

RESOLUTION NO. 13-211

A RESOLUTION OF THE CITY COMMISSION OF THE CITY OF KEY WEST, FLORIDA, APPROVING THE ATTACHED ASSIGNMENT OF LEASE AND CONSENT OF LESSOR FROM SMB RESTAURANT, LLC (ASSIGNOR) TO SUNSET CITY, LLC A DELAWARE LIMITED LIABILITY CORPORATION (ASSIGNEE), A WHOLLY OWNED SUBSIDIARY OF LASALLE HOTEL OPERATING PARTNERSHIP, LP (GUARANTOR) FOR 1405 DUVAL STREET D/B/A THE SOUTHERNMOST BEACH CAFÉ; APPROVING A SUBLEASE BETWEEN SUNSET CITY, LLC AND SUNSET CITY LESSEE, LLC; PROVIDING FOR AN EFFECTIVE DATE

WHEREAS, the City Commission approved the original Lease Agreement with SMB Restaurant, LLC in Resolution 09-110; and

NOW, THEREFORE, BE IT RESOLVED BY THE CITY COMMISSION OF THE CITY OF KEY WEST, FLORIDA AS FOLLOWS:

Section 1: That the attached Assignment of Lease Agreement and Consent of Lessor is hereby approved.

Section 2: That it is further approved, as set forth in the Assignment of Lease Agreement, that Assignee is authorized to sublease to Sunset City Lessee, LLC, a Delaware Limited Liability Corporation, and wholly owned subsidiary of LaSalle Hotel Operating Partnership, LP.

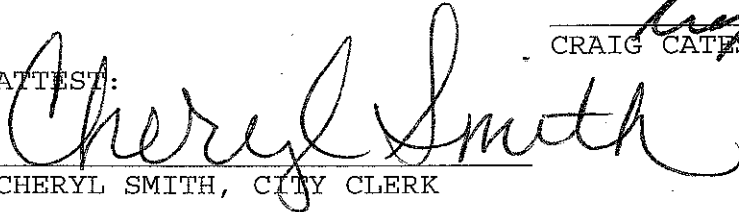
Section 3: That this Resolution shall go into effect immediately upon its passage and adoption and authentication by the signature of the Presiding Officer and the Clerk of the Commission.

Passed and adopted by the City Commission at a meeting held this 20 day of August, 2013.

Authenticated by the Presiding Officer and Clerk of the Commission on 21 day of August, 2013.

Filed with the Clerk on August 21, 2013.

ATTEST:

  
CHERYL SMITH, CITY CLERK

  
CRAIG CATES, MAYOR

# Executive Summary



**TO:** City Commission

**CC:** Bogdan Vitas

**FR:** Marilyn Wilbarger, RPA, CCIM

**DT:** August 16, 2013

**RE:** Lease Assignment for SMB, LLC DBA Southernmost Beach Cafe

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## **ACTION STATEMENT**

The city has received a request from the tenant SMB Restaurant, LLC to consider a lease assignment from SMB Restaurant, LLC to Sunset City, LLC, whose sole member is LaSalle Hotel Operating Partnership, LP which is a wholly owned subsidiary of LaSalle Hotel Properties which is a publicly traded Maryland Real Estate Investment Trust. The Assignee will also be authorized to sublease to Sunset City Lessee LLC, another wholly owned subsidiary.

## **HISTORY**

The CRA entered into a ten year lease for the restaurant building located on South Beach that will expire on April 30, 2019. The current tenant, SMB Restaurant, LLC has entered into a purchase agreement with the Assignee and is requesting a simple assignment meaning that no terms or conditions of the lease change for the remainder of the lease term.

The leases provide for the assignment as described in Section 10 excerpted here, as follows:

**“10. ASSIGNMENT AND HYPOTHECATION** - This Lease is not transferable or LANDLORD which may be withheld and shall be at the sole discretion of the LANDLORD.

