
**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 June 30, 2007

OR

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

Commission File Number 1-3924

MAXXAM INC.

(Exact name of Registrant as Specified in its Charter)

Delaware

(State or other jurisdiction
of incorporation or organization)

1330 Post Oak Blvd., Suite 2000

Houston, Texas

(Address of Principal Executive Offices)

95-2078752

(I.R.S. Employer
Identification Number)

77056

(Zip Code)

Registrant's telephone number, including area code: **(713) 975-7600**

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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. (Check one):

Large accelerated filer ☐

Accelerated filer ☒

Non-accelerated filer ☐

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ☐ No ☒

Number of shares of common stock outstanding at August 3, 2007: 5,251,117

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MAXXAM INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In millions of dollars, except share information)

	June 30, 2007	December 31, 2006
	(Unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 34.7	\$ 34.8
Marketable securities and other short-term investments	117.5	126.2
Receivables:		
Trade, net of allowance for doubtful accounts of \$0.8 and \$0.7, respectively	1.9	9.9
Other	2.0	9.7
Inventories:		
Lumber	—	16.3
Logs	—	25.5
Real estate inventory	5.0	5.8
Prepaid expenses and other current assets	4.1	16.2
Restricted cash and marketable securities	2.4	43.1
Total current assets	167.6	287.5
Property, plant and equipment, net of accumulated depreciation of \$92.5 and \$234.5, respectively	223.5	337.0
Timber and timberlands, net of accumulated depletion of \$232.2 at December 31, 2006	—	200.3
Real estate	48.9	46.0
Deferred income taxes	97.6	97.5
Intangible assets	—	2.0
Deferred financing costs	5.2	22.6
Long-term receivables and other assets	7.3	8.8
Restricted cash and marketable securities	3.5	8.2
	<u>\$ 553.6</u>	<u>\$ 1,009.9</u>
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$ 5.5	\$ 10.0
Accrued interest	0.9	28.8
Accrued compensation and related benefits	3.1	13.8
Accrued development costs	1.7	1.8
Accrued other taxes	2.3	2.6
Deferred revenue	2.5	1.8
Other accrued liabilities	14.8	20.1
Short-term borrowings and current maturities of long-term debt	4.9	180.7
Total current liabilities	35.7	259.6
Long-term debt, less current maturities	213.0	885.4
Accrued pension and other postretirement benefits	7.9	20.8
Other noncurrent liabilities	44.2	55.9
Losses in excess of investment in Debtors	483.6	—
Commitments and contingencies (see Note 8)		
Stockholders' deficit:		
Preferred stock, \$0.50 par value; \$0.75 liquidation preference; 2,500,000 shares authorized; Class A \$0.05 Non-Cumulative Participating Convertible Preferred Stock; 668,964 shares issued and 668,119 shares outstanding	0.3	0.3
Common stock, \$0.50 par value; 13,000,000 shares authorized; 10,063,359 shares issued; 5,251,117 and 5,257,657 shares outstanding	5.0	5.0
Additional capital	225.3	225.3
Accumulated deficit	(315.0)	(296.0)
Accumulated other comprehensive income	1.2	1.0
Treasury stock, at cost (shares held: preferred – 845; common – 4,812,242 and 4,805,702, respectively)	(147.6)	(147.4)
Total stockholders' deficit	(230.8)	(211.8)
	<u>\$ 553.6</u>	<u>\$ 1,009.9</u>

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

MAXXAM INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In millions of dollars, except per share information)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(Unaudited)			
Sales:				
Forest products, net of discounts	\$ —	\$ 33.8	\$ 4.4	\$ 71.6
Real estate	12.8	19.2	24.4	48.2
Racing	10.5	10.5	23.2	23.9
	<u>23.3</u>	<u>63.5</u>	<u>52.0</u>	<u>143.7</u>
Costs and expenses:				
Cost of sales and operations:				
Forest products	—	28.6	4.3	62.2
Real estate	5.7	8.1	11.0	16.4
Racing	9.6	9.5	20.4	20.7
Selling, general and administrative expenses	8.8	11.9	18.8	24.6
Gain on sales of timberlands and other assets	—	(5.2)	(0.1)	(5.9)
Depreciation, depletion and amortization	3.5	8.6	8.0	17.4
	<u>27.6</u>	<u>61.5</u>	<u>62.4</u>	<u>135.4</u>
Operating income (loss):				
Forest products	(0.5)	0.1	(3.5)	(5.4)
Real estate	—	3.5	(0.6)	16.4
Racing	(1.8)	(1.6)	(2.4)	(1.7)
Corporate	(2.0)	—	(3.9)	(1.0)
	<u>(4.3)</u>	<u>2.0</u>	<u>(10.4)</u>	<u>8.3</u>
Other income (expense):				
Investment, interest and other income	1.8	2.3	3.0	6.7
Interest expense	(4.0)	(19.1)	(11.1)	(38.7)
Amortization of deferred financing costs	(0.2)	(0.6)	(0.5)	(1.2)
Loss before income taxes and cumulative effect of accounting change	(6.7)	(15.4)	(19.0)	(24.9)
Benefit for income taxes	—	4.2	—	4.2
Loss before cumulative effect of accounting change	(6.7)	(11.2)	(19.0)	(20.7)
Cumulative effect of accounting change, net of tax	—	—	—	(0.7)
Net loss	<u>\$ (6.7)</u>	<u>\$ (11.2)</u>	<u>\$ (19.0)</u>	<u>\$ (21.4)</u>
Basic and diluted loss per common and common equivalent share before cumulative effect of accounting change	<u>\$ (1.28)</u>	<u>\$ (1.97)</u>	<u>\$ (3.62)</u>	<u>\$ (3.56)</u>
Cumulative effect of accounting change	—	—	—	(0.12)
Basic and diluted loss per common and common equivalent share after cumulative effect of accounting change	<u>\$ (1.28)</u>	<u>\$ (1.97)</u>	<u>\$ (3.62)</u>	<u>\$ (3.68)</u>

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

MAXXAM INC. AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions of dollars)

	Six Months Ended June 30,	
	2007	2006
	(Unaudited)	
Cash flows from operating activities:		
Net loss	\$ (19.0)	\$ (21.4)
Adjustments to reconcile net loss to net cash used for operating activities:		
Depreciation, depletion and amortization	8.0	17.4
Non-cash stock-based compensation benefit	(0.4)	(3.4)
Gains on sales of timberlands and other assets	(0.1)	(5.9)
Net gains (losses) from marketable securities	(0.6)	0.1
Amortization of deferred financing costs and discounts on long-term debt	0.5	1.2
Equity (income) loss of unconsolidated affiliates, net of dividends received	(0.4)	0.3
Increase (decrease) in cash resulting from changes in:		
Receivables	8.5	(1.3)
Inventories	0.8	9.2
Prepaid expenses and other assets	0.8	(0.3)
Accounts payable	0.4	3.6
Accrued and deferred income taxes	(0.1)	(4.2)
Other accrued liabilities	(2.1)	(6.4)
Accrued interest	2.7	0.1
Long-term assets and long-term liabilities	(4.4)	0.7
Other	(0.3)	(0.6)
Net cash used for operating activities	<u>(5.7)</u>	<u>(10.9)</u>
Cash flows from investing activities:		
Net proceeds from the disposition of property and investments	0.1	8.1
Maturities of marketable securities and other investments	105.6	228.7
Sales of marketable securities and other investments	53.2	51.8
Purchases of marketable securities and other investments	(150.8)	(278.2)
Net proceeds from restricted cash	0.7	9.5
Capital expenditures	(1.9)	(4.2)
Decrease in cash attributable to the deconsolidation of Debtors	(1.1)	-
Contribution to joint venture	(0.6)	-
Net cash provided by investing activities	<u>5.2</u>	<u>15.7</u>
Cash flows from financing activities:		
Proceeds from issuance of long-term debt	-	0.2
Redemptions and repurchases of, and principal payments on, long-term debt	(2.3)	(21.8)
Principal payments on Scopac Timber Notes held in the SAR Account	-	6.5
Borrowings under revolving and short-term credit facilities, net	2.2	(3.8)
Incurrence of deferred financing costs	-	(1.3)
Treasury stock purchases	(0.2)	(22.4)
Net proceeds from refundable deposits	0.7	0.9
Net cash provided by (used for) financing activities	<u>0.4</u>	<u>(41.7)</u>
Net decrease in cash and cash equivalents	<u>(0.1)</u>	<u>(36.9)</u>
Cash and cash equivalents at beginning of the period	<u>34.8</u>	<u>72.9</u>
Cash and cash equivalents at end of the period	<u><u>\$ 34.7</u></u>	<u><u>\$ 36.0</u></u>
Supplemental disclosure of cash flow information:		
Interest paid	\$ 8.4	\$ 38.6

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

MAXXAM INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The information contained in the following notes to the consolidated financial statements is condensed from that which would appear in the annual consolidated financial statements; accordingly, the condensed consolidated financial statements included herein should be read in conjunction with the consolidated financial statements and related notes thereto contained in the Form 10-K. Any capitalized terms used but not defined in these Condensed Notes to Consolidated Financial Statements are defined in the "Glossary of Defined Terms" contained in Appendix A. All references to the "Company" include MAXXAM Inc. and its consolidated majority and wholly owned subsidiaries, unless otherwise noted or the context indicates otherwise. All references to specific entities refer to the respective companies and their subsidiaries, unless otherwise specified or the context indicates otherwise. Accounting measurements at interim dates inherently involve greater reliance on estimates than at year end. The results of operations for the interim periods presented are not necessarily indicative of the results to be expected for the entire year.

The consolidated financial statements included herein are unaudited; however, they include all adjustments of a normal recurring nature which, in the opinion of management, are necessary for a fair presentation of the consolidated financial position of the Company at June 30, 2007, the consolidated results of operations for the three months and six months ended June 30, 2007 and 2006, and the consolidated cash flows for the six months ended June 30, 2007 and 2006.

Deconsolidation of Palco and its Subsidiaries

Under GAAP, consolidation is generally required for investments of more than 50% of the outstanding voting stock of an investee, except when control is not held by the majority owner. Under these principles, legal reorganization or bankruptcy represent conditions which can preclude consolidation in instances where control rests with the bankruptcy court, rather than the majority owner. As discussed below, on January 18, 2007, the Debtors - Palco and its subsidiaries - filed for reorganization under Chapter 11 of the Bankruptcy Code. See the "Reorganization Proceedings of Palco and its Subsidiaries" section below for further information regarding the Debtors' reorganization proceedings. As a result, the Company deconsolidated the Debtors' financial results beginning January 19, 2007, and began reporting its investment in the Debtors using the cost method. These consolidated financial statements do not reflect any adjustment related to the deconsolidation of the Debtors other than presenting the Company's investment in the Debtors using the cost method.

Through January 18, 2007, under generally accepted principles of consolidation, the Company had recognized losses in excess of its investment in the Debtors of \$483.6 million. Since the Debtors' results are no longer consolidated, any adjustments reflected in the Debtors' financial statements subsequent to January 19, 2007 (relating to the recoverability and classification of recorded asset amounts and classification of liabilities or the effects on existing stockholders' deficit as well as adjustments made to the Debtors' financial information for loss contingencies and other matters), are not expected to impact the Company's consolidated financial results.

The Company will reevaluate the accounting treatment of its investment in the Debtors when either: (i) the Debtors' bankruptcies are resolved, or (ii) there is a change in the equity ownership of the Debtors.

