

Sunstone Hotel Investors, Inc.
Form 10-Q
May 06, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2011

OR

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

For the transition period from to

Commission file number 001-32319

Sunstone Hotel Investors, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Maryland
(State or Other Jurisdiction of
Incorporation or Organization)

20-1296886
(I.R.S. Employer
Identification Number)

120 Vantis, Suite 350
Aliso Viejo, California
(Address of Principal Executive Offices)

92656
(Zip Code)

Registrant's telephone number, including area code: **(949) 330-4000**

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer
(Do not check if a smaller reporting company)

Smaller reporting company

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

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

118,183,239 shares of Common Stock, \$0.01 par value, as of May 1, 2011

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SUNSTONE HOTEL INVESTORS, INC.

QUARTERLY REPORT ON

FORM 10-Q

For the Quarterly Period Ended March 31, 2011

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Table of Contents**PART I FINANCIAL INFORMATION****Item 1. Financial Statements****SUNSTONE HOTEL INVESTORS, INC.****CONSOLIDATED BALANCE SHEETS***(In thousands, except share data)*

	March 31, 2011 (unaudited)	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents (\$1,889 and \$1,365 related to VIEs)	\$ 153,214	\$ 275,881
Restricted cash (\$2,469 and \$3,581 related to VIEs)	61,370	55,972
Accounts receivable, net (\$4,574 and \$1,885 related to VIEs)	29,784	18,173
Due from affiliates	17	44
Inventories (\$224 and \$159 related to VIEs)	2,674	2,568
Prepaid expenses	10,006	8,004
Investment in hotel property of discontinued operations, net	115,909	116,104
Other current assets of discontinued operations, net	3,426	2,635
Total current assets	376,400	479,381
Investment in hotel properties, net	2,361,863	1,918,119
Other real estate, net	12,109	12,012
Investments in unconsolidated joint ventures		246
Deferred financing fees, net	8,628	8,907
Interest rate derivative agreements	348	
Goodwill	13,088	4,673
Other assets, net (\$10 and \$3 related to VIEs)	37,723	12,768
Total assets	\$ 2,810,159	\$ 2,436,106
LIABILITIES AND EQUITY		
Current liabilities:		
Accounts payable and accrued expenses (\$887 and \$713 related to VIEs)	\$ 29,841	\$ 21,187
Accrued payroll and employee benefits (\$851 and \$1,123 related to VIEs)	13,713	12,674
Due to Third-Party Managers	7,855	7,852
Dividends payable	5,137	5,137
Other current liabilities (\$2,168 and \$1,439 related to VIEs)	24,187	17,212
Current portion of notes payable	288,699	16,486
Other current liabilities of discontinued operations, net	21,338	20,700
Total current liabilities	390,770	101,248
Notes payable, less current portion	1,163,654	1,126,817
Other liabilities (\$12 and \$30 related to VIEs)	9,517	8,742
Total liabilities	1,563,941	1,236,807

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Commitments and contingencies (*Note 13*)

Preferred stock, Series C Cumulative Convertible Redeemable Preferred Stock, \$0.01 par value, 4,102,564 shares authorized, issued and outstanding at March 31, 2011 and December 31, 2010, liquidation preference of \$24.375 per share	100,000	100,000
Equity:		
Stockholders' equity:		
Preferred stock, \$0.01 par value, 100,000,000 shares authorized. 8.0% Series A Cumulative Redeemable Preferred Stock, 7,050,000 shares issued and outstanding at March 31, 2011 and December 31, 2010, stated at liquidation preference of \$25.00 per share	176,250	176,250
Common stock, \$0.01 par value, 500,000,000 shares authorized, 117,166,822 shares issued and outstanding at March 31, 2011 and 116,950,504 shares issued and outstanding at December 31, 2010	1,172	1,170
Additional paid in capital	1,314,099	1,313,498
Retained earnings	80,928	29,593
Cumulative dividends	(423,212)	(418,075)
Accumulated other comprehensive loss	(3,137)	(3,137)
Total stockholders' equity	1,146,100	1,099,299
Non-controlling interest	118	
Total equity	1,146,218	1,099,299
Total liabilities and equity	\$ 2,810,159	\$ 2,436,106

The abbreviation VIEs above refers to Variable Interest Entities.

See accompanying notes to consolidated financial statements.

Table of Contents**SUNSTONE HOTEL INVESTORS, INC.****UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS***(In thousands, except per share data)*

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
REVENUES		
Room	\$ 107,833	\$ 90,378
Food and beverage	40,403	38,208
Other operating	14,339	12,313
Total revenues	162,575	140,899
OPERATING EXPENSES		
Room	29,445	24,207
Food and beverage	30,614	27,688
Other operating	6,834	6,738
Advertising and promotion	8,828	7,407
Repairs and maintenance	7,415	6,463
Utilities	6,968	5,829
Franchise costs	5,250	4,515
Property tax, ground lease and insurance	14,135	10,307
Property general and administrative	20,496	17,145
Corporate overhead	7,664	4,580
Depreciation and amortization	26,482	23,558
Total operating expenses	164,131	138,437
Operating income (loss)	(1,556)	2,462
Equity in net earnings of unconsolidated joint ventures	21	112
Interest and other income	72	171
Interest expense	(17,944)	(20,041)
Gain on remeasurement of equity interests	69,230	
Income (loss) from continuing operations	49,823	(17,296)
Income (loss) from discontinued operations	1,512	(3,795)
NET INCOME (LOSS)	51,335	(21,091)
Distributions to non-controlling interest	(7)	
Preferred stock dividends and accretion	(5,137)	(5,187)
Undistributed income allocated to unvested restricted stock compensation	(302)	
Undistributed income allocated to Series C preferred stock	(209)	
INCOME AVAILABLE (LOSS ATTRIBUTABLE) TO COMMON STOCKHOLDERS	\$ 45,680	\$ (26,278)
Basic per share amounts:		
Income (loss) from continuing operations available (attributable) to common stockholders	\$ 0.38	\$ (0.23)
Income (loss) from discontinued operations	0.01	(0.04)
Basic income available (loss attributable) to common stockholders per common share	\$ 0.39	\$ (0.27)
Diluted per share amounts:		
Income (loss) from continuing operations available (attributable) to common stockholders	\$ 0.38	\$ (0.23)

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Income (loss) from discontinued operations	0.01	(0.04)
Diluted income available (loss attributable) to common stockholders per common share	\$ 0.39	\$ (0.27)
Weighted average common shares outstanding:		
Basic	117,074	97,047
Diluted	117,211	97,047
Dividends declared per common share	\$	\$

See accompanying notes to consolidated financial statements.

Table of Contents**SUNSTONE HOTEL INVESTORS, INC.****CONSOLIDATED STATEMENT OF EQUITY***(In thousands, except share data)*

	Preferred Stock		Common Stock		Additional Paid in Capital	Retained Earnings	Cumulative Dividends	Accumulated Other Comprehensive Loss	Non- controlling Interest	Total
	Number of Shares	Amount	Number of Shares	Amount						
Balance at December 31, 2010	7,050,000	\$ 176,250	116,950,504	\$ 1,170	\$ 1,313,498	\$ 29,593	\$ (418,075)	\$ (3,137)		\$ 1,099,299
Vesting of restricted common stock (unaudited)			216,318	2	601					603
Non-controlling interest assumed at acquisition (unaudited)									125	125
Distributions to non-controlling interest (unaudited)									(7)	(7)
Series A preferred dividends and dividends payable at \$0.50 per share year to date (unaudited)							(3,525)			(3,525)
Series C preferred dividends and dividends payable at \$0.393 per share year to date (unaudited)							(1,612)			(1,612)
Net income and comprehensive income (unaudited)						51,335				51,335
Balance at March 31, 2011 (unaudited)	7,050,000	\$ 176,250	117,166,822	\$ 1,172	\$ 1,314,099	\$ 80,928	\$ (423,212)	\$ (3,137)	\$ 118	\$ 1,146,218

See accompanying notes to consolidated financial statements.

