in first nine months 2013. In first nine months 2013, other revenues include \$562,000 in delay rental payments received from others associated with our owned mineral interests principally related to extending the lease term on approximately 1,800 net mineral acres.

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Cost of oil and gas producing activities consists of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Depletion and amortization	\$8,098	\$5,048	\$19,907	\$12,939
Exploration costs	4,764	1,713	14,082	5,124
Production costs	5,389	3,265	13,694	8,417
Other	219	64	333	282
	\$18,470	\$10,090	\$48,016	\$26,762

In first nine months 2014, cost of oil and gas producing activities increased compared with first nine months 2013 due to higher exploration, production and depletion expenses. Depletion and amortization represent the non-cash cost of producing oil and gas associated with our working interests and is computed based on the units of production method. Exploration costs principally represent exploratory dry hole costs, geological and geophysical and seismic study costs. Dry hole costs in third quarter 2014 were \$3,802,000, which includes \$2,338,000 associated with a well in Oklahoma, \$1,414,000 primarily in Kansas and Nebraska and \$50,000 in east Texas compared with dry hole costs of \$910,000 in third quarter 2013. Dry hole costs in first nine months 2014 were \$9,467,000, which includes \$4,938,000 primarily in Kansas and Nebraska, \$2,338,000 associated with a well in Oklahoma and \$2,191,000 in east Texas, compared with dry hole costs of \$2,206,000 in first nine months 2013.

As a result of expiring leasehold, we recorded non-cash charges on our unproved oil and gas properties of \$2,074,000 in first nine months 2014. No non-cash charges related to expiring leases were recorded in first nine months 2013. Periodic assessment of proved oil and gas properties did not result in any impairment charges for first nine months 2014 or 2013.

Production costs principally represent lease operating expenses associated with producing working interest wells and our share of production severance taxes related to both our royalty and working interests.

Oil and gas produced and average unit prices related to our royalty and working interests follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
Consolidated entities:				
Oil production (barrels)	250,500	177,500	632,800	463,600
Average oil price per barrel	\$86.13	\$100.13	\$90.73	\$95.64
NGL production (barrels)	11,500	11,400	38,500	39,000
Average NGL price per barrel	\$41.12	\$30.46	\$42.56	\$29.68
Total oil production (barrels), including NGLs	262,000	188,900	671,300	502,600
Average total oil price per barrel, including NGLs	\$84.16	\$95.95	\$87.97	\$90.53
Gas production (millions of cubic feet)	450.6	480.5	1,293.8	1,451.6
Average price per thousand cubic feet	\$4.25	\$3.71	\$4.40	\$3.42
Our share of ventures accounted for using the equity method:				
Gas production (millions of cubic feet)	49.1	60.9	152.3	188.9
Average price per thousand cubic feet	\$4.21	\$3.66	\$4.07	\$3.30
Total consolidated and our share of equity method ventures:				
Oil production (barrels)	250,500	177,500	632,800	463,600
Average oil price per barrel	\$86.13	\$100.13	\$90.73	\$95.64
NGL production (barrels)	11,500	11,400	38,500	39,000
Average NGL price per barrel	\$41.12	\$30.46	\$42.56	\$29.68
Total oil production (barrels), including NGLs	262,000	188,900	671,300	502,600
Average total oil price per barrel, including NGLs	\$84.16	\$95.95	\$87.97	\$90.53
Gas production (millions of cubic feet)	499.7	541.4	1,446.1	1,640.5
Average price per thousand cubic feet	\$4.24	\$3.70	\$4.37	\$3.41

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Total BOE (barrel of oil equivalent) ^(a)	345,400	279,100	912,400	776,000
Average price per barrel of oil equivalent	\$70.00	\$72.11	\$71.65	\$65.83

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(a) Gas is converted to barrels of oil equivalent (BOE) using a conversion of six Mcf to one barrel of oil.

Operating expenses consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Employee compensation and benefits	\$2,291	\$2,116	\$7,305	\$5,746
Professional and consulting services	156	462	833	922
Depreciation	241	342	756	866
Other	476	763	2,341	1,719
	\$3,164	\$3,683	\$11,235	\$9,253

First nine months 2014 operating expenses increased compared with first nine months 2013, primarily as a result of increased personnel costs for additional staffing hired in the second half of 2013 to support our oil and gas operations as an independent exploration, development and production company.

Other Natural Resources

Our other natural resources segment manages our timber holdings, recreational leases and water resource initiatives. At third quarter-end 2014, we have about 108,000 real estate acres we own directly or through ventures, primarily in Georgia, with timber, and about 2,000 acres of timber under lease. Our other natural resources segment revenues are principally derived from the sales of wood fiber from our land and leases for recreational uses. We have water interests in approximately 1.5 million acres, including a 45 percent nonparticipating royalty interest in groundwater produced or withdrawn for commercial purposes or sold from 1.4 million acres in Texas, Louisiana, Georgia and Alabama, and approximately 20,000 acres of ground water leases in central Texas.

