

**Motion for an Order Pursuant to Section 363(b) of the Bankruptcy Code and Rule 9019 of the Federal Rules of Bankruptcy Procedure Approving Settlement Agreement Regarding LH-EH Layton Lakes Estates, L.L.C. (the “Layton Lakes Motion”).**

By the Layton Lakes Motion, the Debtors seek entry of an order authorizing TOUSA Homes, Inc. (“Homes”) to enter into (i) a compromise and settlement agreement regarding LH-EH Layton Lakes Estates, L.L.C. (the “Compromise Agreement”), (ii) an escrow agreement for off-site improvement construction costs (the “Escrow Agreement”), and (iii) an option agreement (the “New Option Agreement” and, together with the Compromise Agreement and Escrow Agreement, the “Settlement Agreement”) with Lennar Communities Development, Inc. (“Lennar”), LH-EH Lakes Estates L.L.C. (the “JV”), North American Title Company (the “Escrow Agent”), and the town of Gilbert, Arizona (the “Town”).

On January 24, 2003, Lennar’s predecessor in interest, U.S. Home Corporation (“USH”), and Homes entered into that certain Arizona Operating Agreement of LH-EH Layton Lakes Estates, L.L.C. (as amended, the “Operating Agreement”), pursuant to which USH and Homes formed the JV.<sup>1</sup> The JV was formed to develop a master planned community known as Layton Lakes located in Arizona. The JV’s only property is in the Layton Lakes Community, which was intended to be developed in multiple phases to include 1,595 single family residential lots, 346 lots for townhome construction and approximately 46 acres of property zoned for commercial use.

Pursuant to the Operating Agreement, Lennar and Homes each hold a 50% financial interest in the JV. Under option agreements with the JV, both Lennar and Homes (the “Old Option”) have options to purchase various tracts of land in Layton Lakes.

In addition, the JV and Town entered into an Off-Site Improvements Agreement, dated November 29, 2005 (the “Improvements Agreement”) whereby the JV agreed to construct certain improvements for Layton Lakes (the “Improvements”).<sup>2</sup>

The JV had been funding development of Layton Lakes from (i) capital contributions made by Lennar and Homes; (ii) loans made by Lennar to the JV; and (iii) the proceeds of a secured acquisition and development loan (the “Loan”) from Bank Midwest, N.A. (the “Lender”) in the original principal amount of \$90 million.

Lennar’s affiliate, Lennar Corporation (“Lennar Corp.”) and Homes’ parent, TOUSA, Inc. (“TOUSA”) each executed a Completion and Limited Indemnity Agreement, dated October 16, 2006 and an Environmental Indemnity, dated October 16, 2006, in favor of the Lender in connection with the Loan (together, the “Guaranties”). Under the Guaranties, Lennar Corp. and TOUSA agreed to, among other things, (i) guarantee performance of the JV’s development obligations under the Loan and assume payment responsibility for all costs related thereto and

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<sup>1</sup> Lennar acquired USH’s right, title and interest in the JV and was admitted as a member of the JV in 2005.

<sup>2</sup> In connection with entry into the Improvements Agreement, Bond Safeguard Insurance Company (“Safeguard”) issued a surety bond to the Town (the “Bond”), which provided financial assurance that the Improvements would be timely constructed.

(ii) indemnify the Lender with respect to damages arising out of, among other things, (a) misapplication or misappropriation of funds by the JV, (b) fraud, material misrepresentation or failure to disclose a material fact by the JV, (c) waste as a result of intentional misconduct or gross negligence, and (iii) the filing of a bankruptcy petition by the JV or any affiliate, officer, director, or representative which controls the JV.<sup>3</sup>

Lennar Corp. and TOUSA also entered into a Reimbursement and Indemnity Agreement (the “Indemnity Agreement”) whereby Lennar Corp. and TOUSA exchanged reciprocal contribution rights in the event either party pays any amounts under the Guaranties.<sup>4</sup>

Since the petition date, Homes has not made any additional capital contributions to the JV. In addition, the Lender exercised re-margin and call rights under the Loan requiring the JV to repay approximately \$14.5 million of principal and accrued interest outstanding under the Loan (the “Repayment”). The JV, however, did not have the liquidity to make the Repayment and, thus, is in default under the Loan and the Lender has refused to advance additional funds under the Loan. Accordingly, the JV has ceased constructing the Improvements, which has resulted in the Town refusing to issue certificates of occupancy (“COs”) for residences completed by Lennar and Homes within Layton Lakes.<sup>5</sup>

In addition to the inability to obtain COs, there is an ongoing dispute between Homes and Lennar concerning, among other things, the parties’ respective funding obligations under the Operating Agreement, whereby Lennar asserts that Homes’ failure to make certain required capital contributions has resulted in a default under the Operating Agreement.