Any assignment or sub-letting, even with LANDLORD’S consent shall not relieve TENANT from liability for payment of Rent or from the obligation to keep and be bound by the agreements of this Lease. The acceptance of Rent from any other person shall not be deemed to be a waiver of any of the agreements of this Lease or to be consent to the assignment for the benefit of creditors or by operation of law and shall not be effective to transfer any rights to any assignee without prior consent of LANDLORD. In the event TENANT wishes to assign this Lease and LANDLORD consents to such assignment, LANDLORD may charge a reasonable fee, not to exceed **\$500.00** to help offset any costs LANDLORD may have in preparing such assignment, or in examining the information, financial statements, operating history, references, etc., necessary to effectuate same. Any assignment, transfer, hypothecation, mortgage, or subletting without LANDLORD’S written consent shall give LANDLORD the right to terminate this Lease and to re-enter and repossess the Demised Premises and the LANDLORD’S right to damages shall survive.

If the TENANT is a corporation, then a sale or transfer of a controlling interest in the corporation by sale of stock or otherwise shall constitute an assignment for purposes of this provision.”

The proposed Assignee's parent organization is excerpted here from the most recent SEC Form 10-Q filing, Section 1.

**"Organization**

LaSalle Hotel Properties (the "Company"), a Maryland real estate investment trust organized on January 15, 1998, primarily buys, owns, redevelops and leases upscale and luxury full-service hotels located in convention, resort and major urban business markets. The Company is a self-administered and self-managed real estate investment trust ("REIT") as defined in the Internal Revenue Code of 1986, as amended (the "Code"). As a REIT, the Company is generally not subject to federal corporate income tax on that portion of its net income that is currently distributed to its shareholders. The income of LaSalle Hotel Lessee, Inc. (together with its wholly owned subsidiaries, "LHL"), the Company's wholly owned taxable REIT subsidiary ("TRS"), is subject to taxation at normal corporate rates.

As of June 30, 2013, the Company owned interests in 40 hotels with over 10,600 guest rooms located in nine states and the District of Columbia. Each hotel is leased to LHL (see Note 8) under a participating lease that provides for rental payments equal to the greater of (i) a base rent or (ii) a participating rent based on hotel revenues. The LHL leases expire between December 2013 and December 2015. Lease revenue from LHL is eliminated in consolidation. A third-party non-affiliated hotel operator manages each hotel pursuant to a hotel management agreement.

Substantially all of the Company's assets are held directly or indirectly by, and all of its operations are conducted through, LaSalle Hotel Operating Partnership, LP (the "Operating Partnership"). The Company is the sole general partner of the Operating Partnership. The Company owned, through a combination of direct and indirect interests, 99.7% of the common units of the Operating Partnership at June 30, 2013. The remaining 0.3% is held by limited partners who held 296,300 common units of the Operating Partnership at June 30, 2013. See Note 6 for additional disclosures on common operating partnership units."

The complete 10-Q filing is attached for reference.

**FINANCIAL STATEMENT:**

The current tenant has met all of the financial obligations of the lease and the rent will continue pursuant to the existing lease. The financial safeguards in the lease, namely the required letter of credit in the amount of \$150,000 will provide additional security to ensure that rent will be paid for an adequate period of time to regain possession in the event of a default. Additionally LaSalle Hotel Operating Partnership LP will guaranty the complete performance of all of the covenants and obligations of the Assignee.

**CONCLUSION:**

The requested action is permitted under the terms of the lease, at the sole discretion of the Landlord, and the current tenant is not relieved from liability if the assignee defaults in its obligations under the terms of the lease therefore the financial risk to the City is minimized. The business is highly successful in a very desirable location that would attract substantial interest should there ever be an opportunity to offer it for lease.

**ATTACHMENTS:**

Lease: City resolution 09-110

Lease Assignment and Consent of Lessor

2<sup>nd</sup> Quarter 2013 United States Securities and Exchange Commission Form 10-Q Quarterly Report

Corporate formation filings Sunset City, LLC

Corporate formation filings Sunset City Lessee, LLC

## ASSIGNMENT OF LEASE AGREEMENT AND CONSENT OF LESSOR

THIS ASSIGNMENT (this "Assignment") is made this 19~~th~~ day of August, 2013, by and between SMB Restaurant, LLC ("Assignor") and Sunset City LLC, a Delaware LLC ("Assignee"), a wholly owned subsidiary of LaSalle Hotel Operating Partnership, LP ("Guarantor").