The following proforma financial data reflects the results of operations of the Company, excluding the Debtors, for the periods presented (in millions, except share data).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Sales	\$ 23.3	\$ 29.7	\$ 47.6	\$ 72.1
Costs and expenses	(27.6)	(28.0)	(55.7)	(59.0)
Operating income (loss)	(4.3)	1.7	(8.1)	13.1
Other income, net	1.8	1.8	2.9	6.0
Interest expense, including amortization of deferred financing costs	(4.2)	(4.3)	(8.5)	(8.7)
Income (loss) before income taxes and cumulative effect of accounting change	(6.7)	(0.8)	(13.7)	10.4
Benefit for income taxes	—	(0.5)	—	(0.5)
Income (loss) before cumulative effect of accounting change	(6.7)	(1.3)	(13.7)	9.9
Cumulative effect of accounting change, net of tax	—	—	—	(0.7)
Net income (loss)	<u>\$ (6.7)</u>	<u>\$ (1.3)</u>	<u>\$ (13.7)</u>	<u>\$ 9.2</u>
Net income (loss) per share:				
Basic	\$ (1.28)	\$ (0.23)	\$ (2.61)	\$ 1.58
Diluted	\$ (1.28)	\$ (0.23)	\$ (2.61)	\$ 1.35

Reorganization Proceedings of Palco and its Subsidiaries

On January 18, 2007, Palco and its five wholly owned subsidiaries, including Scopac, filed separate voluntary petitions in the United States Bankruptcy Court for the Southern District of Texas for reorganization under Chapter 11 of the Bankruptcy Code. The six companies that filed for voluntary protection are Scopac and the Palco Debtors: Palco, Britt, SDLLC, Salmon Creek and Scotia Inn. The Bankruptcy Cases are being jointly administered, with the Debtors managing their business in the ordinary course as debtors-in-possession subject to the control and supervision of the Bankruptcy Court.

The filing of the Bankruptcy Cases was precipitated by liquidity shortfalls at Palco and Scopac and their resultant inability to make January 2007 interest payments on their respective debt obligations, arising from regulatory restrictions and limitations on timber harvest, increased timber harvesting costs and cyclical lumber prices. Both Scopac and Palco undertook various efforts in 2006 to generate additional liquidity to satisfy their respective debt service obligations; however, the cash generated from their efforts, together with their cash flows from operations, was not sufficient to cover their respective interest payment shortfalls in January 2007.

Scopac's indebtedness consists of its 6.55% Class A-1, 7.11% Class A-2 and 7.71% Class A-3 Timber Collateralized Notes due 2028 (\$713.8 million principal outstanding as of December 31, 2006) and a line of credit with a group of banks (\$36.2 million principal outstanding as of December 31, 2006), each of which is secured by (i) Scopac's timber, timberlands and timber rights, (ii) certain contract rights and other assets, (iii) the proceeds of the foregoing, and (iv) the funds held by the Trustee in various accounts related to the Scopac Timber Notes.

Palco's indebtedness consists of a five-year \$85.0 million secured term loan (\$84.3 million principal outstanding as of December 31, 2006) and a five-year \$60.0 million secured asset-based revolving credit facility (\$24.1 million of borrowings outstanding and \$13.7 million of letters of credit issued as of December 31, 2006). These facilities are secured by the stock of Palco and substantially all of the assets of the Palco Debtors (other than Palco's equity interest in Scopac).

The outstanding principal of, and accrued interest on, all secured indebtedness of the Debtors became immediately due and payable as a result of the commencement of the Bankruptcy Cases. However, the vast majority of the claims in existence at the Filing Date (including claims for principal and accrued interest and substantially all legal proceedings) are stayed (deferred) while the Debtors continue to operate the businesses. The Bankruptcy Court has, however, upon a motion of the Debtors, permitted the Debtors to pay or otherwise honor certain unsecured pre-Filing Date claims, including employee wages and benefits and certain customer claims in the ordinary course of business, subject to certain limitations.

The Debtors' overall objectives in the Bankruptcy Cases are to achieve an operational and financial restructuring of each of the Debtors' long-term debt obligations in view of estimated lower harvest levels, increased regulatory compliance costs and cyclical lumber prices, and also to continue their businesses. There can be no assurance that the Debtors will be able to attain these objectives and achieve a successful operational and financial reorganization. In the event the Debtors are unsuccessful in attaining a successful operational and financial reorganization, the Debtors could be forced to surrender all or substantially all of their assets to their creditors. The outcome of the Bankruptcy Cases is impossible to predict and could have a material adverse effect on the businesses of the Debtors, on the interests of creditors, and on the Company.

As provided by the Bankruptcy Code, each of the Debtors generally has the exclusive right to propose a plan of reorganization during the Exclusivity Period, which has been extended to September 18, 2007. The Debtors' objective is to file such plan(s) during the extended Exclusivity Period, but may request additional extensions, depending on the status of negotiations with parties in interest and other relevant factors. The Debtors are pursuing discussions in order to accomplish restructuring plan(s) on a consensual basis, but there can be no assurance that a consensual plan(s) of reorganization will be agreed upon. Once reorganization plan(s) are filed, the Debtors are required to seek approval of the plan(s) by the creditors and equity holders entitled to vote on the plan(s), and to seek confirmation of the plan(s) by the Bankruptcy Court. The Debtors' efforts to obtain creditor approvals and Bankruptcy Court confirmation may not be successful. If the Debtors fail to file plans of reorganization during the Exclusivity Period or any extension thereof, or if such plans are not accepted by the requisite creditors and equity holders entitled to vote on the plans, or if the Debtors do not obtain Bankruptcy Court confirmation, other parties in interest in the Bankruptcy Cases may be permitted to propose their own plans of reorganization for the Debtors.

The Debtors anticipate that substantially all of their liabilities as of the Filing Date will be resolved under plan(s) of reorganization proposed, voted on and confirmed in accordance with the Bankruptcy Code. However, there can be no assurance that the liabilities of one or more of the Debtors will not exceed the fair value of its or their assets. If a debtor's creditors are not paid in full, the Bankruptcy Code provides that the debtor's equity holders are not entitled to retain their equity interests, unless certain exceptions apply. If the liabilities of one or more of the Debtors are ultimately found to exceed the fair value of its or their assets, claims of creditors could be paid at less than 100% of their face value. In that event, Palco could lose all or a material portion of its equity ownership in Scopac and Palco's other subsidiaries, MGI could lose all or a material portion of its equity ownership in Palco, or the value of such equity interests could be diluted, impaired or eliminated.

Palco Debtors' Liquidity

The Palco Debtors estimate that they will have significant liquidity shortfalls in 2007. On August 6, 2007, the Palco Debtors closed on the DIP Facility, a \$75.0 million Debtor-in-Possession revolving credit facility that matures on the earliest of, among other things, (i) the sale of substantially all of the assets of the Palco Debtors; (ii) an event of default; (iii) the effective date of a plan of reorganization; or (iv) August 6, 2008. The DIP Facility was used to pay off the Palco Revolving Credit Facility. The DIP Facility provides the lender with a "super-priority" claim, which provides for payment of the DIP Facility before any other secured or unsecured creditors and equity holders of the Palco Debtors are paid. The DIP Facility contains restrictive financial covenants that, among others, require the Palco Debtors to maintain a minimum level of EBITDA and meet weekly cash flow projections. Continued compliance with the DIP Facility is dependent on the ability of the Palco Debtors to meet the financial covenants. However, operating cash flow estimates used to establish the EBITDA maintenance covenants and the weekly cash flow projections are subject to a number of assumptions and actual results could differ materially from these estimates. There can be no assurance that the Palco Debtors will meet the restrictive financial covenants specified in the DIP Facility, in which case they may not be able to continue operations and reorganize under Chapter 11 of the Bankruptcy Code.

Scopac Liquidity

Scopac has been authorized by the Bankruptcy Court to fund budgeted ongoing operating and bankruptcy-related costs using operating cash flow and, to the extent needed, funds available in the SAR Account (subject to no more than \$5.0 million in withdrawals from the SAR Account being outstanding at any given time). If these sources of liquidity are not adequate, and if Scopac is unable to obtain additional sources of liquidity and the necessary Bankruptcy Court approval to utilize such additional sources of liquidity, Scopac may not be able to continue operations and reorganize successfully under Chapter 11 of the Bankruptcy Code.

The financial information of the Debtors contained herein and consolidated with the Company's results at December 31, 2006, was prepared on a "going concern" basis, which contemplates the realization of assets and the liquidation of liabilities in the ordinary course of business; however, as a result of the commencement of the Bankruptcy Cases, such realization of assets and liquidation of liabilities are subject to significant uncertainties. For example, the financial information of the Debtors for the year ended December 31, 2006, contained herein does not present: (a) the

realizable value of assets on a liquidation basis, (b) the estimated costs and expenses associated with the Bankruptcy Cases, (c) the amount that will ultimately be paid to settle liabilities and contingencies which may be allowed in the Bankruptcy Cases, or (d) the effect of any changes that may be made in connection with the Company's investment in the Debtors or with the Debtors' operations resulting from a plan of reorganization. Because of the ongoing nature of and uncertainties related to the Bankruptcy Cases, the discussions and financial information of the Debtors contained herein are subject to material uncertainties.

The following tables contain summarized GAAP-based consolidated financial information of the Debtors (in millions) for the periods presented.

	June 30, 2007	December 31, 2006
Current assets	\$ 94.8	\$ 105.5
Property, plant and equipment, net	103.8	108.3
Timber and timberlands, net	199.8	200.4
Other assets	38.4	40.4
Total assets	<u>\$ 436.8</u>	<u>\$ 454.6</u>
Secured debt obligations, including accrued interest	\$ 910.1	\$ 873.7
Other liabilities, including parent company loans	117.1	110.5
Stockholders' deficit	(590.4)	(529.6)
Total liabilities and stockholders' deficit	<u>\$ 436.8</u>	<u>\$ 454.6</u>

	Three Months Ended June 30, 2007	2006	Six Months Ended June 30, 2007⁽¹⁾	2006
Sales, net of discounts	\$ 32.7	\$ 33.8	\$ 64.7	\$ 71.6
Costs and expenses ⁽²⁾	(46.1)	(33.5)	(90.0)	(76.4)
Operating income (loss)	(13.4)	0.3	(25.3)	(4.8)
Other income, net	0.5	0.5	2.1	0.7
Interest expense	(15.1)	(15.4)	(37.6)	(31.2)
Loss before income taxes	(28.0)	(14.6)	(60.8)	(35.3)
Benefit for income taxes	—	4.7	—	4.7
Net loss	<u>\$ (28.0)</u>	<u>\$ (9.9)</u>	<u>\$ (60.8)</u>	<u>\$ (30.6)</u>

⁽¹⁾ The operating results of the Debtors from January 1, 2007 to January 18, 2007 are included in the Company's consolidated financial statements. See Note 3.

⁽²⁾ Costs and expenses include bankruptcy-related legal and advisor fees of \$8.1 million for the three months ended June 30, 2007 and \$13.8 million for the six months ended June 30, 2007.

Potential Impact on Registrant and Certain Related Entities

The Bankruptcy Cases could result in claims against and could have adverse impacts on MAXXAM Parent and its affiliates, including MGHI and/or MGI. For example, under ERISA, if Palco's pension plan were to be terminated, MAXXAM Parent and its wholly owned subsidiaries would be jointly and severally liable for any unfunded pension plan obligations. The unfunded termination obligation attributable to Palco's pension plan as of December 31, 2006, is estimated not to exceed \$23.0 million based upon annuity placement interest rate assumptions as of such date. In addition, it is possible that certain transactions could be completed in connection with a potential restructuring or reorganization of the Debtors, such as a sale of all or a portion of the equity ownership in the Debtors, a sale of a substantial portion of the Debtors' assets and/or a cancellation of some or all of the Debtors' indebtedness, which could require the utilization of all or a substantial portion of, or the loss of a significant portion of, the Company's net operating losses or other tax attributes for federal and state income tax purposes, and could require tax payments.