Table of Contents**SUNSTONE HOTEL INVESTORS, INC.****UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS***(In thousands)*

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	\$ 51,335	\$ (21,091)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Bad debt expense (recovery)	3	(40)
Gain on remeasurement of equity interests	(69,230)	
Loss on derivatives, net	44	
Depreciation	27,239	25,189
Amortization of franchise fees and other intangibles	1,613	186
Amortization and write-off of deferred financing fees	616	2,089
Amortization of loan discounts	261	246
Amortization of deferred stock compensation	544	962
Equity in net earnings of unconsolidated joint ventures	(21)	(112)
Changes in operating assets and liabilities:		
Restricted cash	11,938	(7,353)
Accounts receivable	(5,892)	(4,674)
Due from affiliates	27	1
Inventories	(4)	51
Prepaid expenses and other assets	1,408	129
Accounts payable and other liabilities	6,310	11,446
Accrued payroll and employee benefits	(2,153)	(1,517)
Due to Third-Party Managers	3	(108)
Discontinued operations	(688)	(6,920)
Net cash provided by (used in) operating activities	23,353	(1,516)
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of hotel properties and other assets	42	
Restricted cash replacement reserve	(2,422)	2,291
Acquisitions of hotel properties and other assets	(102,159)	(4,000)
Renovations and additions to hotel properties and other real estate	(32,606)	(8,625)
Net cash used in investing activities	(137,145)	(10,334)
CASH FLOWS FROM FINANCING ACTIVITIES		
Payments on notes payable	(3,394)	(2,745)
Payments of deferred financing costs	(337)	(4)
Dividends paid	(5,137)	(5,137)
Distributions to non-controlling interest	(7)	
Net cash used in financing activities	(8,875)	(7,886)
Net decrease in cash and cash equivalents	(122,667)	(19,736)
Cash and cash equivalents, beginning of period	275,881	353,255
Cash and cash equivalents, end of period	\$ 153,214	\$ 333,519
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid for interest	\$ 16,469	\$ 16,902

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NONCASH INVESTING ACTIVITY

Deconsolidation of assets of hotel placed into receivership	\$	\$	18,393
Deconsolidation of liabilities of hotel placed into receivership	\$	\$	26,876
Amortization of deferred stock compensation construction activities	\$	57	\$ 42
Amortization of deferred stock compensation unconsolidated joint venture	\$	2	\$ 10

NONCASH FINANCING ACTIVITY

Assumption of debt in connection with acquisitions of hotel properties	\$	312,183	\$
Dividends payable	\$	5,137	\$ 5,137

See accompanying notes to consolidated financial statements.

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SUNSTONE HOTEL INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Description of Business

Sunstone Hotel Investors, Inc. (the Company) was incorporated in Maryland on June 28, 2004 in anticipation of an initial public offering of common stock, which was consummated on October 26, 2004. The Company, through its 100% controlling interest in Sunstone Hotel Partnership, LLC (the Operating Partnership), of which the Company is the sole managing member, and the subsidiaries of the Operating Partnership, including Sunstone Hotel TRS Lessee, Inc. (the TRS Lessee) and its subsidiaries, is currently engaged in acquiring, owning, asset managing and renovating hotel properties. The Company may also sell certain hotel properties from time to time. The Company operates as a real estate investment trust (REIT) for federal income tax purposes.

As a REIT, certain tax laws limit the amount of non-qualifying income the Company can earn, including income derived directly from the operation of hotels. As a result, the Company leases all of its hotels to its TRS Lessee, which in turn enters into long-term management agreements with third parties to manage the operations of the Company's hotels. As of March 31, 2011, the Company owned 33 hotels, including the Royal Palm Miami Beach, which was classified as held for sale as of March 31, 2011 and included in discontinued operations due to its sale in April 2011, leaving 32 hotels (the 32 hotels) held for investment. The Company's third-party managers included a subsidiary of Interstate Hotels & Resorts, Inc., manager of 13 of the Company's 32 hotels; subsidiaries of Marriott International, Inc. or Marriott Hotel Services, Inc. (collectively, Marriott), managers of 13 of the Company's 32 hotels; and Davidson Hotel Company, Fairmont Hotels & Resorts (U.S.), Highgate Hotels, Hilton Worldwide, Hyatt Corporation and Sage Hospitality Resources, each managers of one of the Company's 32 hotels. In addition, as of January 2011, the Company owns 100% of BuyEfficient, LLC (BuyEfficient), an electronic purchasing platform that allows members to procure food, operating supplies, furniture, fixtures and equipment.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements as of March 31, 2011 and December 31, 2010, and for the three months ended March 31, 2011 and 2010, include the accounts of the Company, the Operating Partnership, the TRS Lessee and their subsidiaries. All significant intercompany balances and transactions have been eliminated.

The accompanying interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and in conformity with the rules and regulations of the Securities and Exchange Commission. In the Company's opinion, the interim financial statements presented herein reflect all adjustments, consisting solely of normal and recurring adjustments, which are necessary to fairly present the interim financial statements. These financial statements should be read in conjunction with the financial statements included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2010, filed with the Securities and Exchange Commission on February 17, 2011.

Certain prior year amounts have been reclassified in the consolidated financial statements in order to conform to the current year presentation.

The Company has evaluated subsequent events through the date of issuance of these financial statements.

Use of Estimates

The preparation of consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ materially from those estimates.

Reporting Periods

The results the Company reports in its consolidated statements of operations are based on results reported to the Company by its hotel managers. These hotel managers use different reporting periods. Marriott uses a fiscal year ending on the Friday closest to December 31 and reports twelve weeks of operations each for the first three quarters of the year, and sixteen or seventeen weeks of operations for the fourth quarter of the year. The Company's other hotel managers report operations on a standard monthly calendar. The Company has elected to adopt quarterly close periods of March 31, June 30 and September 30, and an annual year end of December 31. As a result, the Company's 2011 results of operations for the

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Marriott-managed hotels include results from January 1 through March 25 for the first quarter, March 26 through June 17 for the second quarter, June 18 through September 9 for the third quarter, and September 10 through December 30 for the fourth quarter. The Company's 2010 results of operations for the Marriott-managed hotels include results from January 2 through March 26 for the first quarter, March 27 through June 18 for the second quarter, June 19 through September 10 for the third quarter, and September 11 through December 31 for the fourth quarter.

Fair Value of Financial Instruments

As of March 31, 2011 and December 31, 2010, the carrying amount of certain financial instruments, including cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued expenses were representative of their fair values due to the short-term maturity of these instruments.