A. Assignor, as tenant and City of Key West, as landlord ("Landlord") have previously entered into that certain lease dated May 1, 2009 per Resolution 09-110 (the "Lease"), a copy of which is attached hereto as Exhibit "A". The Lease pertains to real property located at 1405 Duval Street, in Monroe County, Florida, and more particularly described on Exhibit B, which is attached hereto and incorporated by reference.

B. Assignor desires to assign all of its right, title and interest in the Lease to Assignee, Assignee desires to accept and assume the same, and Landlord is willing to consent to the proposed Assignment, all on the terms and conditions hereof.

NOW, THEREFORE, in consideration of the mutual terms and conditions herein contained, and other good and valuable consideration, the receipt of which is hereby acknowledged, the parties hereby agree as follows:

1. Assignor hereby assigns and transfers unto Assignee all of its right, title, and interest in and to the Lease, subject to all the conditions and terms contained therein.

2. Assignor herein expressly represents and warrants that (a) it is the lawful and sole owner of the lessee's interest assigned herein, (b) Assignor's interest in the Lease is free from all encumbrances, and (c) Assignor has not received any written notice from Landlord that Assignor has failed to perform all the duties and obligations or failed to make any payments required under the Lease.

3. Assignor herein expressly acknowledges, pursuant to paragraph 8 of the Lease, that this Assignment shall not relieve Assignor from liability for payment of rent or from the obligation to keep and be bound by the terms, conditions, and covenants contained in the Lease, provided, however, no such liability shall extend beyond the expiration of the current expiration date of the initial Term (as defined in the Lease) which is April 30, 2019.

4. Assignee herein expressly agrees to assume, perform and be liable for all of the duties and obligations of "Tenant" required by and under the terms of the Lease, including but not limited to, the obligation to pay all rent due thereunder from and after the effective date of this Assignment.

5. Assignee is hereby authorized to sublease to Sunset City Lessee LLC, Delaware LLC and wholly owned subsidiary of LaSalle Hotel Operating Partnership, LP.

6. This Assignment is contingent upon the completion of the sale between Assignor and Assignee of the business known as "Southernmost Beach Café" and conducted on and from the Premises. References herein to the "effective date" shall mean the date of the closing of the aforementioned sale transaction.

7. Assignee agrees to indemnify, defend and hold Assignor and its legal representatives, successors and assigns harmless from and against any and all losses, damages, claims, demands, suits, judgments, liabilities, costs and expenses (including, without limitation, reasonable attorneys' fees and court costs), suffered or incurred by any of said indemnitees under or in connection with the Lease arising on or after the effective date hereof. Assignor agrees to indemnify, defend and hold Assignee and its legal representatives, successors and assigns harmless from and against any and all losses, damages, claims, demands, suits, judgments, liabilities, costs and expenses (including, without limitation, reasonable attorneys' fees and court costs), suffered or incurred by any of said indemnitees under or in connection with the Lease and arising prior to the effective date hereof.

8. No later than the effective date of this Assignment, Assignee herein expressly agrees to provide to Landlord a letter of credit from a federally insured bank in favor of Landlord as security for the faithful performance by Assignee of the terms, conditions and covenants of the Lease. The amount of the letter of credit shall be \$150,000.00.

9. In the event Assignee files any form of bankruptcy, Landlord shall be entitled to immediate termination of the automatic stay provisions of 11 U.S.C. §362, granting Landlord complete relief and allowing Landlord to exercise all of its legal and equitable rights and remedies, including, without limitation, the right to terminate the Lease and dispossess Assignee from the Premises in accordance with Florida law. Additionally, Assignee agrees not to directly or indirectly oppose or otherwise defend against Landlord's effort to gain relief from any automatic stay. Landlord shall be entitled as aforesaid to the lifting of the automatic stay without the necessity of an evidentiary hearing and without the necessity or requirement of Landlord to establish or prove the value of the leasehold, the lack of adequate protection of his interest in the leasehold, or the lack of equity in the same. Assignee specifically agrees and acknowledges that the lifting of the automatic stay hereunder by the appropriate bankruptcy court shall be deemed to be "for cause" pursuant to section 362(d)(1).


10. The Guarantor does hereby absolutely, unconditionally and irrevocably guarantee to the City the full and complete performance of all of Assignee's covenants and obligations under the Lease and full payment by Assignee of all rentals, additional charges and other charges and amounts required to be paid hereunder during the entire term. Guarantor's obligations hereunder shall be primary and not secondary and are independent of the obligations of the Assignee.