A summary of our other natural resources results follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Revenues	\$2,250	\$2,656	\$7,284	\$8,963
Cost of sales	(711)	(454)	(2,288)	(1,662)
Operating expenses	(1,051)	(1,675)	(3,652)	(4,550)
	488	527	1,344	2,751
Gain on sale and partial termination of timber lease	165	—	850	—
Equity in earnings of unconsolidated ventures	16	22	26	41
Segment earnings	\$669	\$549	\$2,220	\$2,792

Cost of sales principally includes non-cash cost of timber cut and sold and delay rental payments paid to others related to groundwater leases in central Texas.

In third quarter 2014, we recorded a \$165,000 gain associated with sale of water rights associated with a real estate project in Colorado. In first nine months 2014, we also recorded a \$685,000 gain associated with partial termination of a timber lease related to 697 acres of undeveloped land in Georgia from a consolidated venture.

Revenues consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Fiber	\$1,770	\$2,405	\$5,514	\$8,105
Water	250	—	1,000	—
Recreational leases and other	230	251	770	858
	\$2,250	\$2,656	\$7,284	\$8,963

Third quarter and first nine months 2014 water revenues are associated with a groundwater reservation agreement.

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Fiber sold consists of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
Pulpwood tons sold	71,500	65,700	157,900	314,400
Average pulpwood price per ton	\$11.18	\$8.85	\$11.00	\$9.12
Sawtimber tons sold	21,500	74,900	100,000	202,700
Average sawtimber price per ton	\$21.31	\$21.52	\$22.38	\$22.47
Total tons sold	93,000	140,600	257,900	517,100
Average stumpage price per ton ^(a)	\$13.52	\$15.60	\$15.41	\$14.36

^(a) Average stumpage price per ton is based on gross revenues less cut and haul costs.

In first nine months 2014, total fiber revenues decreased compared with first nine months 2013, due to decreased harvest activity, offset partially by higher average prices.

Information about our recreational leases follows:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
Average recreational acres leased	107,800	118,700	111,400	120,900
Average price per leased acre	\$8.66	\$8.63	\$9.17	\$9.08

Operating expenses consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Professional and consulting services	\$230	\$607	\$1,437	\$2,157
Employee compensation and benefits	602	799	1,711	1,643
Other	219	269	504	750
	\$1,051	\$1,675	\$3,652	\$4,550

Items Not Allocated to Segments

Unallocated items represent income and expenses managed on a company-wide basis and include general and administrative expenses, share-based compensation, gain on sale of strategic timberland, interest expense and other corporate non-operating income and expense. General and administrative expenses principally consist of accounting and finance, tax, legal, human resources, internal audit, information technology and our board of directors. These functions support all of our business segments and are not allocated.

General and administrative expenses consist of:

	Third Quarter		First Nine Months	
	2014	2013	2014	2013
	(In thousands)			
Employee compensation and benefits	\$2,447	\$1,940	\$7,173	\$6,040
Professional services	733	858	2,643	2,606
Depreciation and amortization	168	218	463	660
Insurance costs	201	214	716	661
Facility costs	229	196	705	633
Other	1,412	1,222	4,224	4,335
	\$5,190	\$4,648	\$15,924	\$14,935

Income Taxes

Our effective tax rate was 35 percent in third quarter and first nine months 2014, which includes a one percent benefit for noncontrolling interests. Our effective tax rate was a 29 percent benefit in third quarter 2013 and less than one percent benefit

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in first nine months 2013, which included a four percent benefit for noncontrolling interests. Our third quarter and first nine months 2013 effective tax rates included a benefit from recognition of \$6,326,000 of previously unrecognized tax benefits upon lapse of the statute of limitations for a previously reserved tax position. Our effective tax rates in third quarter and first nine months 2013 would have been 33 percent excluding the impact of the foregoing tax benefits. Our 2014 and 2013 effective tax rates also include the effect of state income taxes, nondeductible items and benefits of percentage depletion.

We have not provided a valuation allowance for our federal deferred tax asset because we believe it is likely it will be recoverable in future periods based on considerations including taxable income in prior carryback years, future reversals of existing temporary differences, tax planning strategies and future taxable income. If these sources of income are not sufficient in future periods, we may be required to provide a valuation allowance for our federal deferred tax asset.

Capital Resources and Liquidity

Sources and Uses of Cash

We operate in cyclical industries and our cash flows fluctuate accordingly. Our principal sources of cash are proceeds from the sale of real estate and timber, the cash flow from oil and gas and income producing properties, borrowings and reimbursements from utility and improvement districts. Our principal cash requirements are for the acquisition and development of real estate and investment in oil and gas leasing and production activities, either directly or indirectly through ventures, taxes, interest and compensation. Operating cash flows are affected by the timing of the payment of real estate development expenditures and the collection of proceeds from the eventual sale of the real estate, the timing of which can vary substantially depending on many factors including the size of the project, state and local permitting requirements and availability of utilities, and by the timing of oil and gas leasing and production activities. Working capital varies based on a variety of factors, including the timing of sales of real estate and timber, oil and gas leasing and production activities, collection of receivables, reimbursement from utility and improvement districts and the payment of payables and expenses.