The Company follows the requirements of the Fair Value Measurements and Disclosure Topic of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC), which establishes a framework for measuring fair value and disclosing fair value measurements by establishing a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy are described below:

- Level 1 Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.
- Level 2 Inputs reflect quoted prices for identical assets or liabilities in markets that are not active; quoted prices for similar assets or liabilities in active markets; inputs other than quoted prices that are observable for the asset or the liability; or inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3 Unobservable inputs reflecting the Company's own assumptions incorporated in valuation techniques used to determine fair value. These assumptions are required to be consistent with market participant assumptions that are reasonably available.

As discussed in Note 9, the Company entered into interest rate protection agreements to manage, or hedge, interest rate risks in conjunction with its acquisitions of the outside 62% equity interests in the Doubletree Guest Suites Times Square and the JW Marriott New Orleans during the first quarter of 2011. The Company records interest rate protection agreements on the balance sheet at their fair value. Changes in the fair value of derivatives are recorded each period in the consolidated statements of operations as they are not designated as hedges. In accordance with the Fair Value Measurements and Disclosure Topic of the FASB ASC, the Company estimates the fair value of its interest rate protection agreements based on quotes obtained from the counterparties, which are based upon the consideration that would be required to terminate the agreements. The Company has valued these derivative contracts using Level 2 measurements at \$0.3 million as of March 31, 2011.

The Company currently pays the premiums for a \$5,000,000 split life insurance policy for its former Chief Executive Officer and current Executive Chairman, Robert A. Alter. The Company has valued this policy using Level 2 measurements at \$1.9 million as of both March 31, 2011 and December 31, 2010. These amounts are included in other assets, net in the accompanying consolidated balance sheets.

The Company also has a Retirement Benefit Agreement with Mr. Alter. The Company has valued this agreement using Level 2 measurements at \$1.9 million as of both March 31, 2011 and December 31, 2010. These amounts are included in accrued payroll and employee benefits in the

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accompanying consolidated balance sheets.

On an annual basis and periodically when indicators of impairment exist, the Company has analyzed the carrying values of its hotel properties using Level 3 measurements, including a discounted cash flow analysis to estimate the fair value of its hotel properties taking into account each property's expected cash flow from operations, holding period and estimated proceeds from the disposition of the property. The factors addressed in determining estimated proceeds from disposition included anticipated operating cash flow in the year of disposition and terminal capitalization rate. For the three months ended March 31, 2011 and 2010, the Company did not identify any properties with indicators of impairment.

The Company also analyzes the carrying value of its goodwill using Level 3 measurements including a discounted cash flow analysis to estimate the fair value of its reporting units. For the three months ended March 31, 2011 and 2010, the Company did not identify any goodwill with indicators of impairment.

As of March 31, 2011 and December 31, 2010, 81.4% and 100%, respectively, of the Company's outstanding debt had fixed interest rates, including the effect of an interest rate swap agreement. The Company's carrying value of its debt totaled \$1.5 billion and \$1.1 billion as of March 31, 2011 and December 31, 2010, respectively. Using Level 3 measurements, including the Company's weighted average cost of capital ranging between 6.0% and 9.6%, the Company estimates that the fair market value of its debt as of March 31, 2011 and December 31, 2010 totaled \$1.4 billion and \$1.1 billion, respectively.

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The following tables present our assets and liabilities measured at fair value on a recurring and non-recurring basis at March 31, 2011 and December 31, 2010 (in thousands):

	Fair Value Measurements at Reporting Date			
	Total March 31, 2011 (unaudited)	Level 1 (unaudited)	Level 2 (unaudited)	Level 3 (unaudited)
Assets:				
Interest rate derivative agreements	\$ 348	\$	\$ 348	\$
Life insurance policy	1,934		1,934	
Goodwill	13,088			13,088
Total assets	\$ 15,370	\$	\$ 2,282	\$ 13,088
Liabilities:				
Retirement benefit agreement	\$ 1,934	\$	\$ 1,934	\$
Total liabilities	\$ 1,934	\$	\$ 1,934	\$

	Fair Value Measurements at Reporting Date			
	Total December 31, 2010	Level 1	Level 2	Level 3
Assets:				
Other real estate, net (1)	\$ 2,506	\$	\$	\$ 2,506
Life insurance policy	1,868		1,868	
Goodwill	4,673			4,673
Total assets	\$ 9,047	\$	\$ 1,868	\$ 7,179
Liabilities:				
Retirement benefit agreement	\$ 1,868	\$	\$ 1,868	\$
Total liabilities	\$ 1,868	\$	\$ 1,868	\$

(1) Includes the office building and land adjacent to one of the Company's hotels that was impaired and recorded at fair value in June 2010.

The following table presents the goodwill account balance rollforward from the prior period, as well as the activity recorded for assets measured at fair value on a non-recurring basis using Level 3 inputs during the reporting period (in thousands):

	Goodwill	
Balance at December 31, 2010	\$	4,673
Purchase of outside 50% equity interest in BuyEfficient (unaudited)		8,415
Balance at March 31, 2011 (unaudited)	\$	13,088

The following table presents the gains included in earnings as a result of applying Level 3 measurements for the three months ended March 31, 2011 and 2010 (in thousands):

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	Three Months Ended March 31, 2011 (unaudited)		Three Months Ended March 31, 2010 (unaudited)	
Investment in unconsolidated joint ventures (1)	\$	69,230	\$	
Total Level 3 measurement gains included in earnings	\$	69,230	\$	

(1) Includes the gains recorded by the Company on the remeasurements of the Company's equity interests in its Doubletree Guest Suites Times Square and BuyEfficient joint ventures.

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Accounts Receivable

Accounts receivable primarily represents receivables from hotel guests who occupy hotel rooms and utilize hotel services. Accounts receivable also includes, among other things, receivables from customers who utilize the Company's commercial laundry facilities in Salt Lake City, Utah, and Rochester, Minnesota, receivables from vendors who offer purchase volume rebates to BuyEfficient, as well as tenants who lease space in the Company's hotels. The Company maintains an allowance for doubtful accounts sufficient to cover potential credit losses. The Company's accounts receivable at both March 31, 2011 and December 31, 2010 includes an allowance for doubtful accounts of \$0.1 million.

Goodwill

The Company follows the requirements of the Intangibles—Goodwill and Other Topic of the FASB ASC, which states that goodwill and intangible assets deemed to have indefinite lives are subject to annual impairment tests. As a result, the carrying value of goodwill allocated to the hotel properties and other assets is reviewed at least annually for impairment. In addition, when facts and circumstances suggest that the Company's goodwill may be impaired, an interim evaluation of goodwill is prepared. Such review entails comparing the carrying value of the individual hotel property or other asset (the reporting unit) including the allocated goodwill to the fair value determined for that reporting unit (see Fair Value of Financial Instruments for detail on the Company's valuation methodology). If the aggregate carrying value of the reporting unit exceeds the fair value, the goodwill of the reporting unit is impaired to the extent of the difference between the fair value and the aggregate carrying value, not to exceed the carrying amount of the allocated goodwill. The Company's annual impairment evaluation is performed each year as of December 31.

During the first quarter ended March 31, 2011, the Company recorded additional goodwill of \$8.4 million related to its purchase of the outside 50% equity interest in its BuyEfficient joint venture.

Deferred Financing Fees

Deferred financing fees consist of loan fees and other financing costs related to the Company's outstanding indebtedness and are amortized to interest expense over the terms of the related debt. Upon repayment or refinancing of the underlying debt, any related unamortized deferred financing fee is charged to interest expense. Upon any loan modification, any related unamortized deferred financing fee is amortized over the remaining terms of the modified loan.