**[REMAINDER OF PAGE INTENTIONALLY LEFT BLANK;  
SIGNATURES ON FOLLOWING PAGE]**

IN WITNESS WHEREOF, the parties have executed this Assignment as of the date first above written.

**ASSIGNOR: SMB Restaurant, LLC**

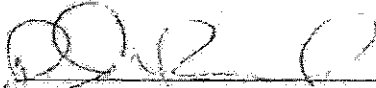
  
Witness to Assignor


By   
Name: Stuart Kaufman  
Title: Manager Member

**ASSIGNEE: Sunset City LLC, a Delaware LLC**

By: LaSalle Hotel Operating Partnership, L.P., its  
Managing member


By: LaSalle Hotel Properties, its general partner

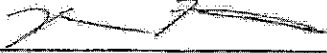
  
Witness to Assignee

By   
Name: Russ Rossini  
Title: CFO

**GUARANTOR: LaSalle Hotel Operating Partnership,  
L.P.**

By: LaSalle Hotel Properties, its general partner

  
Witness to Guarantor

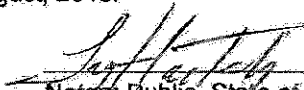
By   
Name: Russ Rossini  
Title: CFO

ASSIGNOR ACKNOWLEDGMENT

State of MICHIGAN }  
County of Franklin

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgments, STUART KAUFMAN, to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same individually and for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this 19 day of August, 2013.

  
\_\_\_\_\_  
Notary Public, State of MICHIGAN  
My Commission Expires: 2-28-15

ASSIGNEE ACKNOWLEDGMENT

State of \_\_\_\_\_ }  
County of \_\_\_\_\_ }

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgments, \_\_\_\_\_, to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same individually and for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this \_\_\_\_ day of August, 2013.

\_\_\_\_\_  
Notary Public, State of \_\_\_\_\_  
My Commission Expires:



ASSIGNOR ACKNOWLEDGMENT

State of MICHIGAN }  
County of \_\_\_\_\_ }

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgments, STUART KAUFMAN, to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same individually and for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this \_\_\_\_ day of August, 2013.

\_\_\_\_\_  
Notary Public, State of \_\_\_\_\_  
My Commission Expires:

ASSIGNEE ACKNOWLEDGMENT

State of Maryland }  
County of Montgomery }

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgments, Bruce Reagin, to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same individually and for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this 19<sup>th</sup> day of August, 2013.

Elizabeth A. Hoyle  
Notary Public, State of Maryland  
My Commission Expires:

ELIZABETH A. HOYLE  
Notary Public-Maryland  
Montgomery County  
My Commission Expires  
July 22, 2016



GUARANTOR ACKNOWLEDGMENT

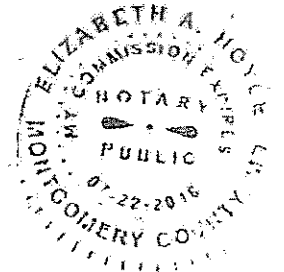
State of Maryland }  
County of Montgomery

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgments, Bruce Rogers, to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same individually and for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this 17<sup>th</sup> day of August, 2013.

Elizabeth A. Hoyle  
Notary Public, State of Maryland  
My Commission Expires:

ELIZABETH A. HOYLE  
Notary Public - Maryland  
Montgomery County  
My Commission Expires  
July 22, 2016



**CONSENT OF LANDLORD**

I, Craig Cates, Mayor of the City of Key West, the landlord named in that certain lease dated May 1, 2009 per Resolution 09-110, herein expressly consent to the Assignment so long as the sale between Assignor and Assignee of the business known as "Southernmost Beach Cafe" which is conducted on and from the Premises is completed on or before September 30, 2013, failing which this Consent shall be deemed null and void, of no force or effect and withdrawn.

I also consent to the agreement by Assignee to assume, after the effective date of the Assignment, the payment of rent and the performance of all duties and obligations as set forth in the Lease and accept Assignee as tenant in the place of Smithburg, Inc. alone. Landlord hereby agrees that (i) any security deposit delivered by Assignor to Landlord in connection with the Lease will be returned to Assignor within 15 days following the effective date of the Assignment and (ii) a fee will be charged by Landlord in connection with the Assignment and Landlord's consent thereto.