Use of Estimates and Assumptions

The preparation of financial statements in accordance with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions that affect (i) the reported amounts of assets and liabilities, (ii) the disclosure of contingent assets and liabilities known to exist as of the date the financial statements are published, and (iii) the reported amount of revenues and expenses recognized during each period presented. The Company reviews all significant estimates affecting its consolidated financial statements on a recurring basis and records the effect of any necessary adjustments prior to filing such statements with the SEC. Adjustments made to estimates often relate to improved information not previously available. Uncertainties are inherent in such estimates and related assumptions; accordingly, actual results could differ materially from these estimates.

Risks and uncertainties are inherent with respect to the ultimate outcome of the Bankruptcy Cases and the matters discussed in Note 8. The results of a resolution of such uncertainties could have a material effect on the Company's consolidated financial position, results of operations or liquidity. In addition, uncertainties related to the projection of future taxable income could affect the realization of the Company's deferred tax assets discussed in Note 6. Estimates of future benefit payments used to measure the Company's pension and other postretirement benefit obligations are subject to a number of assumptions about future experience, as are the estimated future cash flows projected in the evaluation of long-lived assets for possible impairment. To the extent there are material differences between these estimates and actual results, the Company's consolidated financial position, results of operations and/or liquidity could be materially affected.

Reclassifications

Certain reclassifications have been made to the consolidated financial statements of prior years to be consistent with the current year's presentation. Specifically, certain balance sheet amounts as of December 31, 2006 have been shown as a separate line item to comply with current period reporting requirements. Additionally, sales and maturities of marketable securities and other investments on the consolidated statement of cash flows have been categorized as separate line items, one for sales and one for maturities.

2. New Accounting Standards

Accounting for Uncertainty in Income Taxes

On January 1, 2007, the Company adopted the provisions of FIN 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with FASB No. 109 and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

Fair Value Measurements

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements*, which is intended to increase consistency and comparability in fair value measurements by defining fair value, establishing a framework for measuring fair value, and expanding disclosures about fair value measurements. SFAS No. 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company will adopt SFAS No. 157 on January 1, 2008, and has not yet determined the impact, if any, on its consolidated financial statements.

The Fair Value Option for Financial Assets and Financial Liabilities

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities — Including an amendment of FASB Statement No. 115*. SFAS No. 159 permits entities to measure eligible assets and liabilities at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. SFAS No. 159 is optional and, if adopted by a Company, is effective for fiscal years beginning after November 15, 2007. The Company is in the process of evaluating whether or not to adopt SFAS No. 159.

3. Segment Information and Other Items

Sales and operating income (loss) for each reportable segment are presented in the Consolidated Statements of Operations. The amounts reflected in the "MGI" column represent MGI's assets, liabilities and general and administrative expenses on a stand-alone basis (without Palco or any of Palco's subsidiaries). Operating losses for "Corporate" represent general and administrative expenses not directly attributable to the reportable segments. The amounts reflected in the "Corporate" column also serve to reconcile the total of the reportable segments' amounts to totals in the Company's consolidated financial statements.

The following table presents certain other unaudited financial information by reportable segment (in millions).

	Reportable Segments						Total Excluding Debtors	Reportable Segment	Consolidated Total	
	Real Estate		Racing		MGI		Corporate		Forest Products ⁽¹⁾	
Investment, interest and other income for the three months ended:										
June 30, 2007	\$ 1.0	\$	0.1	\$	—	\$	0.7	\$	1.8 ⁽²⁾	\$ 1.8
June 30, 2006	1.5		0.1		0.1		0.4		0.2	2.3
Investment, interest and other income for the six months ended:										
June 30, 2007	\$ 1.2	\$	0.1	\$	—	\$	1.5	\$	2.8 ⁽³⁾	\$ 3.0
June 30, 2006	2.5		0.1		0.1		3.5		0.5	6.7
Selling, general and administrative expense for the three months ended:										
June 30, 2007	\$ 4.0	\$	2.3	\$	0.5	\$	2.0	\$	8.8 ⁽²⁾	\$ 8.8
June 30, 2006	4.0		2.2		0.2		—		5.5	11.9
Selling, general and administrative expense for the six months ended:										
June 30, 2007	\$ 7.9	\$	4.4	\$	1.2	\$	3.8	\$	17.3 ⁽³⁾	\$ 18.8
June 30, 2006	8.2		4.2		0.6		0.9		10.7	24.6
Operating income (loss) for the three months ended:										
June 30, 2007	\$ —	\$	(1.8)	\$	(0.5)	\$	(2.0)	\$	(4.3) ⁽²⁾	\$ (4.3)
June 30, 2006	3.5		(1.6)		(0.2)		—		1.7	2.0
Operating income (loss) for the six months ended:										
June 30, 2007	\$ (0.6)	\$	(2.4)	\$	(1.2)	\$	(3.9)	\$	(8.1) ⁽³⁾	\$ (10.4)
June 30, 2006	16.4		(1.7)		(0.6)		(1.0)		13.1	8.3
Depreciation, depletion and amortization for the three months ended:										
June 30, 2007	\$ 3.1	\$	0.4	\$	—	\$	—	\$	3.5 ⁽²⁾	\$ 3.5
June 30, 2006	3.6		0.4		—		—		4.6	8.6
Depreciation, depletion and amortization for the six months ended:										
June 30, 2007	\$ 6.2	\$	0.8	\$	—	\$	0.1	\$	7.1 ⁽³⁾	\$ 8.0
June 30, 2006	7.2		0.7		—		0.1		8.0	17.4
Total assets as of:										
June 30, 2007	\$ 292.5	\$	35.5	\$	0.2	\$	225.4	\$	553.6 ⁽²⁾	\$ 553.6
December 31, 2006	299.5		36.4		0.9		232.1		568.9	1,009.9

⁽¹⁾ Excludes MGI.

⁽²⁾ As a result of the deconsolidation of the Debtors, their data is not included in the consolidated results of operations for the three months ended June 30, 2007 or in consolidated total assets as of June 30, 2007.

⁽³⁾ Amounts attributable to the Debtors are for the period from January 1, 2007 through January 18, 2007.

4. Cash, Cash Equivalents, Marketable Securities and Investments in Limited Partnerships

The following table presents cash, cash equivalents, marketable securities and other investments, in the aggregate (in millions):

	June 30, 2007	December 31, 2006
Cash and cash equivalents	\$ 40.6	\$ 44.0
Marketable securities	87.7	142.2
Investments in limited partnerships	29.8	26.1
	158.1	212.3
Less: restricted cash and restricted marketable securities	(5.9)	(51.3)
Unrestricted cash and unrestricted marketable securities	<u>\$ 152.2</u>	<u>\$ 161.0</u>

Cash Equivalents

Cash equivalents consist of highly liquid money market instruments with maturities of three months or less. As of June 30, 2007 and December 31, 2006, the carrying amounts of the Company's cash equivalents approximated fair value.

Restricted Cash, Cash Equivalents, Marketable Securities and Other Investments

Cash, marketable securities and other investments include the following amounts which are restricted (in millions):

	June 30, 2007	December 31, 2006
Current:		
Restricted cash and cash equivalents	\$ 2.4 ⁽¹⁾	\$ 3.6
Restricted marketable securities, held in SAR Account	39.5	39.5
	<u>2.4</u>	<u>43.1</u>
Non-Current:		
Restricted Scopac Timber Notes and other amounts held in SAR Account	(1)	2.8
Other amounts restricted under the Scopac Indenture	(1)	2.5
Other long-term restricted amounts	3.5 ⁽¹⁾	5.7
Less: Amounts attributable to Scopac Timber Notes held in SAR Account	(2.8)	(2.8)
	<u>3.5</u>	<u>8.2</u>
Total restricted cash and cash equivalents and marketable securities	<u>\$ 5.9</u>	<u>\$ 51.3</u>

⁽¹⁾ As a result of the deconsolidation of the Debtors, their investment amounts are not included in the consolidated total as of June 30, 2007.

Marketable Securities

Marketable securities consist of the following classification of investments (in millions):

	June 30, 2007 ⁽¹⁾	December 31, 2006
Debt securities:		
Maturities less than one year	\$ 29.5	\$ 100.2
Maturities one to five years	—	6.2
Equity securities and other investments	58.2	35.8
Total marketable securities	<u>\$ 87.7</u>	<u>\$ 142.2</u>

⁽¹⁾ As a result of the deconsolidation of the Debtors, their amounts are not included in the consolidated total as of June 30, 2007.

	June 30, 2007	December 31, 2006
	(In millions of dollars)	
Unrealized gains on available-for-sale investments in other comprehensive income, net	\$ 0.8	\$ 0.6

Included in other comprehensive income are unrealized net gains of \$0.8 million as of June 30, 2007, consisting of unrealized gains of \$0.9 million and unrealized losses of \$0.1 million. As of December 31, 2006, there were unrealized gains of \$0.6 million and no unrealized losses.

5. Debt

Principal amounts of outstanding debt consist of the following (in millions):

	June 30, 2007	December 31, 2006
7.56% Lakepointe Notes due June 8, 2021	\$ 112.7	\$ 113.5
7.03% Motel Notes due May 1, 2018	44.0	44.7
6.08% Beltway Notes due November 9, 2024	28.3	28.6
7.12% Palmas Notes due December 20, 2030	28.5	28.7
Other notes and contracts, primarily secured by receivables, buildings, real estate and equipment	4.4	4.8
Total principal outstanding	217.9	220.3
Forest products segment debt obligations ⁽¹⁾ :		
Palco Revolving Credit Facility	(1)	24.1
Palco Term Loan	(1)	84.3
Scopac Line of Credit	(1)	36.2
6.55% Scopac Class A-1 Timber Notes	(1)	7.3
7.11% Scopac Class A-2 Timber Notes	(1)	243.2
7.71% Scopac Class A-3 Timber Notes	(1)	463.3
Other notes and contracts, primarily secured by receivables, buildings, real estate and equipment	(1)	0.5
Total principal outstanding	(1)	858.9
Less: short term borrowings and current maturities	(4.9)	(180.7)
Scopac Class A-1 Timber Notes held in the SAR Account, at par value	(1)	(2.8)
Discount on sale of Scopac Class A-2 Timber Notes held in SAR Account	(1)	(10.3)
	<u>\$ 213.0</u>	<u>\$ 885.4</u>

⁽¹⁾ As a result of the deconsolidation of the Debtors, their debt amounts are not included in the consolidated total as of June 30, 2007.

Letters of Credit

The Company's real estate segment has posted letters of credit in the amount of \$3.5 million at December 31, 2006 and June 30, 2007 to satisfy certain liability insurance policy requirements.

Loan Covenants

Certain debt instruments restrict the ability of the Company's subsidiaries to transfer assets, make loans and advances or pay dividends to the Company, and require certain subsidiaries to maintain a minimum net worth.