During the three months ended March 31, 2011 and 2010, approximately \$0.3 million and \$4,000, respectively were incurred and paid related to new debt and debt refinancings.

Total amortization and write-off of deferred financing fees for the three months ended March 31, 2011 and 2010 was as follows (in thousands):

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	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Continuing operations:		
Amortization of deferred financing fees	\$ 616	\$ 493
Write-off of deferred financing fees (1)		1,462
Total deferred financing fees - continuing operations	616	1,955
Discontinued operations:		
Amortization of deferred financing fees		134
Total amortization and write-off of deferred financing fees	\$ 616	\$ 2,089

(1) Includes unamortized deferred financing costs written off by the Company and charged to interest expense due to the termination of its credit facility during the first quarter of 2010.

Earnings Per Share

The Company applies the two-class method when computing its earnings per share as required by the Earnings Per Share Topic of the FASB ASC, which requires the net income per share for each class of stock (common stock and convertible preferred stock) to be calculated assuming 100% of the Company's net income is distributed as dividends to each class of stock based on their contractual rights. To the extent the Company has undistributed earnings in any calendar quarter, the Company will follow the two-class method of computing earnings per share.

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The Company follows the requirements of ASC 260-10, which states that unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. For the three months ended March 31, 2011 and 2010, undistributed earnings representing nonforfeitable dividends of \$0.3 million and zero, respectively, were allocated to the participating securities.

In accordance with the Earnings Per Share Topic of the FASB ASC, basic earnings available (loss attributable) to common stockholders per common share is computed based on the weighted average number of shares of common stock outstanding during each period. Diluted earnings available (loss attributable) to common stockholders per common share is computed based on the weighted average number of shares of common stock outstanding during each period, plus potential common shares considered outstanding during the period, as long as the inclusion of such awards is not anti-dilutive. Potential common shares consist of unvested restricted stock awards (using the treasury stock method), the incremental common shares issuable upon the exercise of stock options (using the treasury stock method) and the conversion of the Company's Series C Cumulative Convertible Redeemable Preferred Stock (Series C preferred stock).

The following table sets forth the computation of basic and diluted earnings (loss) per common share (in thousands, except per share data):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Numerator:		
Net income (loss)	\$ 51,335	\$ (21,091)
Less distributions to non-controlling interest	(7)	
Less preferred stock dividends and accretion	(5,137)	(5,187)
Undistributed income allocated to unvested restricted stock compensation	(302)	
Undistributed income allocated to Series C preferred stock	(209)	
Numerator for basic and diluted earnings available (loss attributable) to common stockholders	\$ 45,680	\$ (26,278)
Denominator:		
Weighted average basic common shares outstanding	117,074	97,047
Unvested restricted stock awards	137	
Weighted average diluted common shares outstanding	117,211	97,047
Basic earnings available (loss attributable) to common stockholders per common share	\$ 0.39	\$ (0.27)
Diluted earnings available (loss attributable) to common stockholders per common share	\$ 0.39	\$ (0.27)

The Company's shares of Series C preferred stock issuable upon conversion and shares associated with common stock options have been excluded from the above calculation of earnings (loss) per share for the three months ended March 31, 2011 and 2010, as their inclusion would have been anti-dilutive. The Company's unvested restricted shares associated with its long-term incentive plan have been excluded from the above calculation of loss per share for the three months ended March 31, 2010 as their inclusion would have been anti-dilutive.

Segment Reporting

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The Company reports its consolidated financial statements in accordance with the Segment Reporting Topic of the FASB ASC. Currently, the Company operates in one segment, operations held for investment. Previously, the Company operated in an additional segment, operations held for non-sale disposition. As a result of deed backs and title transfers, the Company has disposed of all assets and liabilities from its operations held for non-sale disposition segment. Accordingly, all assets, liabilities and the operations from its non-sale disposition segment have been reclassified to discontinued operations.

Table of Contents**3. Investment in Hotel Properties**

Investment in hotel properties, net consisted of the following (in thousands):

	March 31, 2011 (unaudited)	December 31, 2010
Land	\$ 266,914	\$ 239,564
Buildings and improvements	2,175,430	1,884,602
Furniture, fixtures and equipment	295,691	256,421
Intangibles	142,821	34,081
Franchise fees	1,031	983
Construction in process	42,696	38,253
	2,924,583	2,453,904
Accumulated depreciation and amortization	(562,720)	(535,785)
	\$ 2,361,863	\$ 1,918,119

In January 2011, the Company purchased the outside 62% equity interests in its Doubletree Guest Suites Times Square joint venture for \$37.5 million, and, as a result, became the sole owner of the entity that owns the 460-room Doubletree Guest Suites Times Square hotel located in New York City, New York. The hotel is encumbered by \$270.0 million of non-recourse senior mortgage and mezzanine debt that matures in January 2012, and bears a blended interest rate of LIBOR plus 115 basis points. The Company expects to refinance this debt in 2011, and intends to fund any refinancing shortfall with existing cash. The hotel is encumbered by an additional \$30.0 million mezzanine loan that is owned by the Company, and, therefore, eliminated in consolidation on the Company's March 31, 2011 balance sheet. The Company recorded the acquisition at fair value using an independent third-party analysis, with the purchase price allocated to investment in hotel properties, notes payable and hotel working capital assets and liabilities. The Company recognized acquisition-related costs of \$2.3 million during the three months ended March 31, 2011, which are included in corporate overhead on the Company's statement of operations. The results of operations for the Doubletree Guest Suites Times Square have been included in the Company's statement of operations from the acquisition date of January 14, 2011 through the first quarter ended March 31, 2011. Preferred dividends earned by investors from an entity that owns the Doubletree Guest Suites Times Square, less administrative fees, totaled \$7,000 during the quarter ended March 31, 2011, and are included in distributions to non-controlling interest on the Company's statement of operations.

In February 2011, the Company purchased the 494-room JW Marriott New Orleans located in New Orleans, Louisiana for approximately \$51.6 million in cash and the assumption of a \$42.2 million floating-rate, non-recourse senior mortgage. The mortgage, which matures in September 2015, has been swapped to a fixed rate of 5.45%, and is subject to a 25-year amortization schedule. The Company recorded the acquisition at fair value using an independent third-party analysis, with the purchase price allocated to investment in hotel properties, notes payable and hotel working capital assets. The Company recognized acquisition-related costs of \$0.4 million during the three months ended March 31, 2011, which are included in corporate overhead on the Company's statement of operations. The results of operations for the JW Marriott New Orleans have been included in the Company's statement of operations from the acquisition date of February 15, 2011 through the end of Marriott's first quarter March 25, 2011.

The fair values of the assets acquired and liabilities assumed at the dates of acquisition for the Doubletree Guest Suites Times Square and the JW Marriott New Orleans were consistent with the purchase prices of these two hotels and were allocated based on independent third-party analyses. The following table summarizes the fair values of assets acquired and liabilities assumed in these two acquisitions (in thousands):

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Assets:		
Investment in hotel properties (1)	\$	434,990
Cash		12,958
Restricted cash		14,914
Accounts receivable		4,957
Other assets		5,367
Total assets acquired		473,186
Liabilities:		
Notes payable		312,183
Accounts payable and other current liabilities		11,310
Total liabilities acquired		323,493
Non-controlling interest		125
Gain on remeasurement of equity interests (2)		60,501
Total cash paid for acquisitions	\$	89,067

(1) Investment in hotel properties was allocated to land (\$27.4 million), buildings and improvements (\$275.1 million), furniture, fixtures and equipment (\$23.8 million) and intangibles (\$108.7 million).