Defined terms used in this Consent of Landlord shall have the meanings ascribed to such terms in the Assignment of Lease by and between SMB, LLC, as assignor and, Sunset City, LLC, as assignee, to which this Consent of Landlord is attached.

**LANDLORD:**

City of Key West

Vivian Perez  
Witness as to Landlord

Craig Cates  
Craig Cates, Mayor

State of Florida }  
County of Monroe }

I HEREBY CERTIFY that on this day personally appeared before me, an officer duly authorized to administer oaths and take acknowledgements, Craig Cates to me personally known or who provided \_\_\_\_\_ as photo identification, and who executed the foregoing instrument and he acknowledged before me that he executed the same for the purposes therein expressed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in the County and State last aforesaid, this 21st day of August, 2013.

Susan P. Harrison  
Notary Public, State of Florida  
My Commission Expires:



**DISCLOSURE STATEMENT**

STATE OF MARYLAND  
COUNTY OF MONTGOMERY

Personally appeared before me, Ian Gaum, who after being duly sworn and cautioned, did depose and state as follows:

1. I am Ian Gaum, Senior Vice-President of LaSalle Hotel Properties, the general partner of LaSalle Hotel Operating Partnership, L.P. ("LHOP"), the managing member and sole owner of Sunset City, LLC (the "Assignee"). Upon approval of the lease assignment from SMB, LLC to the Assignee for Southernmost Beach Cafe, 100% of the assets, gross income and primary source of the income of SMB, LLC will be transferred from SMB, LLC to the Assignee. I make this affidavit regarding the present financial information of the Assignee, as the managing member of Assignee and as a Senior Vice-President of LaSalle Hotel Properties, in accordance with City Ordinance, Article VIII. City Property, Division 1, Generally, Section 2-871 (d)

2. I herein expressly certify and affirm that the Assignee will have a net worth of approximately \$184,500,000, will have no liabilities and its source of income will be from the operation of the Southernmost Hotel Collection and rent from the subleasing of the Southernmost Beach Cafe upon the purchase of the Southernmost Hotel Collection and the assignment of the lease to Assignee.

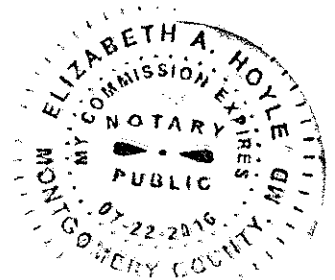
[Signature]

Sworn to and subscribed before me this 15<sup>th</sup> day of August, 2013.

[Signature]  
Notary Public - State of Maryland

My commission expires:

ELIZABETH A. HOYLE  
Notary Public-Maryland  
Montgomery County  
My Commission Expires  
July 22, 2016



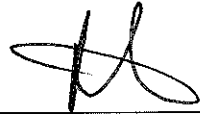
**DISCLOSURE STATEMENT**

STATE OF MARYLAND  
COUNTY OF MONTGOMERY

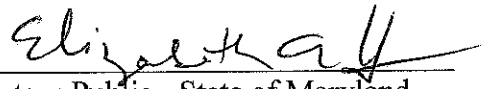
Personally appeared before me, Ian Gaum, who after being duly sworn and cautioned, did depose and state as follows:

1. I am Ian Gaum, Senior Vice-President of LaSalle Hotel Lessee, Inc. a wholly owned subsidiary of LaSalle Hotel Operating Partnership, L.P, the managing member and sole owner of Sunset City Lessee, LLC (the "Sublessee"). Upon approval of the lease assignment from SMB, LLC to Sunset City, LLC (the "Lessee") for Southernmost Beach Cafe, the Lessee will sublease the Southernmost Beach Café to the Sublessee. I make this affidavit regarding the present financial information of the Sublessee, as the managing member of Sublessee and as a Senior Vice-President of LaSalle Hotel Lessee, Inc., in accordance with City Ordinance, Article VIII. City Property, Division 1, Generally, Section 2-871 (d)

2. I herein expressly certify and affirm that the Sublessee will have no liabilities and its source of income will be from the operation of the Southernmost Hotel Collection and the Southernmost Beach Cafe upon the purchase of the Southernmost Hotel Collection by Sublessee.