6. Income Taxes

The Company had losses before income taxes of \$6.7 million and \$19.0 million for the second quarter and first six months of 2007, respectively; however, the Company has not recorded any tax benefit during these periods as the Company anticipates an effective tax rate of zero for those years. Each period, the Company evaluates appropriate factors in determining the realizability of the deferred tax assets attributable to losses and credits generated in that period and those being carried forward. Based on this evaluation, the Company provided valuation allowances with respect to the deferred tax assets attributable to the losses and credits generated during the three months and six months ended June 30, 2007. These valuation allowances were in addition to the valuation allowances that were provided in prior years.

On January 1, 2007, the Company adopted the provisions of FIN 48, *Accounting for Uncertainty in Income Taxes – an interpretation of FASB No. 109*. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with FASB No. 109 and prescribes a recognition threshold and measurement attributes for financial statement disclosure of tax positions taken or expected to be taken on a tax return. Under FIN 48, the impact of an uncertain income tax position on the income tax return must be recognized as the largest amount that is more likely than not to be sustained upon audit by the relevant taxing authority. An uncertain tax position need not be recognized if it has less than a 50% likelihood of being sustained. Additionally, FIN 48 provided guidance on the classification of unrecognized tax benefits, disclosures for interest and penalties, accounting and disclosures for interim reporting periods, and transition requirements. The adoption of this standard did not have a material impact on the Company's consolidated financial statements.

The Company has unrecognized tax benefits associated with net operating losses and capital losses. These unrecognized tax benefits, if recognized, would not be expected to affect the effective tax rate because it is expected that valuation allowances would be required in respect of the related tax benefits.

The Company has elected under FIN 48 to classify interest and penalties related to unrecognized tax benefits as income taxes in the financial statements. For the period ended June 30, 2007, there were no recognized or unrecognized interest or penalties related to unrecognized tax benefits.

The Company files U.S. federal income tax returns as well as income tax returns in various states and Puerto Rico. The tax years of 2000 to 2006 remain open to examination by the United States taxing jurisdiction and the tax years 2002 to 2006 remain open to examination by the Puerto Rican taxing jurisdiction. Additionally, any net operating losses that were generated in prior years and utilized in these years may also be subject to examination by the taxing authorities.

7. Employee Benefit Plans

The components of pension and other postretirement benefits expense are as follows (in millions):

	Frozen Pension Benefits		Medical/Life Benefits		Frozen Pension Benefits		Medical/Life Benefits	
	Three Months Ended June 30,				Six Months Ended June 30,			
	2007	2006	2007	2006	2007	2006	2007	2006
Components of net periodic benefit costs:								
Service cost	\$ –	\$ –	\$ –	\$ 0.1	\$ –	\$ –	\$ –	\$ 0.2
Interest cost	0.5	1.4	–	0.1	1.0	2.7	–	0.2
Expected return on assets	(0.5)	(1.4)	–	–	(1.0)	(2.8)	–	–
Amortization of prior service costs	–	–	–	–	–	–	–	–
Recognized net actuarial loss	–	0.1	–	–	–	0.2	–	–
Net periodic benefit costs	<u>\$ –</u>	<u>\$ 0.1</u>	<u>\$ –</u>	<u>\$ 0.2</u>	<u>\$ –</u>	<u>\$ 0.1</u>	<u>\$ –</u>	<u>\$ 0.4</u>

The MAXXAM Pension Plan was frozen effective December 31, 2005; as a result, this plan will continue, but no additional benefits will accrue to participants subsequent to December 31, 2005.

8. Contingencies

Certain present and former directors and officers of the Company are defendants in certain of the actions described below. The Company's bylaws provide for indemnification of its officers and directors to the fullest extent permitted by Delaware law. The Company is obligated to advance defense costs to its officers and directors, subject to the individual's obligation to repay such amount if it is ultimately determined that the individual was not entitled to indemnification. In addition, the Company's indemnity obligation can, under certain circumstances, include amounts other than defense costs, including judgments and settlements.

Actions Involving Present and Former Directors and Officers

In November 2002, the *Cook* action and the *Cave* action were filed in the Superior Court of Humboldt County, California. The defendants in these actions include the Company and certain of its subsidiaries, as well as certain affiliates such as Mr. Charles E. Hurwitz (Chairman and Chief Executive Officer of the Company). The *Cook* action alleges, among other things, that Palco's logging practices have contributed to an increase in flooding along Freshwater Creek (which runs through Palco's timberlands), resulting in personal injury and damages to the plaintiffs' properties. Plaintiffs further allege that in order to have timber harvest plans approved in the affected areas, the defendants engaged

in certain unfair business practices. The plaintiffs seek, among other things, compensatory and exemplary damages, injunctive relief, and appointment of a receiver to ensure the watershed is restored. The *Cave action* contains similar allegations and requests similar relief with respect to the Elk River watershed (a portion of which is contained on Palco's timberlands). In October 2005, the *Johnson action* was filed in Humboldt County Superior Court and contains allegations similar to the *Cave* and *Cook actions*. The defendants in the *Johnson action* include the Company and certain of its subsidiaries and Mr. Hurwitz. The Company does not believe the resolution of these actions should result in a material adverse effect on its consolidated financial condition, results of operations or liquidity.

On December 7, 2006, the *Wilson state action* was filed under seal in the Superior Court of San Francisco, California, and on the same day, the *Wilson federal action* was filed under seal in the U.S. District Court for the Northern District of California. The defendants in the *Wilson actions* include the Company and certain of its forest products subsidiaries, as well as Mr. Hurwitz. The *Wilson actions* allege violations of the California False Claims Act and the Federal False Claims Act, respectively, and are *qui tam* actions (actions ostensibly brought by the government, but on the information and at the instigation of a private individual, who would receive a portion of any amount recovered). As the State of California declined to participate in the *Wilson state action* and the United States declined to participate in the *Wilson federal action*, the seal on each case was lifted and the private individuals are entitled to proceed with the suits. Both suits allege that the defendants made false claims by submitting to the CDF a sustained yield plan misrepresenting as sustainable the projected harvest yields of the timberlands of Palco and Scopac. The remedies being sought are actual damages (essentially based on over \$450.0 million of cash and timberlands transferred by the United States and California in exchange for various timberlands purchased from Palco and its subsidiaries), treble damages and civil penalties of up to \$10,000 for every violation of the California False Claims Act and the Federal False Claims Act, respectively. There can be no assurance that the *Wilson actions* will not have a material adverse impact on the Company's consolidated financial condition, results of operations or liquidity.

OTS Contingency and Related Matters

In December 1995, the OTS initiated the *OTS action*, a formal administrative proceeding against the Company and others alleging, among other things, misconduct by the Respondents and others with respect to the failure of USAT. The OTS sought damages ranging from \$326.6 million to \$821.3 million under various theories. Following 110 days of proceedings before an administrative law judge during 1997-1999, and over two years of post-trial briefing, on September 12, 2001, the administrative law judge issued a recommended decision in favor of the Respondents on each claim made by the OTS. On October 17, 2002, the *OTS action* was settled for \$0.2 million with no admission of wrongdoing on the part of the Respondents.

As a result of the dismissal of the *OTS action*, a related civil action, alleging damages in excess of \$250.0 million, was subsequently dismissed. The *FDIC action* was originally filed by the FDIC in August 1995 against Mr. Hurwitz.

In May 2000, the Respondents filed a counterclaim to the *FDIC action* in the U.S. District Court in Houston, Texas (No. H95-3956). In November 2002, the Respondents filed the Sanctions Motion consisting of an amended counterclaim and an amended motion for sanctions. The Sanctions Motion states that the FDIC illegally paid the OTS to bring the *OTS action* against the Respondents and that the FDIC illegally sued for an improper purpose (i.e., in order to acquire timberlands, held by a subsidiary of the Company). The Respondents are seeking as a sanction to be made whole for the attorneys' fees they have paid (plus interest) in connection with the *OTS and FDIC actions*. As of June 30, 2007, such fees were in excess of \$41.1 million. On August 23, 2005, the District Court ruled on the Sanctions Motion, ordering the FDIC to pay the Respondents \$72.3 million, a portion of which is accrued interest. The FDIC has appealed the District Court decision to the U.S. Fifth Circuit Court of Appeals. The U.S. District Court award has not been accrued as of June 30, 2007 or December 31, 2006. There can be no assurance that the Company will ultimately collect all or any portion of this award.

Other Matters

On December 6, 2005, the *Herrera action* was filed in the state District Court of Harris County, Texas. The defendants in this action are SHRP, Ltd. and its managing general partner. The plaintiffs allege, among other things, that due to the gross negligence of SHRP, Ltd., Mr. Herrera was thrown while exercising a horse at Sam Houston Race Park, rendering him a paraplegic. The case was settled in July 2007; the settlement did not have a material adverse effect on the Company's consolidated financial condition, results of operations or liquidity.

On September 2, 2004, the Company was advised that the NJDEP alleged that one of its former subsidiaries is a successor to a company that manufactured munitions for the U.S. Navy during World War II. The owner of the underlying property, which is located in Cranbury, New Jersey, was seeking the Company's participation in efforts to address contamination of the site resulting from such operations. In January 2005, MGI and the owner of the property entered into an Administrative Consent Order with the NJDEP providing for, among other things, cleanup of the facility.

In April 2005, MGI filed a Complaint against the United States of America, the U.S. Navy, and the U.S. Army for cost recovery and contribution; the defendants subsequently denied all of the claims. In early 2006, the property was sold to a new owner and the Administrative Consent Order was amended to substitute the new owner for the original property owner. MGI also reached an agreement with several potentially responsible parties regarding cleanup at the site, the terms of which the Company believes will not result in a material adverse effect on the Company's consolidated financial position, results of operations or liquidity. MGI retained its cause of action against the government parties noted above.

The Company is involved in other claims, lawsuits and proceedings. While uncertainties are inherent in the final outcome of such matters and it is presently impossible to determine the actual costs that ultimately may be incurred or their effect on the Company, management believes that the resolution of such other uncertainties and the incurrence of such costs should not result in a material adverse effect on the Company's consolidated financial condition, results of operations or liquidity.

9. Stock-Based Compensation Plans

Under the Company's stock-based compensation plans, stock options and similar instruments may be granted to employees and outside directors at no less than the fair market value of the Company's Common Stock on the date of grant. Grants generally vest ratably over a five-year period for grants to employees and over a four-year period for grants to outside directors and expire ten years after the grant date. Grants have generally been settled in cash upon exercise.

The fair value of grants is determined using a Black-Scholes option-pricing model. The following assumptions apply to the options granted through the periods presented.

	Six Months Ended June 30,	
	2007	2006
Expected volatility	30%	34%
Expected dividends	—	—
Expected term (in years)	7.33	6.34
Risk-free rate	4.9%	5.1%

Expected volatilities are based on historical volatility of the market price for the Company's Common Stock. The dividend yield on the Company's Common Stock is assumed to be zero since the Company has not paid dividends in the past five years and has no current plans to do so in the future. The Company uses historical experience regarding exercises of grants to determine the grants' expected term. The expected term represents the period of time that the options granted are expected to remain outstanding. The risk-free interest rate is based on the U.S. Treasury yield curve in effect for the expected term of the option at the reporting date.