(2) Gain on remeasurement of equity interests includes a gain of \$30.1 million recognized on the remeasurement of the Company's equity interest in its Doubletree Guest Suites Times Square joint venture to its fair market value, and a gain of \$30.4 million recognized on the remeasurement of the Company's investment in a \$30.0 million, 8.5% mezzanine loan secured by the Doubletree Guest Suites Times Square to its fair market value in connection with the Company's purchase of the outside 62% equity interests in the Doubletree Guest Suites Times Square joint venture.

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Acquired properties are included in the Company's results of operations from the date of acquisition. The following unaudited pro forma results of operations reflect the Company's results as if the acquisitions of the Doubletree Guest Suites Times Square in January 2011 and the JW Marriott New Orleans in February 2011 both occurred on January 1, 2010. In the Company's opinion, all significant adjustments necessary to reflect the effects of the acquisitions have been made (in thousands, except per share data):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Revenues	\$ 167,412	\$ 158,223
Income available (loss attributable) to common stockholders from continuing operations	\$ 49,545	\$ (18,950)
Income (loss) per diluted share available (attributable) to common stockholders from continuing operations	\$ 0.42	\$ (0.25)

4. Discontinued Operations

The Company has classified the Royal Palm Miami Beach as held for sale as of March 31, 2011, reclassifying the hotel's assets and liabilities on its March 31, 2011 and December 31, 2010 balance sheets as held for sale, and the hotel's results of operations for the three months ended March 31, 2011, to discontinued operations. As the hotel was purchased by the Company in August 2010, no results of operations for the Royal Palm Miami Beach are included in the Company's statement of operations for the three months ended March 31, 2010. The Royal Palm Miami Beach was sold in April 2011 for \$130.0 million, subject to \$90.0 million of seller financing.

In 2009, pursuant to a secured debt restructuring program, the Company elected to cease the subsidization of debt service on four loans secured by 11 of its hotels: W San Diego, Renaissance Westchester, Marriott Ontario Airport, and the Mass Mutual eight (Renaissance Atlanta Concourse, Hilton Huntington, Residence Inn by Marriott Manhattan Beach, Marriott Provo, Courtyard by Marriott San Diego (Old Town), Holiday Inn Downtown San Diego, Holiday Inn Express San Diego (Old Town), and Marriott Salt Lake City (University Park)). In December 2009, the Company transferred possession and control of the Renaissance Westchester to a court-appointed receiver. In June 2010, the Company reacquired the Renaissance Westchester, and the \$29.2 million non-recourse mortgage secured by the hotel was cancelled. The Company recorded a gain on extinguishment of debt of \$6.7 million to discontinued operations in June 2010. In July 2010, the Company completed the deed back of the W San Diego, and title to the hotel was transferred to the lender. The Company recorded a gain on extinguishment of debt of \$35.4 million to discontinued operations in July 2010, and removed the hotel's net assets and liabilities from its 2010 balance sheet. In August 2010, the Marriott Ontario Airport was sold by the receiver, and title to the hotel was transferred to the new owner. In connection with this sale, the Company recorded a \$5.1 million gain on extinguishment of debt to discontinued operations in August 2010, and removed the net assets and liabilities from its 2010 balance sheet. In November 2010, the Company completed the deed back of the Mass Mutual eight hotels, and titles to the hotels were transferred to the lender. In connection with such transfer, Mass Mutual delivered to the Company a covenant and agreement pursuant to which Mass Mutual agreed to not sue the Company for any matter or claim which Mass Mutual may ever have relating to the hotels, the loan or the loan documents. There are certain customary carveouts from this covenant not to sue, including fraud, a breach of the deed in lieu agreement itself and the environmental indemnity agreement delivered at the time the loan was originated. Additionally, the Company made certain customary representations and warranties, all of which survive the closing for a period of six months. Five of the Mass Mutual eight hotels remain subject to franchise agreements which contain corporate guaranties. If the franchise agreements on these five hotels were to be terminated, the Company may be liable for up to \$19.6 million in termination fees. The Company recorded a gain on extinguishment of debt of \$39.0 million to discontinued operations in the fourth quarter of 2010, and the net assets and liabilities were removed from its 2010 balance sheet. Additional gain of \$19.6 million will be deferred until all significant contingencies are resolved. The Company expects the franchise agreements on these five hotels to be finalized during the second quarter of 2011, and to record any necessary adjustments to its liability for the termination fees in its statement of operations for the three months ended June 30, 2011, however, resolution may not be achieved until the second half of 2011.

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The following sets forth the discontinued operations for the three months ended March 31, 2011 and 2010, related to the Royal Palm Miami Beach and to the 11 hotel properties deeded back to lenders or sold by the receiver during 2010 (in thousands):

	Three Months Ended		Three Months Ended	
	March 31, 2011		March 31, 2010	
	(unaudited)		(unaudited)	
Operating revenues	\$	6,918	\$	21,676
Operating expenses		(3,973)		(17,968)
Interest expense				(5,686)
Depreciation and amortization expense		(1,433)		(1,817)
Income (loss) from discontinued operations	\$	1,512	\$	(3,795)

5. Other Real Estate

Other real estate, net consisted of the following (in thousands):

	March 31,		December 31,	
	2011		2010	
	(unaudited)			
Land	\$	2,768	\$	2,768
Buildings and improvements		9,297		9,297
Furniture, fixtures and equipment		6,796		6,687
Construction in process		310		116
		19,171		18,868
Accumulated depreciation		(7,250)		(7,044)
		11,921		11,824
Land held for investment		188		188
	\$	12,109	\$	12,012

As of March 31, 2011, other real estate, net included the Company's two commercial laundry facilities, an office building and one vacant parcel of land.

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6. Investments in Unconsolidated Joint Ventures

In December 2006, the Company entered into a joint venture agreement to obtain a 38% interest in the 460-room Doubletree Guest Suites Times Square in New York City, New York. The Company accounted for its ownership interest in the hotel using the equity method, and its accounting policies were consistent with those of the unconsolidated joint venture. In January 2011, the Company purchased the outside 62% equity interests in its Doubletree Guest Suites Times Square joint venture for \$37.5 million, and, as a result, became the sole owner of the entity that owns the hotel. In conjunction with this purchase, the Company recognized a gain of \$30.1 million on the remeasurement of the Company's equity interest in this joint venture to its fair market value, and a gain of \$30.4 million on the remeasurement of the Company's investment in a \$30.0 million, 8.5% mezzanine loan secured by the hotel which it purchased in April 2010 for \$3.45 million to its fair market value. Subsequent to this acquisition, the Company consolidates the results of operations of the Doubletree Guest Suites Times Square with its continuing operations.