We regularly evaluate alternatives for managing our capital structure and liquidity profile in consideration of expected cash flows, growth and operating capital requirements and capital market conditions. We may, at any time, be considering or be in discussions with respect to the purchase or sale of our common stock, debt securities, convertible securities or a combination thereof.

Cash Flows from Operating Activities

Cash flows from our real estate development activities, undeveloped land sales, commercial and income producing properties, timber sales, income from oil and gas properties, recreational leases and reimbursements from utility and improvement districts are classified as operating cash flows.

In first nine months 2014, net cash provided by operating activities was \$36,386,000 principally due to increased residential lot sales and undeveloped land sales activity. This is partially offset by \$82,864,000 of real estate development and acquisition expenditures exceeding \$59,251,000 of real estate cost of sales. In first nine months 2013, net cash provided by operating activities was \$45,083,000 principally as result of selling Promesa, a 289-unit multifamily property we developed and sold for \$41,000,000, generating net proceeds to us of \$21,522,000. Real estate cost of sales, which include \$29,707,000 in carrying value related to the sale of Promesa, exceeded expenditures for real estate development and acquisition expenditures, which includes the acquisition of one community development site in Nashville for \$6,841,000 and a multifamily site in Charlotte for \$4,849,000.

Cash Flows from Investing Activities

Capital contributions to and capital distributions from unconsolidated ventures, business acquisitions and investment in oil and gas properties and equipment are classified as investing activities. In addition, proceeds from the sale of property and equipment, software costs and expenditures related to reforestation activities are also classified as investing activities.

In first nine months 2014, net cash used in investing activities was \$82,929,000 principally due to our investment of \$65,661,000 in oil and gas properties and equipment associated with our exploration and production operations and

purchase of our partner's interest in our 257-unit multifamily property in Austin for \$20,155,000, net of cash. In addition, we invested \$13,583,000 in property and equipment, software and reforestation, of which \$6,440,000 is related to capital expenditures on our 413 guest room hotel in Austin and \$4,954,000 is related to water well development, and a net investment in unconsolidated ventures of \$3,415,000. These are partially offset by proceeds of \$17,017,000 related to sale of certain oil and gas properties in North Dakota and Oklahoma. In first nine months 2013, net cash used for investing activities was \$62,316,000

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principally due to our investment of \$56,482,000 in oil and gas properties and equipment associated with our exploration and production operations. In addition, we invested \$6,241,000 in property and equipment, software and reforestation of which \$3,185,000 is related to capital expenditures on our 413 guest room hotel in Austin.

Cash Flows from Financing Activities

In first nine months 2014, net cash provided by financing activities was \$24,842,000 principally due to net proceeds of \$241,947,000 from the issuance of 8.5% senior secured notes, partially offset by debt payments of \$222,468,000, of which \$200,000,000 is related to retirement of the term loan associated with our senior secured credit facility, \$7,200,000 is related to payments of our amortizing notes associated with our tangible equity units, \$2,878,000 is related to debt outstanding for our Lantana partnerships and the remaining associated with payment of other indebtedness. In first nine months 2013, net cash provided by financing activities was \$61,641,000 principally due to net proceeds of \$120,795,000 from the issuance of 3.75% convertible senior notes partially offset by debt payments of \$96,915,000, of which \$68,000,000 is related to outstanding borrowings under our senior secured credit facility and \$18,902,000 is related to paying off the loan associated with Promesa.

Real Estate Acquisition and Development Activities

We secure entitlements and develop infrastructure, primarily for single family residential and mixed-use communities. We also develop and own directly or through ventures multifamily communities as income producing properties, primarily in our target markets. Once these multifamily communities reach stabilization, we market the properties for sale.

We categorize real estate development and acquisition expenditures as operating activities on the statement of cash flows. These development and acquisition expenditures include costs for development of residential lots and mixed-used communities and multifamily community projects we develop and sell as a merchant builder.

In first nine months 2014, net real estate development and acquisition expenditures were \$82,864,000 which principally includes the acquisition of four new community development sites for \$10,900,000, three multifamily sites for \$26,110,000 and real estate development costs of \$45,054,000.

Oil and Gas Drilling and Other Exploration and Development Activities

In third quarter and first nine months 2014, we participated in 31 and 97 gross wells. At third quarter-end 2014, we held interests in 961 gross productive wells. In first nine months 2014, we acquired leasehold interests in over 126,000 net mineral acres in new and existing projects for \$18,476,000. Also, leasehold interests of approximately 15,000 net mineral acres expired in the normal course of business.

For full year 2014, our current plan is to drill or participate as a non-operator in approximately 155 gross wells.

Regional allocation of our capital expenditures incurred for drilling and completion activities in first nine months 2014 as compared with our 2014 projected annual drilling and completion capital expenditures is shown below:

	Drilling and Completion Expenditures	
	First Nine Months 2014	Projected 2014
	(In thousands)	
Bakken and Three Forks formations of North Dakota	\$24,116	\$37,686
Lansing - Kansas City formation of Nebraska and Kansas	15,244	18,759
Other formations principally in Texas and Oklahoma	7,825	20,358
	\$47,185	\$76,803

Our accrued capital expenditures for drilling and completion costs and leasehold acquisitions at third quarter-end 2014 were \$14,253,000 and are included in other accrued expenses in our consolidated balance sheets. These oil and gas property additions will be reflected as cash used for investing activities in the period the accrued payables are settled.