A summary of activity under the Company's stock option plans during 2007 is presented below:

	Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in millions)
Balance at January 1, 2007	1,081,853	\$ 25.06		
Granted	2,400	29.25		
Exercised	(37,652)	17.00		
Forfeited or expired	(65,440)	45.04		
Balance at June 30, 2007	981,161	\$ 24.55	5.27	\$ 7.3
Exercisable at June 30, 2007	696,569	\$ 23.98	4.25	\$ 6.1

The Company has recognized a liability for stock-based compensation in the amount of \$6.4 million at June 30, 2007 and \$7.2 million at December 31, 2006. Total compensation cost for share-based payment arrangements for the six months ended June 30, 2007, was \$0.9 million. As of June 30, 2007, total estimated compensation related to non-vested grants not yet recognized is \$3.3 million, although the Company may ultimately not have to pay all of such amount, and the weighted average period over which it is expected to be recognized is 2.0 years. During the six months ended June 30, 2007, options with a fair value of \$0.6 million were exercised, resulting in cash payments of \$0.4 million, (the difference between the market price of the stock on the exercise date and the option strike price). During the six months ended June 30, 2006, no options were exercised. 3,400 options with a fair value of \$0.1 million vested during the three months and six months ended June 30, 2007. Options granted during the six months ended June 30, 2007 and

2006 had a grant date fair value of \$0.1 million and \$0.2 million, respectively. There were no shares issued during the six months ended June 30, 2007 and 2006 as the result of stock option exercises.

10. Per Share Information

The weighted average number of shares used to determine basic and diluted earnings per share was:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Weighted average number of common shares outstanding - basic: ..	5,251,226	5,665,846	5,253,267	5,816,059
Effect of dilution ⁽¹⁾ :				
Conversion of Class A Convertible Preferred Stock	—	—	—	—
Exercise of stock options	—	—	—	—
Weighted average number of common and common equivalent shares - diluted:	<u>5,251,226</u>	<u>5,665,846</u>	<u>5,253,267</u>	<u>5,816,059</u>

- ⁽¹⁾ The Common Stock options and Class A Preferred Stock were not included in the computation of basic or diluted earnings per share because the Company had a loss for the three months and six months ended June 30, 2007 and 2006, respectively, and the effect would thus be anti-dilutive. If the Company was required to include dilutive shares in its per share calculations, the number of dilutive shares for the three months ended June 30, 2007 and 2006 would be 949,876 and 1,010,337, respectively. The number of dilutive shares for the six months ended June 30, 2007 and 2006 would be 808,998 and 839,228, respectively.

11. Comprehensive Loss

The following table sets forth comprehensive loss (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Net loss:	\$ (6.7)	\$ (11.2)	\$ (19.0)	\$ (21.4)
Other comprehensive loss:				
Unrealized gain on available-for-sale investments	0.2	—	0.2	0.2
Total comprehensive loss	<u>\$ (6.5)</u>	<u>\$ (11.2)</u>	<u>\$ (18.8)</u>	<u>\$ (21.2)</u>

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following should be read in conjunction with the financial statements in Part I, Item 1 of this Report and Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations" and Item 8. "Financial Statements and Supplementary Data" of the Form 10-K. Any capitalized terms used but not defined in this Item are defined in the "Glossary of Defined Terms" contained in Appendix A. Except as otherwise noted, all references to Notes refer to the Condensed Notes to Consolidated Financial Statements included herein.

This Quarterly Report on Form 10-Q contains statements which constitute "forward-looking statements" within the meaning of the PSLRA. These statements appear in a number of places in this report. Such statements can be identified by the use of forward-looking terminology such as "believes," "expects," "may," "estimates," "will," "should," "could," "plans," "intends," "projects," "seeks," or "anticipates" or the negative thereof or other variations thereon or comparable terminology, or by discussions of strategy. Readers are cautioned that any such forward-looking statements are not guarantees of future performance and involve significant risks and uncertainties, and that actual results may vary materially from the forward-looking statements as a result of various factors. These factors include the effectiveness of management's strategies and decisions, general economic and business conditions, developments in technology, new or modified statutory, environmental or regulatory requirements, litigation developments, and changing prices and market conditions. This Form 10-Q and the Form 10-K identify other factors which could cause differences between such forward-looking statements and actual results. No assurance can be given that these are all of the factors that could cause actual results to vary materially from the forward-looking statements.

Results of Operations

This section contains statements which constitute "forward-looking statements" within the meaning of the PSLRA. See the statement in the second paragraph of Item 2. above for cautionary information with respect to such forward-looking statements.

The Company now operates in two primary industries: real estate investment and development, through various subsidiaries and joint ventures; and racing operations through SHRP, Ltd. MGHI owns 100% of MGI and is a wholly owned subsidiary of the Company. MGI owns 100% of the common stock of Palco, which, along with its subsidiaries, recently filed for protection under Chapter 11 of the Bankruptcy Code. See Note 1 for information regarding the deconsolidation of the Debtors' financial results, the Debtors' Chapter 11 proceedings, and the accounting treatment of MGI's investment in the Debtors. Any reference herein to a company includes the subsidiaries of that company unless otherwise noted or the context indicates otherwise.

Consolidated Operations

Selected Operational Data

The following table presents selected proforma financial information for the periods indicated for the Company's consolidated operations, excluding the Debtors (in millions).

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Sales	\$ 23.3	\$ 29.7	\$ 47.6	\$ 72.1
Costs and expenses	(27.6)	(28.0)	(55.7)	(59.0)
Operating income (loss)	(4.3)	1.7	(8.1)	13.1
Other income, net	1.8	1.8	2.9	6.0
Interest expense, including amortization of deferred financing costs	(4.2)	(4.3)	(8.5)	(8.7)
Income (loss) before income taxes and cumulative effect of accounting change	(6.7)	(0.8)	(13.7)	10.4
Benefit for income taxes	—	(0.5)	—	(0.5)
Income (loss) before cumulative effect of accounting change	(6.7)	(1.3)	(13.7)	9.9
Cumulative effect of accounting change, net of tax	—	—	—	(0.7)
Net income (loss)	<u>\$ (6.7)</u>	<u>\$ (1.3)</u>	<u>\$ (13.7)</u>	<u>\$ 9.2</u>

Overview of Results of Operations, Excluding the Debtors

Sales

Sales, excluding the Debtors, for the three months and six months ended June 30, 2007, declined \$6.4 million and \$24.5 million, respectively, as compared to the comparable periods in the prior year, primarily due to the substantial sell-out of lots at Mirada in 2006 and a reduction in deferred profit and profit participation payments at Palmas in 2007.

Operating Income (Loss)

The Company's operating losses, excluding the Debtors, for the three months and six months ended June 30, 2007 declined \$6.0 million and \$21.2 million, respectively, as compared to the same comparable periods in the prior year, due primarily to the decline in real estate sales noted above.

Other Income, net

Consolidated other income for the six months ended June 30, 2007, was impacted by lower returns on marketable securities and other short-term investments.

Real Estate Operations

Industry Overview and Selected Operational Data

The Company, principally through its wholly owned subsidiaries and joint ventures, invests in and develops residential and commercial real estate primarily in Puerto Rico, Arizona, California and Texas. Results of operations between quarterly periods for the Company's real estate operations are generally not comparable due to the timing of individual real estate sales transactions and cash collections. Accordingly, results for any one quarter are not necessarily indicative of results to be expected for the full year. In 2005 and 2006, the Company's real estate operations realized substantial revenues related to sales at the Company's Fountain Hills, Mirada and Palmas developments. As the proceeds from these asset sales have not been redeployed on other real estate assets, this level of sales activity is not expected to recur for the foreseeable future.

The following table presents selected operational and financial information for the three months and six months ended June 30, 2007 and 2006, for the Company's real estate operations.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(In millions of dollars)			
Sales:				
Real estate:				
Fountain Hills	\$ 2.3	\$ 1.1	\$ 4.9	\$ 3.2
Mirada	1.4	6.8	1.4	15.9
Palmas	0.1	1.9	0.2	10.5
Total	<u>3.8</u>	<u>9.8</u>	<u>6.5</u>	<u>29.6</u>
Resort, commercial and other:				
Fountain Hills	0.9	1.1	2.1	2.1
Palmas	3.4	3.7	6.5	7.1
Commercial lease properties	4.6	4.6	9.2	9.2
Other	0.1	—	0.1	0.2
Total	<u>9.0</u>	<u>9.4</u>	<u>17.9</u>	<u>18.6</u>
Total sales	<u>\$ 12.8</u>	<u>\$ 19.2</u>	<u>\$ 24.4</u>	<u>\$ 48.2</u>
Operating income (loss):				
Fountain Hills	\$ 0.5	\$ (0.3)	\$ 0.7	\$ 0.1
Mirada	0.7	3.3	0.6	8.1
Palmas	(3.2)	(1.2)	(6.1)	4.7
Commercial lease properties	2.6	2.1	5.2	4.2
Other	(0.6)	(0.4)	(1.0)	(0.7)
Total operating income (loss)	<u>\$ —</u>	<u>\$ 3.5</u>	<u>\$ (0.6)</u>	<u>\$ 16.4</u>
Investment, interest and other income:				
Equity in earnings (losses) from real estate joint ventures	\$ 0.4	\$ (0.1)	\$ 0.4	\$ (0.3)
Other	0.6	1.6	0.8	2.8
	<u>\$ 1.0</u>	<u>\$ 1.5</u>	<u>\$ 1.2</u>	<u>\$ 2.5</u>
Interest expense	(4.3)	(4.3)	(8.5)	(8.7)
Income (loss) before income taxes and cumulative effect of accounting change	<u>\$ (3.3)</u>	<u>\$ 0.7</u>	<u>\$ (7.9)</u>	<u>\$ 10.2</u>

Sales and Operating Income (Loss)

Total sales and operating income for the real estate operations for the three months and six months ended June 30, 2007 declined substantially, as compared to the same periods in 2006, primarily due to the substantial sell-out of lots at Mirada in 2006 and a reduction in deferred profit and profit participation payments at Palmas in 2007, partially offset by higher sales at Fountain Hills.

Racing Operations

Industry Overview and Selected Operational Data

The Company owns SHRP, Ltd., which owns and operates Sam Houston Race Park, a Class 1 horse racing facility in Houston, Texas, and Valley Race Park, a greyhound racing facility located in Harlingen, Texas. Results of operations between quarterly periods are generally not comparable for these facilities due to the timing, varying lengths and types of racing meets held. Accordingly, results for any one quarter are not necessarily indicative of results to be expected for any other quarter or for the full year. Historically, Sam Houston Race Park and Valley Race Park have derived a significant amount of their annual pari-mutuel commissions from live racing and simulcasting. Pari-mutuel commissions have typically been highest during the first and fourth quarters of the year, the time during which Sam Houston Race Park and Valley Race Park have historically conducted live thoroughbred and greyhound racing, respectively. In an effort to increase attendance on days with live racing, Sam Houston Race Park in June 2007 expanded and enhanced its summer concert series, including improving its facilities to allow the concerts to be held on the race track's infield.