In light of the JV’s financial situation, Homes’ inability to obtain COs from the Town, and the existing dispute with Lennar regarding the Operating Agreement, the Debtors assert that it was prudent to negotiate with Lennar and the Town to reach a global settlement resolving all disputes concerning the JV. After lengthy negotiations among the parties, the Settlement Agreement was reached containing the following salient terms:

- (i) Homes will deposit \$1.3 million (the “Deposit”) into an escrow account to secure completion of the Improvements;
- (ii) Lennar will assume responsibility for (i) commencing and completing the Improvements and (ii) any and all costs associated with the Improvements and other fees and charges if such costs exceed the Deposit. Any failure of

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<sup>3</sup> On May 15, 2008, the Lender filed a proof of claim against TOUSA asserting a secured claim in the total amount of \$61,480,130 with respect to the Loan (the “Lender Claim”). The Debtors intend to object to the Lender Claim.

<sup>4</sup> Both Lennar and Lennar Corp. have filed proofs of claims against the Debtors (together, the “Lennar Claims”) asserting contingent and unliquidated claims for amounts due under the Operating Agreement, the Guaranties and the Indemnity Agreement.

<sup>5</sup> In addition, the Town issued a demand to Safeguard that the Improvements be completed. Safeguard, however, refused such demand. As a result, on October 24, 2008, the Town filed a lawsuit against Safeguard and the JV, among others, alleging breach of contract and performance under the Bond and seeking recovery of the costs of completing the Improvements.

Lennar to complete the Improvements will result in the Deposit being disbursed to the Town;

- (iii) Upon the placement of the Deposit in escrow, the Town will process and issue COs (even during construction of the Improvements);
- (iv) Lennar and Homes will enter into the New Option Agreement, pursuant to which Homes will have the right to acquire 207 residential lots within Layton Lakes;<sup>6</sup>
- (v) Homes will withdraw as a member of the JV and relinquish all of its rights and interests under the Operating Agreement, which will be rejected and terminated;
- (vi) Following Homes' withdrawal as a member of the JV, Lennar will dissolve the JV, including making adequate provision for the performance and satisfaction of the debts and obligations of the JV. Further, Lennar will assume all responsibility with respect to Improvements, which were guaranteed by TOUSA pursuant to the Indemnity Agreement; and
- (vii) Lennar and Homes will mutually release each other from any and all claims arising under or relating to the Old Option and the Operating Agreement including, without limitation, any rejection damage or administrative claims associated with such agreements.

The Debtors assert that the Settlement Agreement is in the best interests of their estates because (i) immediately following escrowing of the Deposit, the Town will issue COs that will permit Homes to close sales on 39 homes, which the Debtors believe should all close in the first quarter of 2009 and generate approximately \$12.2 million in net revenue; (ii) the Deposit, as well as an agreement from Lennar to contribute any additional amounts to complete the Improvements, will enhance the value of Layton Lakes to the Debtors' direct benefit; (iii) the Settlement Agreement resolves all claims and outstanding disputes arising under or relating to the Old Option and the Operating Agreement, including the release of any and all rejection damage and administrative claims that may be asserted by Lennar against the Debtors, including the Lennar Claims, which will be disallowed and expunged; (iv) Lennar will make adequate provision for the performance and satisfaction of the amounts due and owing to the Lender (and thereby mitigate any damages asserted in the Lender Claim); and (v) entry into the New Option Agreement will afford Homes

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<sup>6</sup> On the Effective Date of the New Option Agreement, TOUSA Homes shall be deemed to have exercised the option to purchase 7 lots within Layton Lakes for approximately \$425,000, which amount will be deposited with the Escrow Agent and distributed to Lennar once all conveyance documents have been provided. To maintain its option with respect to the 200 lots after May 31, 2009, Homes is required to pay Lennar an option consideration fee in the amount of \$1 million (the "Option Fee"). Failure to pay the Option Fee will result in the automatic termination of the New Option Agreement. Beginning on June 30, 2009, and in order to maintain its option going forward after payment of the Option Fee, TOUSA Homes will be required to purchase a minimum of 2 lots per month per lot type on a cumulative basis (*i.e.*, six lots every month). The purchase price of the lots increases over time. The New Option Agreement expires on October 31, 2011.

the opportunity to strengthen its presence in Layton Lakes, considered one of the best and most valuable assets in Homes' Phoenix Division, by permitting Homes to immediately purchase seven lots at a competitive price, while providing Homes with important flexibility to continue monitoring the status of Layton Lakes through a difficult economic climate before committing to acquire 200 lots subject to the New Option Agreement.

***A telephonic hearing on the Layton Lakes Motion has been scheduled for November 25, 2008, with an objection deadline of November 24, 2008 at 12:00 p.m. (ET).***