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Our 2014 projected capital expenditures are subject to various conditions, including third-party operator drilling plans, oilfield services and equipment availability, commodity prices and drilling results. Although a portion of our capital expenditure budget is allocated to acquiring additional leasehold interest, we may decide to pursue incremental leasehold acquisitions which would require us to adjust our budget. Other factors that could cause us to adjust our projections include commodity prices, service or material costs, opportunities, changes in conditions, or the performance of wells. We will continue to assess the gas and oil price environment along with our liquidity position and may increase or decrease our capital expenditure budget for exploration, development, or acquisition opportunities accordingly.

Liquidity

In second quarter 2014, we amended our senior secured credit facility in order to consolidate previous amendments and to increase the revolving loan commitment from \$200,000,000 to \$300,000,000, extend the maturity date, increase the minimum interest coverage ratio from 1.50x to 2.50x, eliminate the collateral value to loan commitment ratio covenant and increase the maximum total leverage ratio from 40% to 50%. At third quarter-end 2014, our senior secured credit facility provides for a \$300,000,000 revolving line of credit maturing May 15, 2017 (with two one-year extension options). The revolving line of credit may be prepaid at any time without penalty. The revolving line of credit includes a \$100,000,000 sublimit for letters of credit, of which \$10,118,000 is outstanding at third quarter-end 2014. Total borrowings under our senior secured credit facility (including the face amount of letters of credit) may not exceed a borrowing base formula.

At third quarter-end 2014, net unused borrowing capacity under our senior secured credit facility is calculated as follows:

	Senior Credit Facility (In thousands)
Borrowing base availability	\$ 300,000
Less: borrowings	—
Less: letters of credit	(10,118)
	\$289,882

Our unused borrowing capacity throughout third quarter 2014 was \$289,882,000. This facility is used primarily to fund our operating cash needs, which fluctuate due to timing of residential and commercial real estate sales, undeveloped land sales, oil and gas leasing, exploration and production activities and mineral lease bonus payments received, timber sales, reimbursements from utility and improvement districts, payment of payables and expenses and capital expenditures.

Our senior secured credit facility and other debt agreements contain financial covenants customary for such agreements including minimum levels of interest coverage and limitations on leverage. At third quarter-end 2014, we were in compliance with the financial covenants of these agreements.

The following table details our compliance with the financial covenants calculated as provided in the senior credit facility:

Financial Covenant	Requirement	Third Quarter-End 2014
Interest Coverage Ratio ^(a)	≥2.50:1.0	6.02:1.0
Total Leverage Ratio ^(b)	≤50%	37.0 %
Net Worth ^(c)	≥\$593.3 million	\$702.7 million

Calculated as EBITDA (earnings before interest, taxes, depreciation, depletion and amortization), plus non-cash ^(a) compensation expense, plus other non-cash expenses, divided by interest expense excluding loan fees. This covenant is applied at the end of each quarter on a rolling four quarter basis.

^(b) Calculated as total funded debt divided by adjusted asset value. Total funded debt includes indebtedness for borrowed funds, secured liabilities, reimbursement obligations with respect to letters of credit or similar instruments, and our pro-rata share of joint venture debt outstanding. Adjusted asset value is defined as the sum of

unrestricted cash and cash equivalents, timberlands, high value timberlands, raw entitled lands, entitled land under development, minerals business, Credo asset value, special improvement district receipts (SIDR) reimbursements value, Cibolo Resort Special improvement district hotel occupancy tax (SIDHT) value and other real estate owned at book value without regard to any indebtedness and our pro rata share of joint ventures' book value without regard to any indebtedness. This covenant is applied at the end of each quarter.

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Calculated as the amount by which consolidated total assets (excluding Credo acquisition goodwill over \$50,000,000) exceeds consolidated total liabilities. At third quarter-end 2014, the requirement is \$593,287,000
 (c) computed as: \$589,367,000 plus 85 percent of the aggregate net proceeds received by us from any equity offering, plus 75 percent of all positive net income, on a cumulative basis. This covenant is applied at the end of each quarter.

To make additional discretionary investments, acquisitions, or distributions, we must maintain available liquidity equal to 10 percent of the aggregate commitments in place. At third quarter-end 2014, the minimum liquidity requirement was \$30,000,000, compared with \$458,742,000 in actual available liquidity based on the unused borrowing capacity under our senior secured credit facility plus unrestricted cash and cash equivalents. The failure to maintain such minimum liquidity does not constitute a default or event of default of our senior secured credit facility. Discretionary investments in community development may be restricted in the event that the revenue/capital expenditure ratio is less than or equal to 1.0x. At third quarter-end 2014, the revenue/capital expenditure ratio was 3.4x. Revenue is defined as total gross revenues (excluding revenues attributed to Credo and multifamily properties), plus our pro rata share of the operating revenues from unconsolidated ventures. Capital expenditures are defined as consolidated development and acquisition expenditures (excluding investments related to Credo and multifamily properties), plus our pro rata share of unconsolidated ventures' development and acquisition expenditures.