The following table presents selected operational and financial information for the three months and six months ended June 30, 2007 and 2006, for the Company's racing operations.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(In millions of dollars)			
Number of live race days:				
Sam Houston Race Park	7	11	46	53
Valley Race Park	8	10	70	72
Handle:				
Sam Houston Race Park:				
On-track handle	\$ 32.8	\$ 34.0	\$ 63.6	\$ 67.1
Off-track handle	11.9	12.2	83.8	89.3
Total	<u>\$ 44.7</u>	<u>\$ 46.2</u>	<u>\$ 147.4</u>	<u>\$ 156.4</u>
Valley Race Park:				
On-track handle	\$ 4.3	\$ 4.4	\$ 9.8	\$ 10.3
Off-track handle	0.3	0.4	2.9	2.8
Total	<u>\$ 4.6</u>	<u>\$ 4.8</u>	<u>\$ 12.7</u>	<u>\$ 13.1</u>
Sales:				
Sam Houston Race Park:				
Gross pari-mutuel commissions	\$ 7.6	\$ 7.8	\$ 16.5	\$ 17.3
Other revenues	1.8	1.6	3.7	3.6
Total	<u>9.4</u>	<u>9.4</u>	<u>20.2</u>	<u>20.9</u>
Valley Race Park:				
Gross pari-mutuel commissions	1.0	1.0	2.4	2.5
Other revenues	0.1	0.1	0.6	0.5
Total	<u>1.1</u>	<u>1.1</u>	<u>3.0</u>	<u>3.0</u>
Total sales	<u>\$ 10.5</u>	<u>\$ 10.5</u>	<u>\$ 23.2</u>	<u>\$ 23.9</u>
Operating loss:				
Sam Houston Race Park	\$ (1.2)	\$ (0.7)	\$ (1.5)	\$ (0.5)
Valley Race Park	(0.3)	(0.2)	(0.5)	(0.3)
Other	(0.3)	(0.7)	(0.4)	(0.9)
Total operating loss	<u>\$ (1.8)</u>	<u>\$ (1.6)</u>	<u>\$ (2.4)</u>	<u>\$ (1.7)</u>
Loss before income taxes and cumulative effect of accounting change ..	<u>\$ (1.7)</u>	<u>\$ (1.5)</u>	<u>\$ (2.3)</u>	<u>\$ (1.6)</u>

Sales

Total sales remained flat for the three months ended June 30, 2007, as compared to the prior year period. Declines in the number of live racing days, average daily attendance and associated wagering at Sam Houston Race Park were offset by increases in entertainment revenue.

Total sales declined \$0.7 million for the six months ended June 30, 2007, as compared to the prior year period, principally due to declines in average daily attendance and associated wagering at Sam Houston Race Park.

Operating Loss

Total operating loss increased by \$0.2 million in the second quarter of 2007, as compared to the prior year period, principally due to costs associated with the concert-related changes at Sam Houston Race Park, partially offset by lower spending at Laredo LLC.

Total operating losses increased by \$0.7 million for the six months ended June 30, 2007, as compared to the prior year period, principally due to the decline in revenue discussed above and costs associated with the concert-related changes at Sam Houston Race Park, partially offset by lower spending at Laredo LLC.

Other Items Not Directly Related to Industry Segments

Corporate

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(In millions of dollars)			
Operating loss	\$ (2.0)	\$ —	\$ (3.9)	\$ (1.0)
Income (loss) before income taxes and cumulative effect of accounting change	(1.2)	0.3	(2.3)	2.4

Operating Loss

Corporate operating losses represent general and administrative expenses that are not attributable to the Company's industry segments and include stock-based compensation expense. The \$2.0 million increase in operating losses in the second quarter of 2007, as compared to the prior year period, is primarily due to changes in stock-based compensation expense resulting from fluctuations in the quoted market price of the Company's Common Stock and an increase in legal fees, partially offset by cost cutting initiatives. Stock-based compensation expense was a benefit of \$0.9 million and \$2.2 million for the three months ended June 30, 2007 and 2006, respectively.

The \$2.9 million increase in operating losses for the six months ended June 30, 2007, as compared to the prior year period, is primarily due to changes in stock-based compensation expense resulting from fluctuations in the quoted market price of the Company's Common Stock and an increase in legal fees, partially offset by cost cutting initiatives. Stock-based compensation expense was a benefit of \$0.4 million and \$3.4 million for the six months ended June 30, 2007 and 2006, respectively.

Income (Loss) Before Income Taxes and Cumulative Effect of Accounting Change

The overall loss before income taxes and cumulative effect of accounting changes for the three months and six months ended June 30, 2007 is the result of the cost changes discussed above and earnings on marketable securities and other short-term investments. Earnings on investments were \$0.8 million for the three months ended June 30, 2007, as compared to \$0.3 million in the prior year period. Earnings on investments were \$1.6 million for the six months ended June 30, 2007, as compared to \$3.4 million in the prior year period.

MGI

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(In millions of dollars)			
Operating loss	\$ (0.5)	\$ (0.2)	\$ (1.2)	\$ (0.6)
Loss before income taxes and cumulative effect of accounting change	(0.5)	(0.2)	(1.2)	(0.6)

Operating Loss

MGI's operating losses represent MGI's general and administrative expenses on a stand-alone basis (excluding Debtors) and consists primarily of auditing and legal fees.

Debtors' Operations

The following table presents selected operational and financial information for the periods indicated for the Debtors' operations.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007 ⁽⁶⁾	2006
	(In millions of dollars, except shipments and prices)			
Timber harvest ⁽¹⁾	17.2	21.1	35.1	35.3
Shipments:				
Lumber: ⁽²⁾				
Redwood upper grades	1.2	1.5	2.8	2.1
Redwood common grades	14.7	27.0	40.9	64.0
Douglas-fir upper grades	—	—	—	—
Douglas-fir common grades	14.3	22.3	23.7	45.4
Other	—	1.2	—	1.6
Total lumber	30.2	52.0	67.4	113.1
Cogeneration power ⁽³⁾	25.7	25.6	46.9	53.5
Average sales price:				
Lumber: ⁽⁴⁾				
Redwood upper grades	\$ 1,382	\$ 1,875	\$ 1,372	\$ 1,737
Redwood common grades	815	711	733	666
Douglas-fir upper grades	—	—	—	—
Douglas-fir common grades	290	365	302	365
Cogeneration power ⁽⁵⁾	71	76	74	70
Sales:				
Lumber, net of discount	\$ 23.8	\$ 30.6	\$ 46.9	\$ 63.1
Logs	4.9	(0.4)	10.1	1.6
Cogeneration power	2.0	2.0	3.7	3.9
Wood chips	1.2	0.8	2.4	1.5
Other	0.8	0.8	1.6	1.5
Total sales	\$ 32.7	\$ 33.8	\$ 64.7	\$ 71.6
Operating income (loss) ⁽⁷⁾	\$ (13.4)	\$ 0.3	\$ (25.3)	\$ (4.8)
Loss before income taxes and cumulative effect of accounting change	\$ (28.0)	\$ (14.6)	\$ (60.8)	\$ (35.3)

⁽¹⁾ Timber harvest is expressed in millions of board feet, net Scribner scale.

⁽²⁾ Lumber shipments are expressed in millions of board feet.

⁽³⁾ Power deliveries are expressed in thousands of megawatt hours.

⁽⁴⁾ Dollars per thousand board feet.

⁽⁵⁾ Dollars per megawatt hour.

⁽⁶⁾ The amounts shown in this table represent the Debtors' operating results for the six months ended June 30, 2007. The operating results of the Debtors from January 1, 2007 to January 18, 2007 are included in the Company's consolidated financial statements. See Note 3.

⁽⁷⁾ Operating income (loss) includes bankruptcy-related legal and advisor fees of \$8.1 million for the three months ended June 30, 2007 and \$13.8 million for the six months ended June 30, 2007.

Sales

Sales for the three months and six months ended June 30, 2007, declined \$1.1 million and \$6.9 million, respectively, as compared to the prior year periods, primarily due to lower shipments of redwood and Douglas-fir lumber, partially offset by an increase in the volume of Douglas-fir logs sold.

Operating Loss and Loss Before Income Taxes and Cumulative Effect of Accounting Change

The Debtors reported operating losses of \$13.4 million and \$25.3 million for the three months and six months ended June 30, 2007, respectively, which includes bankruptcy-related costs of \$8.1 million and \$13.8 million, respectively. Additionally, the Debtors' interest expense for the three months and six months ended June 30, 2007, was higher than that of the prior year periods as a result of increased debt levels and higher interest rates.

Financial Condition and Investing and Financing Activities

This section contains statements which constitute “forward-looking statements” within the meaning of the PSLRA. See the statement in the second paragraph of Item 2. above for cautionary information with respect to such forward-looking statements.

Overview

The Company conducts its operations primarily through its subsidiaries. Creditors of subsidiaries of the Company have priority with respect to the assets and earnings of such subsidiaries over the claims of the creditors of the Company.

Cash Flow

The following table summarizes certain data related to financial condition and to investing and financing activities of the Company, for the periods presented (in millions).

	Real Estate	Racing	MGI	MAXXAM Parent	Total Excluding Debtors	Debtors	Consolidated Total
	(In millions of dollars)						
<u>Debt and credit facilities (excluding intercompany notes)</u>							
Short-term borrowings and current maturities of long-term debt:							
June 30, 2007	\$ 4.7	\$ 0.2	\$ —	\$ —	\$ 4.9	⁽¹⁾ \$ —	\$ 4.9
December 31, 2006	4.7	0.2	—	—	4.9	175.8	180.7
Long-term debt, excluding current maturities and discounts:							
June 30, 2007	\$ 212.8	\$ 0.2	\$ —	\$ —	\$ 213.0	⁽¹⁾ \$ —	\$ 213.0
December 31, 2006	215.3	0.2	—	—	215.5	669.9	885.4
<u>Cash, cash equivalents, marketable securities and other investments</u>							
June 30, 2007:							
Current restricted amounts	\$ 0.3	\$ 2.1	\$ —	\$ —	\$ 2.4	⁽¹⁾ \$ —	\$ 2.4
Other current amounts	20.7	1.7	—	129.8	152.2	⁽¹⁾ —	152.2
	<u>21.0</u>	<u>3.8</u>	<u>—</u>	<u>129.8</u>	<u>154.6</u>	⁽¹⁾ <u>—</u>	<u>154.6</u>
Long-term restricted amounts							
	3.5	—	—	—	3.5	⁽¹⁾ —	3.5
	<u>\$ 24.5</u>	<u>\$ 3.8</u>	<u>\$ —</u>	<u>\$ 129.8</u>	<u>\$ 158.1</u>	⁽¹⁾ <u>\$ —</u>	<u>\$ 158.1</u>
<u>Changes in cash and cash equivalents</u>							
Capital expenditures:							
June 30, 2007	\$ 0.4	\$ 1.4	\$ —	\$ 0.1	\$ 1.9	⁽²⁾ \$ —	\$ 1.9
June 30, 2006	0.7	0.2	—	—	0.9	3.3	4.2
Net proceeds from dispositions of property and investments:							
June 30, 2007	\$ 0.1	\$ —	\$ —	\$ —	\$ 0.1	⁽²⁾ \$ —	\$ 0.1
June 30, 2006	—	—	—	—	—	8.1	8.1
Borrowings (repayments) of debt and credit facilities, net of financing costs:							
June 30, 2007	\$ (2.2)	\$ (0.1)	\$ —	\$ —	\$ (2.3)	⁽²⁾ \$ 2.2	\$ (0.1)
June 30, 2006	(1.8)	(0.1)	—	—	(1.9)	(18.3)	(20.2)
Dividends, advances including interest paid, and tax sharing payments received (paid):							
June 30, 2007	\$ 1.1	\$ 2.5	\$ (0.4)	\$ (3.2)	\$ —	⁽²⁾ \$ —	\$ —
June 30, 2006	(1.6)	1.0	7.6	(27.0)	(20.0)	20.0	—

⁽¹⁾ As a result of the deconsolidation of the Debtors discussed in Note 1, their data is not included in the consolidated total as of June 30, 2007.

⁽²⁾ Amounts attributable to the Debtors are for the period from January 1, 2007 through January 18, 2007.

Operating Activities

The Company's operating activities used cash of \$5.7 million in the six months ended June 30, 2007, primarily due to a low level of real estate sales during the first half of 2007.