In December 2007, the Company entered into a joint venture agreement with Strategic Hotels & Resorts, Inc. (Strategic) to own and operate BuyEfficient. Under the terms of the agreement, Strategic acquired a 50% interest in BuyEfficient from the Company. The Company accounted for its ownership interest in BuyEfficient using the equity method, and its accounting policies were consistent with those of the unconsolidated joint venture. In January 2011, the Company repurchased Strategic's 50% share in BuyEfficient for \$9.0 million. In conjunction with this purchase, the Company recognized a gain of \$8.7 million on the remeasurement of the Company's equity interest in this joint venture to its fair market value. Subsequent to this acquisition, the Company is now the sole owner of BuyEfficient, and consolidates BuyEfficient's results of operations with its continuing operations.

7. Interest Rate Derivative Agreements

At March 31, 2011, the Company held one interest rate cap agreement and one interest rate swap agreement to manage its exposure to the interest rate risks related to its floating rate debt. The interest rate cap agreement was acquired in connection with the Company's purchase of the outside 62% equity interests in the Doubletree Guest Suites Times Square as the purchase included the assumption of \$270.0 million of non-recourse senior mortgage and mezzanine debt with a blended interest rate of LIBOR plus 115 basis points. The Company valued this interest rate cap agreement at \$0.1 million at the acquisition date. The notional amount of the related debt totaled \$270.0 million at March 31, 2011. The interest rate cap strike rates range from 3.3208% to 4.49%, and the maturity date is in January 2012. The interest rate swap agreement was acquired in connection with the Company's purchase of the JW Marriott New Orleans, which included the assumption of \$42.2 million of floating rate debt which was swapped to a fixed rate of 5.45%. The Company valued this interest rate swap agreement at \$0.3 million at the acquisition date. The notional amount of the related debt totaled \$42.1 million as of March 31, 2011. The interest rate swap agreement caps the LIBOR interest rate on the underlying debt at a total interest rate of 5.45%, and the maturity date is in September 2015. None of the interest rate derivative agreements qualify for effective hedge accounting treatment. Accordingly, changes in the fair value of the Company's interest rate derivative agreements resulted in a net loss of \$44,000 which has been reflected as an increase in interest expense for the three months ended March 31, 2011. The fair values of the interest rate derivative agreements totaled \$0.3 million at March 31, 2011.

8. Other Assets

Other assets, net consisted of the following (in thousands):

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	March 31, 2011 (unaudited)	December 31, 2010
Deposits on potential acquisitions	\$ 18,000	\$
Property and equipment, net	1,857	1,758
Intangibles, net	8,927	
Notes receivable	500	3,950
Other receivables	5,378	4,403
Other	3,061	2,657
	\$ 37,723	\$ 12,768

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In March 2011, the Company paid a deposit of \$13.0 million towards its acquisition of the Hilton San Diego Bayfront, which the Company completed in April 2011. In addition, the Company paid a \$5.0 million refundable deposit on a potential hotel acquisition.

Due to the purchase of the outside 50% equity interest in its BuyEfficient joint venture (see Footnote 6), the Company's other assets, net as of March 31, 2011, includes BuyEfficient's intangible assets totaling \$9.0 million related to certain trademarks, customer and supplier relationships and internally developed software. These intangibles are amortized using the straight-line method over the remaining useful lives of between seven to 20 years. Accumulated amortization totaled \$0.1 million at March 31, 2011, and amortization expense totaled \$0.1 million for the three months ended March 31, 2011.

In April 2010, the Company purchased two hotel loans with a combined principal amount of \$32.5 million for a total purchase price of \$3.7 million. The loans included (i) a \$30.0 million, 8.5% mezzanine loan maturing in January 2017 secured by the equity interests in the Company's Doubletree Guest Suites Times Square joint venture (see Footnote 6), and (ii) one-half of a \$5.0 million, 8.075% subordinate note maturing in November 2010 secured by the 101-room boutique hotel known as Twelve Atlantic Station in Atlanta, Georgia. The Company purchased the mezzanine loan for \$3.45 million and the subordinate note for \$250,000. In November 2010, the Company purchased the remaining half of the Twelve Atlantic Station subordinate note for an additional \$250,000. In November 2010, the subordinate note was modified to provide for monthly interest only payments of 3.5%, with the remaining interest due at maturity, and the maturity date was extended to November 2012. As the subordinate note was in default, the borrower was required to bring the subordinate note current. As of March 31, 2011, the subordinate note secured by the Twelve Atlantic Station was not in default, however, the Company is accounting for the Twelve Atlantic Station loan using the cost recovery method until such time as the expected cash flows from the loan are reasonably probable and estimable. No amounts were received for the subordinate note during the first quarter of 2011 as payments on the note are currently being accumulated by the loan servicer. In January 2011, the Company purchased the outside 62% equity interests in the Doubletree Guest Suites Times Square joint venture for \$37.5 million and, as a result, became the sole owner of the entity that owns the hotel. In conjunction with this purchase, the Company recognized a gain of \$30.1 million on the remeasurement of its investment in the mezzanine loan to its fair market value. After this acquisition, the mezzanine loan is eliminated in consolidation on the Company's March 31, 2011 balance sheet.

9. Notes Payable

Notes payable consisted of the following (in thousands):

	March 31, 2011 (unaudited)	December 31, 2010
Notes payable requiring payments of interest and principal, with fixed rates ranging from 4.97% to 9.88%, including the effect of an interest rate swap; maturing at dates ranging from July 2012 through May 2021. The notes are collateralized by first deeds of trust on 20 hotel properties and one laundry facility at March 31, 2011, and 19 hotel properties and one laundry facility at December 31, 2010.	\$ 1,121,788	\$ 1,083,000
Notes payable requiring payments of interest only bearing a blended rate of LIBOR plus 115 basis points; maturing in January 2012. The notes are collateralized by first deeds of trust on one hotel property.	270,000	
Senior Notes, with a fixed interest rate of 4.60%, maturing in July 2027. The notes, subject to specified events and other conditions, are exchangeable into, at the Company's option, cash, the Company's common stock, or a combination of cash and the Company's common stock. The notes are guaranteed by the Company and certain of its subsidiaries.	62,500	62,500

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	1,454,288	1,145,500
Less: discount on Senior Notes	(1,935)	(2,197)
	1,452,353	1,143,303
Less: current portion	(288,699)	(16,486)
	\$ 1,163,654	\$ 1,126,817

In January 2011, the Company purchased the outside 62% equity interests in its Doubletree Guest Suites Times Square joint venture for \$37.5 million and, as a result, became the sole owner of the entity that owns the 460-room Doubletree Guest Suites Times Square hotel located in New York City. The hotel is encumbered by \$270.0 million of non-recourse senior mortgage and mezzanine debt that matures in January 2012, and bears a blended interest rate of LIBOR plus 115 basis points. The Company expects to refinance this debt in 2011, and intends to fund any refinancing shortfall with existing cash. The hotel is encumbered by an additional \$30.0 million mezzanine loan that is owned by the Company, and, therefore, eliminated in consolidation on the Company's March 31, 2011 balance sheet.

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In February 2011, the Company purchased the 494-room JW Marriott New Orleans for approximately \$93.8 million. The acquisition included the assumption of a \$42.2 million floating-rate, non-recourse senior mortgage. The mortgage, which matures in September 2015, has been swapped to a fixed rate of 5.45%, and is subject to a 25-year amortization schedule.