In addition, we may elect to make distributions so long as the total leverage ratio is less than 40 percent, the interest coverage is greater than 3.0:1.0 and available liquidity is not less than \$125,000,000.

On May 12, 2014, we issued \$250,000,000 aggregate principal amount of 8.50% senior secured notes due 2022 (Notes) in a private placement. The Notes will pay interest semiannually and will mature on June 1, 2022. Net proceeds from the offering were used to retire the \$200,000,000 term loan under our senior secured credit facility and pay transaction costs and expenses. The remaining net proceeds will be used for general corporate purposes, which may include strategic growth opportunities.

Contractual Obligations and Off-Balance Sheet Arrangements

On July 15, 2014, FMF Littleton LLC, an equity method venture in which we own a 25 percent interest, obtained a senior secured construction loan in the amount of \$46,384,000 to develop a 385-unit multifamily project located in Littleton, Colorado. There was no outstanding balance at third quarter-end 2014. We provided the lender with a guaranty of completion of the improvements; a guaranty for repayment of 25 percent of the principal balance and unpaid accrued interest; and a standard nonrecourse carve-out guaranty. The principal guaranty will reduce from 25 percent of principal to ten percent upon achievement of certain conditions.

In January 2014, CREA FMF Nashville LLC, an equity method venture in which we own a 30 percent interest, obtained a senior secured construction loan in the amount of \$51,950,000 to develop a 320-unit multifamily project located in Nashville, Tennessee. The outstanding balance at third quarter-end 2014 was \$20,289,000. We provided the lender with a guaranty of completion of the improvements; a guaranty for repayment of 25 percent of the principal balance and unpaid accrued interest; and a standard nonrecourse carve-out guaranty. The principal guaranty will reduce from 25 percent of principal to zero percent upon achievement of certain conditions.

In 2012, FMF Peakview LLC, an equity method venture in which we own a 20 percent interest, obtained a senior secured construction loan in the amount of \$31,550,000 to develop a 304-unit multifamily property in Denver. The outstanding balance at third quarter-end 2014 was \$21,088,000. We provided the lender with a construction completion guaranty, a repayment guaranty for 25 percent of the principal and unpaid accrued interest, and a standard non-recourse carve-out guaranty.

Cibolo Canyons—San Antonio, Texas

Cibolo Canyons consists of the JW Marriott[®] San Antonio Hill Country Resort & Spa development owned by third parties and a mixed-use development we own. We have \$75,252,000 invested in Cibolo Canyons at third quarter-end 2014.

Resort Hotel, Spa and Golf Development

In 2007, we entered into agreements to facilitate third party construction and ownership of the JW Marriott[®] San Antonio Hill Country Resort & Spa (the Resort), which includes a 1,002 room destination resort and two PGA Tour[®] Tournament Players Club[®] (TPC) golf courses. Under these agreements, we agreed to transfer to third party owners

700 acres of undeveloped land, to provide \$30,000,000 cash and to provide \$12,700,000 of other consideration principally consisting of golf course construction materials, substantially all of which has been provided.

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In exchange for our commitment to the resort, the third party owners assigned to us certain rights under an agreement between the third party owners and a legislatively created Cibolo Canyons Special Improvement District (CCSID). This agreement includes the right to receive from the CCSID 9 percent of hotel occupancy revenues and 1.5 percent of other resort sales revenues collected as taxes by the CCSID through 2034. The amount we receive will be net of annual ad valorem tax reimbursements by the CCSID to the third party owners of the resort through 2020. In addition, these payments will be net of debt service, if any, on bonds issued by the CCSID collateralized by hotel occupancy tax and other resort sales tax through 2034.

The amounts we collect under this agreement are dependent on several factors including the amount of revenues generated by and ad valorem taxes imposed on the resort and the amount of any applicable debt service incurred by the CCSID. As a result, there is significant uncertainty as to the amount and timing of collections under this agreement. Until these uncertainties are clarified, amounts collected under the agreement will be accounted for as a reduction of our investment in the resort development. The resort began operations in January 2010.

In first nine months 2014, we received \$4,050,000 in reimbursements from the CCSID. Since inception, we have received \$19,206,000 in reimbursements and have accounted for this as a reduction of our investment.

On October 24, 2014, we received \$46,500,000 from the CCSID under 2007 economic development agreements in connection with development of the Resort at our Cibolo Canyons project near San Antonio. CCSID funded payment to us from its issuance of \$48,900,000 Hotel Occupancy Tax (HOT) and Sales and Use Tax Revenue Bonds. These bonds are obligations solely of CCSID and are payable from HOT and sales and use taxes levied by CCSID.