Investing Activities

Net cash provided by investing activities of \$5.2 million for the six months ended June 30, 2007, primarily reflects net purchases of short-term investments. Net cash provided by investing activities of \$15.7 million for the six months ended June 30, 2006, reflected net proceeds from restricted cash and proceeds from the disposition of assets by the Debtors.

Financing Activities

Net cash provided by financing activities of \$0.4 million in the six months ended June 30, 2007, principally reflects additional borrowings by the Debtors to fund their operations from January 1, 2007 to January 18, 2007, offset by repayments on long-term debt. Net cash used for financing activities of \$41.7 million for the six months ended June 30, 2006, reflects scheduled debt payments by the Debtors and treasury stock purchases.

MAXXAM Parent

MAXXAM Parent has in the past provided, and may from time to time in the future, under circumstances determined to be appropriate, provide various forms of direct or indirect financial or liquidity assistance to its subsidiaries, or enter into financing or other transactions with its subsidiaries, including secured or unsecured loans, or asset purchases. There can be no assurance that such subsidiaries will have sufficient liquidity to repay intercompany loans.

Although there are no restrictions on the Company's ability to pay dividends on its capital stock, the Company has not paid any dividends for a number of years and has no present intention to do so. The Company has in the past and may from time to time in the future purchase shares of its Common Stock on national exchanges or in privately negotiated transactions. During the second quarter of 2007, MAXXAM Parent purchased 1,100 shares of its Common Stock at an average price of \$30.05 per share.

At June 30, 2007, MAXXAM Parent had unrestricted cash, cash equivalents and marketable securities and other investments of \$129.8 million and MAXXAM Parent did not have any external debt. MAXXAM Parent believes that its existing resources will be sufficient to fund its working capital requirements for the next year. With respect to long-term liquidity, MAXXAM Parent believes that its existing cash and cash resources, together with future distributions from the real estate segment, will be sufficient to meet its long-term working capital requirements.

See the "Potential Impact on Registrant and Certain Related Entities" section of Note 1 for a discussion of the potential impact of the Bankruptcy Cases on the Company's liquidity.

Real Estate Operations

At June 30, 2007, the real estate segment had cash, cash equivalents and other investments of \$24.5 million, of which \$3.8 million is restricted. Real estate management believes that the segment's existing cash and credit facilities will be sufficient to fund its working capital and capital expenditure requirements for 2007. With respect to the segment's long-term liquidity, real estate management believes that the ability to generate cash from the sale of existing assets, together with the ability to obtain financing and joint venture partners, should provide sufficient funds to meet its working capital and capital expenditure requirements.

Capital expenditures and real estate improvements and development costs were \$5.7 million for the first half of 2007 and are expected to be between approximately \$6.0 million and \$8.0 million for the remainder of 2007. The Company expects that these expenditures will be funded by existing cash and available credit facilities. Subject to available resources, the Company's real estate segment may purchase additional properties and/or seek other investment ventures from time to time as appropriate opportunities arise.

Racing Operations

At June 30, 2007, the racing segment had cash, cash equivalents and other investments of \$3.8 million, of which \$2.1 million is restricted. SHRP, Ltd.'s management expects that SHRP, Ltd. will require additional advances from MAXXAM Parent to fund its operations and capital expenditures in the future. SHRP, Ltd. is experiencing strong competition from Internet wagering and "racinos" in surrounding states. These factors are also expected to adversely affect the long-term liquidity of SHRP, Ltd.

Capital expenditures and investments in new ventures were \$1.4 million for the first half of 2007 and an additional \$1.1 million is expected for the remainder of 2007. Subject to available resources, the Company's racing segment may purchase additional properties and/or seek to expand its operations as opportunities arise that are determined to be appropriate.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet financing, other than operating leases entered into in the normal course of business. The Company does not use derivatives for any of its treasury or risk management activities.

Trends

Real Estate Operations

The Company's real estate segment is engaged in marketing and sales programs of varying magnitudes at its real estate developments. The Company intends to continue selling undeveloped acreage and semi-developed parcels, generally to builders and developers, and fully developed lots to individuals and builders. In 2005 and 2006, the Company's real estate operations realized substantial revenues related to sales at the Company's Fountain Hills, Mirada and Palmas developments. As the proceeds from these asset sales have not been redeployed on other real estate assets, this level of sales activity is not expected to recur for the foreseeable future. The real estate segment may purchase additional properties and/or seek other investment ventures as appropriate opportunities arise.

Racing Operations

The Company has in the past pursued and intends to continue vigorously pursuing Texas gaming legislation favorable to it. The regular legislative session of the Texas Legislature that ended in May 2007 did not result in legislation that enhances state revenues through additional forms of gaming. The next opportunity for approval of such legislation will be during the regular session of the Texas Legislature that begins in January 2009 or any special legislative session that might be held prior to January 2009. Some gaming legislation may require the approval of two-thirds of each legislative house and a majority of Texas voters, and no assurance can be given that any such legislation will be enacted or become effective. Moreover, it is impossible to determine what the provisions of any such legislation would be or to predict its effect on the Company.

In January 2004, a subsidiary of the Company, Laredo LLC, applied to the Racing Commission for an additional license to construct and operate a Class 2 horse racing facility in Laredo, Texas. Following a hearing on Laredo LLC's application and that of a competing applicant, in September 2006, two state administrative law judges recommended to the Racing Commission that Laredo LLC be awarded the license. On March 20, 2007, the Racing Commission ruled that both Laredo LLC and the competing applicant be awarded licenses for the Laredo area. At the August 8, 2007, Racing Commission meeting, Laredo LLC was awarded a license effective September 1, 2007.

In June 2007, Sam Houston Race Park expanded and enhanced its outdoor concert series in an effort to increase attendance on days with live racing.

Critical Accounting Policies and Estimates

See Item 7. "Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies and Estimates" of the Form 10-K for a discussion of the Company's critical accounting policies. There have been no material changes to the Company's critical accounting policies and estimates provided in the Form 10-K except for the deconsolidation of the Debtors as described in Note 1.

New Accounting Pronouncements

See Note 2 for a discussion of new accounting pronouncements and their impact on the Company's consolidated financial statements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

On January 18, 2007, Palco and its five subsidiaries, including Scopac, filed separate voluntary petitions in the United States Bankruptcy Court for the Southern District of Texas for reorganization under Chapter 11 of the Bankruptcy Code. See Note 1 to the Condensed Consolidated Financial Statements for additional information. As a result of the deconsolidation of these entities, the Company no longer has variable interest rate debt.

The Company's cash flow and income may be affected by changes in domestic short-term interest rates due to the investment of available cash in money market funds and auction rate securities. We monitor our net exposure to short-term interest rates and, as appropriate, reallocate investments to maximize returns.

The valuation of our marketable equity security portfolio is subject to equity price risk. We monitor our net exposure to equity price risk and, as appropriate, reallocate investments to minimize the Company's exposure.

The Company does not manage risk through use of derivatives, hedges or other complex financial instruments.

ITEM 4. CONTROLS AND PROCEDURES

The Company maintains disclosure controls and procedures that are designed to ensure that information required to be disclosed in the Company's reports under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Also, the Company has investments in certain unconsolidated entities. As the Company does not control or manage these entities, its disclosure controls and procedures with respect to such entities are necessarily substantially more limited than those it maintains with respect to its consolidated subsidiaries.

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

As of the end of the period covered by this report, our management carried out an evaluation, under the supervision and with the participation of our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on the evaluation, our management, including our Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective as of June 30, 2007.

Changes in Internal Controls Over Financial Reporting

Since December 31, 2006, there have been no significant changes in the Company's internal controls over financial reporting that materially affected or are reasonably likely to materially affect the internal controls over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

The information set forth in Note 8 is incorporated herein by reference.

ITEM 1A. RISK FACTORS

Part I, Item 1A of the Form 10-K contains important risk factors that could cause the Company's actual results to differ materially from those projected in any forward-looking statement. Additional risks and uncertainties not currently known or that are currently deemed immaterial may materially adversely impact our business, financial condition or operating results.

The information presented below updates, and should be read in conjunction with, the risk factor information disclosed in the Form 10-K for the year ended December 31, 2006.

The Company has removed all of the risks under the headings “Risks Related to Forest Products Regulatory Matters” and “Other Risks Related to Our Forest Products Operations” since forest products operations are no longer consolidated with the Company’s financial results.

The Company has amended and restated the second and third items under “Risk Factors: Risks related to the Bankruptcy Cases” to read as follows:

The Debtors may not be able to reorganize successfully, and the Company could lose some or all of its equity ownership interest.

The Debtors’ overall objectives in the Bankruptcy Cases are to achieve an operational and financial restructuring of each of the Debtors’ long-term debt obligations in view of estimated lower harvest levels, increased regulatory compliance costs and cyclical lumber prices, and also to continue their businesses. The Debtors may not be able to attain these objectives and achieve a successful operational and financial reorganization. If the Debtors are unsuccessful in attaining a successful operational and financial reorganization, the Debtors could be forced to surrender all or substantially all of their assets to their creditors.

As provided by the Bankruptcy Code, each of the Debtors generally has the exclusive right to propose a plan of reorganization during the Exclusivity Period, which has been extended to September 18, 2007. The Debtors’ objective is to file such plan(s) during the Exclusivity Period, but may be required to request additional extensions, depending on various factors. The Bankruptcy Court is not obligated to approve any such extension request.

The Debtors are pursuing discussions in order to accomplish restructuring plan(s) on a consensual basis, but consensual plan(s) of reorganization may not be agreed upon. Once reorganization plan(s) are filed, the Debtors are required to seek approval of the plan(s) by the creditors and equity holders entitled to vote on the plan(s), and to seek confirmation of the plan(s) by the Bankruptcy Court. The Debtors’ efforts to obtain creditor approvals and Bankruptcy Court confirmation may not be successful. If the Debtors fail to file plans of reorganization during the Exclusivity Period or any extension thereof, or if such plans are not accepted by the requisite creditors and equity holders entitled to vote on the plans, or if the Debtors do not obtain Bankruptcy Court confirmation, other parties in interest in the Bankruptcy Cases may be permitted to propose their own plans of reorganization for the Debtors.

The Debtors anticipate that substantially all of their liabilities as of the Filing Date will be resolved under one or more plans of reorganization proposed, voted on and confirmed in accordance with the Bankruptcy Code. However, there can be no assurance that the liabilities of one or more of the Debtors will not exceed the fair value of its or their assets. If a debtor’s creditors are not paid in full, the Bankruptcy Code provides that the debtor’s equity holder will not be entitled to retain its equity interest, unless certain exceptions apply. If the liabilities of one or more of the Debtors are ultimately found to exceed the fair value of its assets, claims of creditors could be paid at less than 100% of their face value. In that event, Palco could lose all or a material portion of its equity ownership in Scopac and Palco’s other subsidiaries, MGI could lose all or a material portion of its equity ownership in Palco, or the value of such equity ownership could be diluted, impaired or eliminated.

The Palco Debtors and Scopac may be unable to obtain sufficient additional liquidity to continue operations and reorganize successfully under Chapter 11.

The Palco Debtors estimate that they will have significant liquidity shortfalls in 2007. On August 6, 2007, the Palco Debtors closed on the DIP Facility, which is a \$75.0 million Debtor-in-Possession revolving credit facility. The DIP Facility contains restrictive financial covenants that, among others, require the Palco Debtors to maintain a minimum level of EBITDA and meet weekly cash flow projections. Continued compliance with the DIP Facility is dependent on the ability of the Palco Debtors to meet the financial covenants. However, the operating cash flow estimates used to establish the EBITDA maintenance covenant and the weekly cash flow projections are subject to a number of assumptions and actual results could differ materially from these estimates. The Palco Debtors may not be able to meet the restrictive financial covenants specified in the DIP Facility, in which case they may not be able to continue operations and reorganize under Chapter 11 of the Bankruptcy Code.