Total interest incurred and expensed on the notes payable was as follows (in thousands):

	Three Months Ended		Three Months Ended	
	March 31, 2011		March 31, 2010	
	(unaudited)		(unaudited)	
Interest expense	\$	17,023	\$	16,938
Interest expense - default rate (1)				764
Loss on derivatives, net		44		
Accretion of Senior Notes		261		246
Amortization of deferred financing fees		616		493
Write-off of deferred financing fees				1,462
Loan penalties and fees (1)				138
	\$	17,944	\$	20,041

(1) The default interest expense and the loan penalties and fees were incurred due to the Company's elective default on the Mass Mutual loan.

10. Series C Cumulative Convertible Redeemable Preferred Stock

In July 2005, the Company sold 4,102,564 shares of Series C preferred stock with a liquidation preference of \$24.375 per share to Security Capital Preferred Growth, Incorporated, an investment vehicle advised by Security Capital Research & Management Incorporated, for gross proceeds of \$99.0 million, or \$24.13 per share, which included a 1% discount to the conversion price/liquidation preference. Other costs of the offering totaled \$130,000. Net proceeds of \$99.0 million were contributed to the Operating Partnership in exchange for preferred membership units with economic terms substantially identical to the Series C preferred stock. The net proceeds were used to partially finance the Company's acquisition of six Renaissance hotels. As a result of the Company's stock dividend paid in January 2009, the Series C conversion price was adjusted to \$22.23 per share. Each share of Series C preferred stock is convertible into 1.096 shares of the Company's common stock at the option of the holder, subject to customary antidilution provisions, including stock splits, stock dividends, non-cash distributions and above-market issuer self-tender or exchange offers. As of July 8, 2010, the Series C preferred stock is redeemable at the Company's option, in whole or in part, at any time or from time to time, for cash at a redemption price of \$24.375 per share, plus accrued and unpaid dividends up to and including the redemption date. The holders of the Series C preferred stock have the right to require the Company to redeem the Series C preferred stock in the event of any of the following: (1) a change in control of the Company, if certain conditions are not met; (2) a REIT termination event; or (3) a termination of the Company's listing on either the New York Stock Exchange or NASDAQ. In general, holders of Series C preferred stock vote on an as-converted basis as a single class with holders of the Company's common stock. The holders are eligible to receive a participating dividend to the extent the Company's dividend on its common stock exceeds \$0.339 per share per quarter. The quarterly dividend on the Series C preferred stock is currently \$0.393 per share. If the Company fails to meet certain financial ratios for four consecutive quarters, a financial ratio violation will occur with respect to the Company's Series C preferred stock. During the continuation of a financial ratio violation, among other things, the Company would be restricted from paying dividends on its common stock, and may incur a 50 basis point per quarter dividend increase on the Series C preferred stock. Additionally, the Series C preferred stockholders would gain the right to appoint one board member. The Company currently does not expect to incur a financial ratio violation as it expects to meet its covenants. Should operations deteriorate from current levels, however, the Company may fail to meet its financial ratios with respect to its Series C preferred stock for four consecutive quarters, which would cause the Company to incur a financial ratio violation. The Series C preferred stock has no maturity date and,

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except as set forth above, the Company is not required to redeem the Series C preferred stock at any time. As the Series C preferred stockholders may redeem their shares in certain circumstances outside of the control of the Company, the Series C preferred stock has not been classified as permanent equity.

The initial carrying value of the Series C preferred stock was recorded at its sales price less costs to issue on the date of issuance. This carrying value was periodically adjusted so that the carrying value equals the redemption value on the redemption date, which is the earliest date available for the Company to redeem the Series C preferred stock. The carrying value may also be periodically adjusted for any accrued and unpaid dividends. The initial carrying value of the Series C preferred stock was fully accreted to its redemption value during the third quarter of 2010, resulting in a carrying value of \$0.1 million at both March 31, 2011 and December 31, 2010.

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11. Stockholders Equity

Series A Cumulative Redeemable Preferred Stock

In March 2005, the Company sold an aggregate of 4,850,000 shares of 8.0% Series A and B Cumulative Redeemable Preferred Stock (Series A preferred stock and Series B preferred stock, respectively) with a liquidation preference of \$25.00 per share for gross proceeds of \$121.3 million. Underwriting and other costs of the offering totaled \$3.8 million. Net proceeds of \$117.5 million were contributed to the Operating Partnership in exchange for preferred membership units with economic terms substantially identical to the Series A and B preferred stock. Subsequent to this offering, the shares of Series B preferred stock were exchanged for an equivalent number of shares of Series A preferred stock. The net proceeds were used to reduce borrowings under the Company's credit facility in existence at the time and for acquisitions. As of March 17, 2010, the Series A preferred stock is redeemable at the Company's option, in whole or in part, at any time or from time to time, for cash at a redemption price of \$25.00 per share, plus accrued and unpaid dividends up to and including the redemption date. Holders of Series A preferred stock generally have no voting rights. However, if the Company is in arrears on dividends on the Series A preferred stock for six or more quarterly periods, whether or not consecutive, holders of the Series A preferred stock will be entitled to vote at its next annual meeting and each subsequent annual meeting of stockholders for the election of two additional directors to serve on the Company's board of directors until all unpaid dividends and the dividend for the then-current period with respect to the Series A preferred stock have been paid or declared and a sum sufficient for the payment thereof set aside for payment. As of March 31, 2011, the Company is in compliance with the dividend requirements for the Series A preferred stock. The Series A preferred stock has no maturity date and the Company is not required to redeem the Series A preferred stock at any time.

In April 2006, the Company sold an additional 2,200,000 shares of Series A preferred stock with a liquidation preference of \$25.00 per share for gross proceeds of \$55.0 million. The proceeds to the Company, net of offering costs, were \$54.2 million, and were used together with proceeds of certain debt refinancings to repay the Company's term loan facility.

Common Stock

In November 2010, the Company issued 19,500,000 shares of its common stock for net proceeds of approximately \$190.6 million. The Company used a portion of these proceeds to fund the purchase of the outside 62% equity interests in its Doubletree Guest Suites Times Square joint venture in January 2011, the purchase of the outside 50% equity interest in its BuyEfficient joint venture in January 2011, the purchase of the JW Marriott New Orleans in February 2011 and the purchase of a 75% majority interest in the entity that owns the Hilton San Diego Bayfront in April 2011.

12. Long-Term Incentive Plan

Stock Grants

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Restricted shares and restricted share units granted pursuant to the Company's Long-Term Incentive Plan generally vest over periods from one to five years from the date of grant. The value of shares granted has been calculated based on the share price on the date of grant and is being amortized as compensation expense in accordance with the Company's policy on a straight-line basis over the vesting periods for the entire award. The Company's compensation expense and forfeitures related to these restricted shares and restricted share units for the three months ended March 31, 2011 and 2010 were as follows (in thousands):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Compensation expense	\$ 806	\$ 1,321
Forfeiture expense adjustments	\$ 129	\$ 74

Stock Options

In April 2008, the Compensation Committee of the Company's board of directors approved a grant of 200,000 non-qualified stock options (the Options) to Robert A. Alter, the Company's former Chief Executive Officer and current Executive Chairman. The Options fully vested in April 2009, and will expire in April 2018. The exercise price of the Options is \$17.71 per share.

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The initial fair value of the Options was \$0.7 million, and was estimated using a binomial option pricing model with the following assumptions:

Expected dividend yield	7.90%
Risk-free interest rate	3.29%
Expected volatility	26.90%
Expected life (in years)	5.5

The expected life was calculated using the simplified method as outlined in the Securities and Exchange Commission's Staff Accounting Bulletin No. 107.