The resort hotel owner, SA Real Estate, LLLP (SARE), previously had senior rights to certain payments from CCSID to be funded by HOT and sales and use taxes. To facilitate issuance of the bonds by CCSID, SARE assigned these rights to us so that we could subordinate the rights to the rights of bondholders. In return, we provided SARE a \$10,000,000 surety bond securing the entire obligation. The surety bond will decrease as CCSID satisfies its payment obligation to SARE, which is scheduled to be retired in full by 2020.

In addition, we provided a \$6,846,000 letter of credit to the bond trustee as security for certain debt service fund obligations in the event CCSID tax collections are not sufficient to support payment of the bonds in accordance with their terms. The letter of credit must be maintained until the earlier of redemption of the bonds or scheduled bond maturity in 2034. If the letter of credit is drawn upon in part or in full, we are not required to replenish the letter of credit.

At third quarter-end 2014, we have \$24,067,000 invested in the resort development against which we expect to apply proceeds resulting in a recovery of our full investment in fourth quarter 2014.

Mixed-Use Development

The mixed-use development we own consists of 2,100 acres planned to include approximately 1,720 residential lots and 150 commercial acres designated for multifamily and retail uses, of which 867 lots and 130 commercial acres have been sold through third quarter-end 2014.

In 2007, we entered into an agreement with the SID providing for reimbursement of certain infrastructure costs related to the mixed-use development. Reimbursements are subject to review and approval by the SID and unreimbursed amounts accrue interest at 9.75 percent. The SID's funding for reimbursements is principally derived from its ad valorem tax collections and bond proceeds collateralized by ad valorem taxes, less debt service on these bonds and annual administrative and public service expenses.

Since the amount of each reimbursement is dependent on several factors, including timing of SID approval and the SID having an adequate tax base to generate funds that can be used to reimburse us, there is uncertainty as to the amount and timing of reimbursements under this agreement. We expect to recover our investment from lot and tract sales and reimbursement of approved infrastructure costs from the SID. We have not recognized income from interest due, but not collected. As these uncertainties are clarified, we will modify our accounting accordingly.

Through third quarter-end 2014, we have submitted for reimbursement approximately \$65,465,000 and received approval for \$57,322,000 of infrastructure costs, of which we have received reimbursements totaling \$25,420,000. In first nine months 2014, we received \$1,750,000 in reimbursements from the SID. At third quarter-end 2014, we have \$40,045,000 in pending reimbursements, excluding interest. At third quarter-end 2014, we have \$51,185,000 invested in the mixed-use development.

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Critical Accounting Policies and Estimates

There have been no significant changes in our critical accounting policies or estimates from those disclosed in our 2013 Annual Report on Form 10-K.

New and Pending Accounting Pronouncements

Please read Note 2—New and Pending Accounting Pronouncements to the Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Statistical and Other Data

A summary of our real estate projects in the entitlement process ^(a) at third quarter-end 2014 follows:

Project	County	Market	Project Acres ^(b)
California			
Hidden Creek Estates	Los Angeles	Los Angeles	700
Terrace at Hidden Hills	Los Angeles	Los Angeles	30
Georgia			
Ball Ground	Cherokee	Atlanta	500
Crossing	Coweta	Atlanta	230
Fincher Road	Cherokee	Atlanta	3,890
Garland Mountain	Cherokee/Bartow	Atlanta	350
Martin's Bridge	Banks	Atlanta	970
Mill Creek	Coweta	Atlanta	770
Wolf Creek	Carroll/Douglas	Atlanta	12,230
Yellow Creek	Cherokee	Atlanta	1,060
Texas			
Lake Houston	Harris/Liberty	Houston	3,700
Total			24,430

^(a) A project is deemed to be in the entitlement process when customary steps necessary for the preparation of an application for governmental land-use approvals, like conducting pre-application meetings or similar discussions with governmental officials, have commenced, or an application has been filed. Projects listed may have significant steps remaining, and there is no assurance that entitlements ultimately will be received.

^(b) Project acres, which are the total for the project regardless of our ownership interest, are approximate. The actual number of acres entitled may vary.

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A summary of activity within our active projects in the development process, which includes entitled ^(a), developed and under development real estate projects, at third quarter-end 2014 follows:

Project	County	Interest Owned (b)	Residential Lots ^(c)		Commercial Acres ^(d)		
			Lots Sold Since Inception	Lots Remaining	Acres Sold Since Inception	Acres Remaining ^(e)	
Projects we own							
California							
San Joaquin River	Contra Costa/Sacramento	100	% —	—	—	288	
Colorado							
Buffalo Highlands	Weld	100	% —	164	—	—	
Johnstown Farms	Weld	100	% 269	343	2	7	
Pinery West	Douglas	100	% 45	41	20	94	
Stonebraker	Weld	100	% —	603	—	—	
Tennessee							
Morgan Farms	Williamson	100	% 45	128	—	—	
Weatherford Estates	Williamson	100	% —	17	—	—	
Texas							
Arrowhead Ranch	Hays	100	% —	387	—	6	
Bar C Ranch	Tarrant	100	% 292	813	—	—	
Barrington Kingwood	Harris	100	% 132	48	—	—	
Cibolo Canyons	Bexar	100	% 867	851	130	20	
Harbor Lakes	Hood	100	% 217	232	2	19	
Hunter's Crossing	Bastrop	100	% 483	27	41	62	
La Conterra	Williamson	100	% 200	130	—	58	
Lakes of Prosper	Collin	100	% 74	211	—	4	
Lantana	Denton	100	% 1,065	697	9	3	
Maxwell Creek	Collin	100	% 912	87	10	—	
Oak Creek Estates	Comal	100	% 214	356	13	—	
Parkside	Collin	100	% —	200	—	—	
Stoney Creek	Dallas	100	% 221	533	—	—	
Summer Creek Ranch	Tarrant	100	% 963	311	35	44	
Summer Lakes	Fort Bend	100	% 614	516	56	—	
Summer Park	Fort Bend	100	% 69	129	28	62	
The Colony	Bastrop	100	% 449	704	22	31	
The Preserve at Pecan Creek	Denton	100	% 519	275	—	7	
Village Park	Collin	100	% 753	3	3	2	
Westside at Buttercup Creek	Williamson	100	% 1,496	1	66	—	
Other projects (9)	Various	100	% 1,759	245	133	7	
Georgia							
Seven Hills	Paulding	100	% 753	337	26	113	
The Villages at Burt Creek	Dawson	100	% —	1,715	—	57	
Other projects (18)	Various	100	% 268	2,825	—	705	
Other							
Other projects (3)	Various	100	% 526	426	—	—	
				13,205	13,355	596	1,589

Projects in entities we
consolidate

Texas

City Park	Harris	75	% 1,311	458	50	115
Timber Creek	Collin	88	% —	601	—	—
Willow Creek Farms II	Waller/Fort Bend	90	% 90	160	—	—
Other projects (2)	Various	Various	10	198	—	18

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Project	County	Interest Owned ^(b)	Residential Lots ^(c)		Commercial Acres ^(d)	
			Lots Sold Since Inception	Lots Remaining	Acres Sold Since Inception	Acres Remaining ^(e)
Georgia						
The Georgian	Paulding	75	% 535	—	—	—
			1,946	1,417	50	133
Total owned and consolidated			15,151	14,772	646	1,722

Projects in ventures that we account for using the equity method

Texas						
Entrada	Travis	50	% —	821	—	—
Fannin Farms West	Tarrant	50	% 324	24	—	12
Harper's Preserve	Montgomery	50	% 315	1,378	8	51
Lantana - Rayzor Ranch	Denton	25	% 1,163	—	16	42
Long Meadow Farms	Fort Bend	38	% 1,332	470	187	116
Southern Trails	Brazoria	80	% 748	243	—	—
Stonewall Estates	Bexar	50	% 342	48	—	—
Other projects (2)	Various	Various	—	—	—	15
Total in ventures			4,224	2,984	211	236
Combined total			19,375	17,756	857	1,958

(a) A project is deemed entitled when all major discretionary governmental land-use approvals have been received. Some projects may require additional permits and/or non-governmental authorizations for development.

(b) Interest owned reflects our net equity interest in the project, whether owned directly or indirectly. There are some projects that have multiple ownership structures within them. Accordingly, portions of these projects may appear as owned, consolidated or accounted for using the equity method.

(c) Lots are for the total project, regardless of our ownership interest. Lots remaining represent vacant developed lots, lots under development and future planned lots and are subject to change based on business plan revisions.

(d) Commercial acres are for the total project, regardless of our ownership interest, and are net developable acres, which may be fewer than the gross acres available in the project.

(e) Excludes acres associated with commercial and income producing properties.

A summary of our significant commercial and income producing properties at third quarter-end 2014 follows:

Project	Market	Interest Owned ^(a)	Type	Acres	Description
Radisson Hotel	Austin	100	% Hotel	2	413 guest rooms and suites
Eleven ^(b)	Austin	100	% Multifamily	3	257-unit luxury apartment
360 ^o ^(c)	Denver	20	% Multifamily	4	304-unit luxury apartment
Midtown Cedar Hill ^(c)	Dallas	100	% Multifamily	13	354-unit luxury apartment
Acklen ^(c)	Nashville	30	% Multifamily	4	320-unit luxury apartment

(a) Interest owned reflects our total interest in the project, whether owned directly or indirectly.

(b) Construction complete.

(c) Construction in progress.

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Oil and Gas Owned Mineral Interests

A summary of our oil and gas owned mineral interests ^(a) at third quarter-end 2014 follows:

State	Unleased	Leased ^(b) (Net acres)	Held By Production ^(c)	Total ^(d)
Texas	208,000	17,000	27,000	252,000
Louisiana	132,000	3,000	9,000	144,000
Georgia	152,000	—	—	152,000
Alabama	40,000	—	—	40,000
California	1,000	—	—	1,000
Indiana	1,000	—	—	1,000
	534,000	20,000	36,000	590,000

^(a) Includes ventures.

Includes leases in primary lease term or for which a delay rental payment has been received. In the ordinary course

^(b) of business, leases covering a significant portion of leased net mineral acres may expire from time to time in a single reporting period.