Scopac has been authorized by the Bankruptcy Court to fund budgeted ongoing operating and bankruptcy-related costs using operating cash flow and, to the extent needed, funds available in the SAR Account (subject to no more than \$5.0 million in withdrawals from the SAR Account being outstanding at any given time). If these sources of liquidity are not adequate, and if Scopac is unable to obtain additional sources of liquidity and the necessary Bankruptcy Court approval to utilize such additional sources of liquidity, Scopac may not be able to continue operations and reorganize successfully under Chapter 11 of the Bankruptcy Code.

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

The following table contains information about the Company's purchases of shares of its Common Stock during the three months ended June 30, 2007.

Issuer Purchases of Equity Securities		
Period	Total Number of Shares Purchased ⁽¹⁾	Average Price Paid Per Share
April 1-30, 2007	1,100	\$ 30.05
May 1-31, 2007	—	\$ —
June 1-30, 2007	—	\$ —
Total	1,100	\$ 30.05

⁽¹⁾ All of such purchases were made on national exchanges. The Company currently has no publicly-announced plans or programs to repurchase shares of its Common Stock.

The Company may from time to time purchase additional shares of its Common Stock on national exchanges or in privately negotiated transactions.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

As a result of the commencement of the Bankruptcy Cases, the outstanding principal of and accrued interest on, the secured debt obligations of the Debtors, consisting of the Scopac Timber Notes, the Scopac Line of Credit, the Palco Term Loan and the Palco Revolving Credit Facility became immediately due and payable. However, claims against the Debtors for principal and accrued interest are stayed while the Debtors continue business operations as debtors-in-possession. See Note 1 for additional information regarding the effects of the commencement of the Bankruptcy Cases on the Debtors' debt obligations. Such information is incorporated herein by reference.

ITEM 4. SUBMISSION OF MATTER TO A VOTE OF SECURITY HOLDERS

The annual meeting of stockholders of the Company was held on May 30, 2007, at which meeting the stockholders reelected Messrs. Cruikshank, Rosenberg, Rosenthal and S. Hurwitz as directors of the Company. The results of the matters voted upon at the meeting are shown below.

Nominees for Director

The nominees for election as directors of the Company are listed below, together with voting information for each nominee. Messrs. Charles E. Hurwitz, J. Kent Friedman and Ezra G. Levin continued as directors of the Company.

Nominees for Election by Holders of Common Stock

Robert J. Cruikshank - 4,898,987 votes for, 54,027 votes withheld and -0- broker non-votes.
Stanley D. Rosenberg - 4,905,975 votes for, 47,039 votes withheld and -0- broker non-votes.
Michael J. Rosenthal - 4,903,215 votes for, 49,799 votes withheld and -0- broker non-votes.

Nominees for Election by Holders of Common Stock and Class A Preferred Stock

Shawn M. Hurwitz - 11,030,835 votes for, 250,955 votes withheld and -0- broker non-votes.

ITEM 6. EXHIBITS

a. Exhibits:

- * 31.1 Section 302 Certification of Chief Executive Officer
- * 31.2 Section 302 Certification of Chief Financial Officer
- * 32.1 Section 906 Certification of Chief Executive Officer
- * 32.2 Section 906 Certification of Chief Financial Officer
- * Included with this filing

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, who have signed this report on behalf of the Registrant and as the principal financial and accounting officers of the Registrant, respectively.

MAXXAM INC.

Date: August 9, 2007

By: /S/ M. EMILY MADISON
M. Emily Madison
Vice President, Finance and
Interim Chief Financial Officer
(Principal Accounting Officer and
Interim Principal Financial Officer)

Glossary of Defined Terms

Bankruptcy Cases: The Chapter 11 proceedings of the Debtors

Bankruptcy Code: The United States Bankruptcy Code

Bankruptcy Court: The United States Bankruptcy Court for the Southern District of Texas

Beltway Assets: Beltway Assets LLC, an indirect wholly owned subsidiary of the Company

Beltway Notes: The 6.08% notes of *Beltway Assets* due in November 2024

Britt: Britt Lumber Co., Inc., a wholly owned subsidiary of Palco

Cave action: An action entitled *Steve Cave, et al. v. Gary Clark, et al.* (No. DR020719) filed in the Superior Court of Humboldt County, California

CDF: California Department of Forestry and Fire Protection

Class A Preferred Stock: The Company's Class A \$0.05 Non-Cumulative Participating Convertible Preferred Stock

Common Stock: The Company's \$0.50 par value common stock

Company: MAXXAM Inc., including its majority and wholly owned subsidiaries, except as otherwise indicated

Cook action: An action entitled *Alan Cook, et al. v. Gary Clark, et al.* (No. DR020718) filed in the Superior Court of Humboldt County, California

Debtors: Palco, Scopac, Britt, SDLLC and Palco's other subsidiaries, all of which have filed for reorganization under the Bankruptcy Code

DIP Facility: The \$75.0 million revolving credit agreement dated as of August 6, 2007, among the *Palco Debtors*, as borrowers, and *Marathon*

ERISA: The Employee Retirement Income Security Act of 1974, as amended from time to time

Exclusivity Period: A period following the date of filing of Chapter 11 bankruptcy (generally 120 days, subject to extension by the bankruptcy court), during which the debtor generally has the exclusive right to propose a plan of reorganization

FASB: Financial Accounting Standards Board

FDIC: Federal Deposit Insurance Corporation

FDIC action: An action entitled *Federal Deposit Insurance Corporation, as manager of the FSLIC Resolution Fund v. Charles E. Hurwitz* (No. H-95-3956) filed by the FDIC on August 2, 1995 in the U.S. District Court for the Southern District of Texas

Filing Date: January 18, 2007, the date the Debtors filed separate voluntary petitions with the *Bankruptcy Court*

Form 10-K: Annual Report on Form 10-K of the Company for the fiscal year ended December 31, 2006

Fountain Hills: Fountain Hills, a master-planned residential community located in Fountain Hills, Arizona

GAAP: Generally accepted accounting principles in the United States

Herrera action: An action entitled *Gildardo and Lisa Herrera, individually and on behalf of their children v. Sam Houston Race Park, Ltd. and SHRP General Partners Inc.* (No. 2005-76898) filed in the state District Court of Harris County, Texas

Johnson action: An action entitled *Edyth Johnson, et al. v. Charles E. Hurwitz, an individual, MAXXAM Inc., et al.* (No. DR040720) filed in the Superior Court of Humboldt County, California

Lakepointe Assets: Lakepointe Assets Holdings LLC, an indirect wholly owned subsidiary of the Company

Lakepointe Notes: The 7.56% notes of Lakepointe Assets and its subsidiaries due in June 2021

Laredo LLC: Laredo Race Park LLC, a wholly owned subsidiary of the Company

Marathon: Marathon Structured Finance Fund L.P.

MAXXAM Parent: MAXXAM Inc., excluding its majority and wholly owned subsidiaries

MAXXAM Pension Plan: MAXXAM Parent's pension plan

MGHI: MAXXAM Group Holdings Inc., a wholly owned subsidiary of the Company

MGI: MAXXAM Group Inc., a wholly owned subsidiary of MGHI and Palco's parent

Mirada: The Company's luxury resort-residential project located in Rancho Mirage, California

Motel Assets: Motel Assets Holdings LLC, an indirect wholly owned subsidiary of the Company

Motel Notes: The 7.03% notes of Motel Assets and its subsidiaries due in May 2018

NJDEP: New Jersey Department of Environmental Protection

OTS: The United States Department of Treasury's Office of Thrift Supervision

OTS action: A formal administrative proceeding initiated by the OTS against the Company and others on December 26, 1995

Palco: The Pacific Lumber Company, a wholly owned subsidiary of MGI

Palco Debtors: Palco, Britt, SDLLC, Salmon Creek and Scotia Inn

Palco Revolving Credit Facility: The five-year \$60.0 million secured asset-based revolving credit facility evidenced by the Revolving Credit Agreement dated as of July 18, 2006, among Palco and Britt, as borrowers, and Marathon, as amended

Palco Term Loan: The five-year \$85.0 million secured term loan evidenced by the Term Loan Agreement dated as of July 18, 2006, among Palco and Britt, as borrowers, and Marathon, as amended

Palmas: Palmas del Mar, a master-planned residential community and resort located on the southeastern coast of Puerto Rico near Humacao

Palmas Notes: The 7.12% notes due December 20, 2030 of Palmas Country Club Inc., an indirect wholly owned subsidiary of the Company

PSLRA: Private Securities Litigation Reform Act of 1995

Racing Commission: The Texas Racing Commission

Respondents: Federated Development Company, a principal stockholder of the Company now known as Gideon Holdings, Inc., the Company, Mr. Charles E. Hurwitz, the Chairman of the Board and Chief Executive Officer of the Company, and the other respondents in the *OTS action*

Salmon Creek: Salmon Creek LLC, a wholly owned subsidiary of Palco

Sam Houston Race Park: Texas Class 1 horse racing facility in Houston, Texas owned and operated by SHRP, Ltd.

Sanctions Motion: An amended counterclaim and motion for sanctions filed by the Respondents on November 8, 2002, in connection with the *FDIC action*

SAR Account: Funds held in a reserve account titled the Scheduled Amortization Reserve Account, which was established to support principal payments on the Scopac Timber Notes

Scopac: Scotia Pacific Company LLC, a limited liability company wholly owned by Palco

Scopac Indenture: The indenture governing the Scopac Timber Notes

Scopac Line of Credit: The agreement between a group of lenders and Scopac pursuant to which Scopac may borrow in order to pay up to one year's interest on the Scopac Timber Notes

Scopac Timber: The timber in respect of the Scopac Timberlands and the Scopac Timber Rights

Scopac Timber Notes: Scopac's 6.55% Series B Class A-1 Timber Collateralized Notes, 7.11% Series B Class A-2 Timber Collateralized Notes and 7.71% Series B Class A-3 Timber Collateralized Notes due July 20, 2028

Scopac Timberlands: Approximately 200,000 acres of timberlands owned by Scopac

Scopac Timber Rights: Scopac's exclusive right to harvest on approximately 10,000 acres of timberlands owned by Palco and Salmon Creek

Scotia Inn: Scotia Inn Inc., a wholly owned subsidiary of Palco

SDLLC: Scotia Development LLC, a wholly owned subsidiary of Palco as of the *Filing Date*

SEC: The Securities and Exchange Commission

SFAS: Statement of Financial Accounting Standards

SHRP, Ltd.: Sam Houston Race Park, Ltd., a wholly owned subsidiary of the Company that owns and operates Sam Houston Race Park and Valley Race Park

Trustee: The trustee under the Scopac Indenture

USAT: United Savings Association of Texas

Valley Race Park: The Company's greyhound racing facility located in Harlingen, Texas

Wilson federal action: An action entitled *United States of America, ex rel. Richard Wilson and Chris Maranto v. MAXXAM Inc., et al.* (No. C 06 7497) filed in the U.S. District Court for the Northern District of California

Wilson state action: An action entitled *State of California ex rel. Richard Wilson and Chris Maranto v. MAXXAM Inc., et al.* (No. CGC 06 458528) filed in the Superior Court of San Francisco County, California

Wilson actions: The *Wilson federal action* and *Wilson state action*, collectively