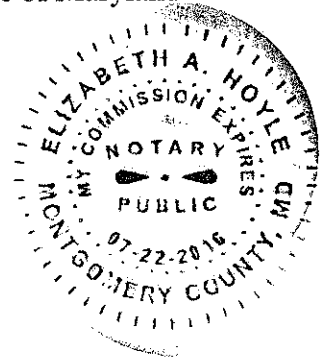


Sworn to and subscribed before me this 15<sup>th</sup> day of August, 2013.

  
Notary Public - State of Maryland

My commission expires:

ELIZABETH A. HOYLE  
Notary Public-Maryland  
Montgomery County  
My Commission Expires  
July 22, 2016



Citibank,N.A.

DATE : AUG. 26, 2013

ISSUING BANK:  
CITIBANK, N.A.  
C/O IT'S SERVICER, CITICORP NORTH AMERICA, INC.  
3800 CITIBANK CENTER, BUILDING B, 3RD FLOOR  
TAMPA, FL 33610  
PHONE: 1-866-945-6284

BENEFICIARY:  
CITY OF KEY WEST  
PROPERTY MANAGEMENT  
525 ANGELA STREET  
KEY WEST, FL 33040

APPLICANT:  
LASALLE HOTEL OPERATING PARTNERSHIP, L.P.  
3 BETHESDA METRO CENTER, SUITE 1200  
BETHESDA, MD 20814

LETTER OF CREDIT NO: 63669015

GENTLEMEN:  
BY ORDER OF OUR CLIENT, LASALLE HOTEL OPERATING PARTNERSHIP, L.P. (THE "APPLICANT"), WE HEREBY OPEN OUR IRREVOCABLE STANDBY LETTER OF CREDIT NO. 63669015, IN YOUR FAVOR FOR AN AMOUNT NOT TO EXCEED IN AGGREGATE USD 150,000.00 (ONE HUNDRED FIFTY THOUSAND AND 00/100 U.S. DOLLARS), EFFECTIVE IMMEDIATELY AND EXPIRING AT THE OFFICE OF OUR SERVICER, CITICORP NORTH AMERICA, INC. AT 3800 CITIBANK CENTER, BUILDING B, 3RD FLOOR, TAMPA, FLORIDA 33610 ATTN. STANDBY LETTER OF CREDIT UNIT OR SUCH OTHER OFFICE AS WE MAY ADVISE YOU FROM TIME TO TIME (THE "OFFICE"), ON SEPTEMBER 01, 2014.

FUNDS HEREUNDER ARE AVAILABLE TO YOU AGAINST PRESENTATION OF YOUR SIGHT DRAFT(S), DRAWN ON US, MENTIONING THEREON OUR LETTER OF CREDIT NUMBER 63669015, ACCOMPANIED BY YOUR WRITTEN AND DATED STATEMENT, SIGNED BY AN AUTHORIZED OFFICER OF YOUR COMPANY, STATING THE FOLLOWING:

"WE HEREBY CERTIFY THAT THE AMOUNT OF ANY DRAFT(S) DRAWN HEREUNDER REPRESENTS FUNDS DUE AND PAYABLE BECAUSE A DEFAULT HAS OCCURRED UNDER THAT CERTAIN LEASE AGREEMENT BETWEEN SUNSET CITY, LLC (THE "TENANT"), AND CITY OF KEY WEST (THE "LANDLORD"), DATED \_\_\_\_\_, WRITTEN NOTICE OF SUCH DEFAULT WAS DULY GIVEN TO THE TENANT AND ALL APPLICABLE GRACE PERIODS EXPIRED UNDER SAID LEASE."