^(c) Acres being held by production are producing oil or gas in paying quantities.

Texas, Louisiana, California and Indiana net acres are calculated as the gross number of surface acres

^(d) multiplied by our percentage ownership of the mineral interest. Georgia and Alabama net acres are calculated as the gross number of surface acres multiplied by our estimated percentage ownership of the mineral interest based on county sampling.

A summary of our Texas and Louisiana owned mineral acres ^(a) by county or parish at third quarter-end 2014 follows:

Texas County	Net Acres	Louisiana Parish	Net Acres
Trinity	46,000	Beauregard	79,000
Angelina	42,000	Vernon	39,000
Houston	29,000	Calcasieu	17,000
Anderson	25,000	Allen	7,000
Cherokee	24,000	Rapides	1,000
Sabine	23,000	Other	1,000
Red River	14,000		144,000
Newton	13,000		
San Augustine	13,000		
Jasper	12,000		
Other	11,000		
	252,000		

^(a) Includes ventures.

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Oil and Gas Mineral Interests Leased

A summary of our net oil and gas mineral acres leased from others at third quarter-end 2014 follows:

State	Undeveloped	Held By Production ^(a)	Total
Nebraska	237,000	10,000	247,000
Kansas	19,000	8,000	27,000
Oklahoma	22,000	18,000	40,000
Alabama	8,000	—	8,000
Texas	11,000	2,000	13,000
North Dakota	4,000	4,000	8,000
Other	11,000	4,000	15,000
	312,000	46,000	358,000

^(a) Excludes approximately 8,000 net acres of overriding royalty interests.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Sensitivity

In May 2014, we retired the \$200,000,000 term loan under our senior secured credit facility. Therefore, at third quarter-end 2014, we have no significant exposure to changes in interest rates.

Foreign Currency Risk

We have no exposure to foreign currency fluctuations.

Commodity Price Risk

We have exposure to commodity price fluctuations from our oil and gas production which can materially affect our revenues and cash flows. The prices we receive for our production depend on numerous factors beyond our control. Based on our third quarter and first nine months 2014 production, a 10% decrease in our average realized oil and gas prices would have reduced our oil and gas production revenues by \$2,397,000 and \$6,475,000. To manage our exposure to commodity price risks associated with the sale of oil and gas, we may periodically enter into derivative hedging transactions for a portion of our estimated production. We do not have any commodity derivative positions outstanding at third quarter-end 2014.

Item 4. Controls and Procedures

(a) Disclosure Controls and Procedures

Our management, with the participation of the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (or the Exchange Act)) as of the end of the period covered by this report. Based on such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures are effective in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

(b) Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II—OTHER INFORMATION

Item 1. Legal Proceedings

We are involved directly or through ventures in various legal proceedings that arise from time to time in the ordinary course of doing business. We believe we have established adequate reserves for any probable losses and that the outcome of any of the proceedings should not have a material adverse effect on our financial position, long-term results of operations or cash flows. It is possible, however, that circumstances beyond our control or significant subsequent developments could result in additional charges related to these matters that could be significant to results of operations or cash flow in any single accounting period.

Item 1A. Risk Factors

There are no material changes from the risk factors disclosed in our 2013 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Issuer Purchases of Equity Securities ^(a)

Period	Total Number of Shares Purchased ^(b)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares That May Yet be Purchased Under the Plans or Programs
Month 7 (7/1/2014 — 7/31/2014)	—	\$—	—	4,997,855
Month 8 (8/1/2014 — 8/31/2014)	2,591	\$19.98	—	4,997,855
Month 9 (9/1/2014 — 9/30/2014)	—	\$—	—	4,997,855
	2,591	\$19.98	—	

On February 11, 2009, we announced that our Board of Directors authorized the repurchase of up to 7,000,000 shares of our common stock. We have purchased 2,002,145 shares under this authorization, which has no ^(a) expiration date. We have no repurchase plans or programs that expired during the period covered by the table above and no repurchase plans or programs that we intend to terminate prior to expiration or under which we no longer intend to make further purchases.

^(b) Represents shares withheld to pay taxes in connection with vesting of equity-settled stock awards and exercises of stock options.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

Exhibit	Description
10.1	Guaranty dated July 15, 2014 by Forestar (USA) Real Estate Group Inc. in favor of Regions Bank (incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K filed with the Commission on July 18, 2014).
31.1	Certification of Chief Executive Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Exchange Act rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.1	The following materials from Forestar's Quarterly Report on Form 10-Q for the quarter ended September 30, 2014, formatted in XBRL (Extensible Business Reporting Language): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income and Comprehensive Income, (iii) Consolidated Statements of Cash Flows, and (iv) Notes to Consolidated Financial Statements.

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SIGNATURES

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

FORESTAR GROUP INC.

Date: November 6, 2014

By: /s/ Christopher L. Nines
Christopher L. Nines
Chief Financial Officer

By: /s/ Sabita C. Reddy
Sabita C. Reddy
Principal Accounting Officer