13. Commitments and Contingencies

Management Agreements

Management agreements with the Company's third-party hotel managers require the Company to pay between 1% and 3.5% of total revenue of the managed hotels to the third-party managers each month as a basic management fee. Total basic management fees incurred by the Company during the three months ended March 31, 2011 and 2010 were included in the Company's statements of operations as follows (in thousands):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Continuing operations – property general and administrative expense	\$ 4,083	\$ 3,507
Discontinued operations	70	489
	\$ 4,153	\$ 3,996

In addition to basic management fees, provided that certain operating thresholds are met, the Company may also be required to pay certain of its third-party managers incentive management fees. Total incentive management fees incurred by the Company were \$0.7 million and \$0.5 million for the three months ended March 31, 2011 and 2010, respectively, all of which were included in property general and administrative expense.

License and Franchise Agreements

The Company has entered into license and franchise agreements related to certain of its hotel properties. The license and franchise agreements require the Company to, among other things, pay monthly fees that are calculated based on specified percentages of certain revenues. The license and franchise agreements generally contain specific standards for, and restrictions and limitations on, the operation and maintenance of the hotels which are established by the franchisors to maintain uniformity in the system created by each such franchisor. Such standards generally regulate the appearance of the hotel, quality and type of goods and services offered, signage and protection of trademarks. Compliance

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with such standards may from time to time require the Company to make significant expenditures for capital improvements.

Total license and franchise costs incurred by the Company during the three months ended March 31, 2011 and 2010 were \$5.3 million and \$5.9 million, respectively, of which royalties totaled \$1.8 million and \$2.3 million, for the three months ended March 31, 2011 and 2010, respectively. The remaining costs included advertising, reservation and priority club assessments. Total license and franchise costs incurred by the Company during the three months ended March 31, 2011 and 2010 were included in the Company's statements of operations as follows (in thousands):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Continuing operations franchise costs	\$ 5,250	\$ 4,515
Discontinued operations		1,373
	\$ 5,250	\$ 5,888

Several of the Company's franchise agreements contain corporate guaranties. In the event of a default under any of these franchise agreements, the Company may be liable for termination fees. Currently, five of the Mass Mutual eight hotels remain subject to franchise agreements which contain corporate guaranties. If the franchise agreements on these five hotels were to be terminated, the Company may be liable for up to \$19.6 million in termination fees, which is included in other current liabilities of discontinued operations, net in the accompanying consolidated balance sheets. The Company expects the franchise agreements on these five hotels to be finalized during the second quarter of 2011, and to record any necessary adjustments to its liability for the termination fees in its statement of operations for the three months ended June 30, 2011, however resolution may not be achieved until the second half of 2011.

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Renovation and Construction Commitments

At March 31, 2011, the Company had various contracts outstanding with third parties in connection with the renovation of certain of its hotel properties aimed at maintaining the appearance and quality of its hotels. The remaining commitments under these contracts at March 31, 2011 totaled \$31.2 million.

Ground and Operating Leases

Total rent expense incurred pursuant to ground lease agreements for the three months ended March 31, 2011 and 2010 was included in the Company's statements of operations as follows (in thousands):

	Three Months Ended March 31, 2011 (unaudited)	Three Months Ended March 31, 2010 (unaudited)
Continuing operations – property general and administrative expense	\$ 2,555	\$ 1,154
Discontinued operations	9	111
	\$ 2,564	\$ 1,265

Rent expense incurred pursuant to the lease on the corporate facility totaled \$0.1 million for both the three months ended March 31, 2011 and 2010, and was included in corporate overhead expense.

Concentration of Risk

As of March 31, 2011, nine of the Company's 32 hotels were located in California, the largest concentration of the Company's hotels in any state, representing approximately 24% of the Company's rooms and approximately 24% of the revenue generated by the Company's 32 hotels during the three months ended March 31, 2011. The concentration of the Company's hotels in California exposes the Company's business to economic conditions, competition and real and personal property tax rates unique to California.

Other

The Company has provided unsecured environmental indemnities to certain lenders. The Company has performed due diligence on the potential environmental risks, including obtaining an independent environmental review from outside environmental consultants. These indemnities obligate the Company to reimburse the indemnified parties for damages related to certain environmental matters. There is no term or damage limitation on these indemnities; however, if an environmental matter arises, the Company could have recourse against other previous owners or a claim against its environmental insurance policies.

At March 31, 2011, the Company had \$1.6 million of outstanding irrevocable letters of credit to guaranty the Company's financial obligations related to workers' compensation insurance programs from prior policy years. The beneficiaries of these letters of credit may draw upon these letters of credit in the event of a contractual default by the Company relating to each respective obligation. No draws have been made through March 31, 2011.

14. Transactions With Affiliates

Other Reimbursements

From time to time, the Company pays for certain expenses such as payroll, insurance and other costs on behalf of certain affiliates. The affiliates generally reimburse such amounts on a monthly basis. At March 31, 2011 and December 31, 2010, amounts owed to the Company by its affiliates amounted to \$17,000 and \$44,000, respectively, and are included in due from affiliates in the accompanying consolidated balance sheets.

15. Variable Interest Entities

The Company adopted Accounting Standards Update (ASU) No. 2009-17, codified in the Consolidation Topic of the FASB ASC, on January 1, 2010, which changed the consolidation guidance applicable to variable interest entities (VIEs). It also amended the guidance governing the determination of whether an enterprise is the primary beneficiary of a VIE, and is, therefore, required to consolidate an entity, by requiring a qualitative analysis rather than a quantitative analysis. The qualitative analysis includes, among other things, consideration of who has the power to direct the activities of the entity that

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most significantly impact the entity's economic performance and who has the obligation to absorb losses or the right to receive benefits of the VIE that could potentially be significant to the VIE. This topic also requires continuous reassessments of whether an enterprise is the primary beneficiary of a VIE. Previously, the applicable standard required reconsideration of whether an enterprise was the primary beneficiary of a VIE only when specific events had occurred. The topic also requires additional disclosures about an enterprise's involvement with a VIE.

Upon adoption of ASU No. 2009-17, the Company evaluated its variable interests, including the management agreements it has with its third-party hotel managers and its interest in the Doubletree Guest Suites Times Square joint venture, to determine whether or not these variable interests are VIEs. The Company's analysis included both quantitative and qualitative reviews. In arriving at the VIE determination for its third-party management agreements, the Company followed the guidance in ASC 810-10-55-37, *Fees Paid to Decision Makers or Service Providers*, which states that fees paid to a legal entity's decision makers or service providers are not variable interests if six conditions are met: 1) the fees are compensation for services provided and are commensurate with the level of effort required to provide those services; 2) substantially all of the fees are at or above the same level of seniority as other operating liabilities of the VIE that arise in the normal course of the VIE's activities, such as trade payables; 3) the decision maker or service provider does not hold other interests in the VIE that individually, or in the aggregate, would absorb more than an insignificant amount of the VIE's expected losses or receive more than an insignificant amount of the VIE's expected residual returns; 4) the service arrangement includes only terms, conditions, or amounts that are customarily present in arrangements for similar services negotiated at arm's length; 5) the total amount of anticipated fees are insignificant relative to the total amount of the VIE's anticipated economic performance; and 6) the anticipated fees are expected to absorb