IT IS A CONDITION OF THIS LETTER OF CREDIT THAT IT SHALL BE DEEMED AUTOMATICALLY EXTENDED, WITHOUT AMENDMENT, FOR ADDITIONAL PERIOD(S) OF ONE YEAR FROM THE EXPIRY DATE HEREOF, OR ANY FUTURE EXPIRATION DATE, UNLESS AT LEAST THIRTY (30) DAYS PRIOR TO ANY EXPIRATION DATE WE NOTIFY YOU BY REGISTERED MAIL OR BY ANY OTHER RECEIPTED MEANS THAT WE ELECT NOT TO CONSIDER THIS LETTER OF CREDIT RENEWED FOR ANY SUCH ADDITIONAL PERIOD, WHEREUPON YOU MAY DRAW FOR THE AVAILABLE AMOUNT UNDER THIS LETTER OF CREDIT BY MEANS OF YOUR SIGHT DRAFT(S), DRAWN ON US, MENTIONING OUR LETTER OF CREDIT NUMBER.

Citibank,N.A.

WE HEREBY AGREE TO HONOR EACH DRAFT DRAWN UNDER AND IN COMPLIANCE WITH THE TERMS AND CONDITIONS OF THIS LETTER OF CREDIT IF PRESENTED, AS SPECIFIED, AT OUR OFFICE ON OR BEFORE EXPIRATION DATE.

SHOULD YOU HAVE OCCASION TO COMMUNICATE WITH US REGARDING THIS LETTER OF CREDIT, PLEASE DIRECT YOUR CORRESPONDENCE TO OUR OFFICE, MAKING SPECIFIC MENTION OF THE LETTER OF CREDIT NUMBER INDICATED ABOVE. FOR INQUIRIES YOU MAY CONTACT US AT 1-866-945-6284.

EXCEPT AS FAR AS OTHERWISE EXPRESSLY STATED HEREIN, THIS STANDBY LETTER OF CREDIT IS SUBJECT TO THE INTERNATIONAL STANDBY PRACTICES ("ISP98"), INTERNATIONAL CHAMBER OF COMMERCE, PUBLICATION NO. 590, AND AS TO MATTERS NOT GOVERNED BY THE ISP98, SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF NEW YORK AND APPLICABLE U.S. FEDERAL LAW.



AUTHORIZED SIGNATURE(S).  
CITIBANK,N.A.



**VIA FEDERAL EXPRESS**

August 15, 2013

**RE: Signed Disclosure Statement documents for Southernmost Hotel**

Dear Matt:

Per Ian Gaum's instructions I have enclosed the signed Disclosure Statement documents for Southernmost Hotel.

If you have any questions, please do not hesitate to contact Ian Gaum. He can be reached at (301) 941-1524 or via email at [igaum@lasallehotels.com](mailto:igaum@lasallehotels.com).

Regards,

Michelle Balzer  
Assistant to COO, Sr. VP Acquisitions



**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, 2013**  
OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_  
Commission file number 1-14045

**LASALLE HOTEL PROPERTIES**

(Exact name of registrant as specified in its charter)

**Maryland**

(State or other jurisdiction of  
incorporation or organization)

**36-4219376**

(IRS Employer  
Identification No.)

**3 Bethesda Metro Center, Suite 1200  
Bethesda, Maryland**

(Address of principal executive offices)

**20814**

(Zip Code)

**(301) 941-1500**

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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. Check one:

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 and preferred shares as of the latest practicable date.

Class	Outstanding at July 17, 2013
Common Shares of Beneficial Interest (\$0.01 par value)	96,256,468
7 ¼% Series G Cumulative Redeemable Preferred Shares (\$0.01 par value)	2,348,888
7 ½% Series H Cumulative Redeemable Preferred Shares (\$0.01 par value)	2,750,000
6 ¾% Series I Cumulative Redeemable Preferred Shares (\$0.01 par value)	4,400,000

**LASALLE HOTEL PROPERTIES  
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## PART I. Financial Information

## Item 1. Financial Statements

**LASALLE HOTEL PROPERTIES**  
**Consolidated Balance Sheets**  
*(in thousands, except share data)*

	June 30, 2013 (unaudited)	December 31, 2012
<b>Assets:</b>		
Investment in hotel properties, net (Note 3)	\$ 3,037,923	\$ 3,053,044
Note receivable (net of unamortized discount of \$2,302 and \$3,510, respectively)	69,698	68,490
Property under development	26,101	16,890
Cash and cash equivalents	15,113	35,090
Restricted cash reserves (Note 5)	15,766	17,414
Hotel receivables (net of allowance for doubtful accounts of \$530 and \$345, respectively)	41,698	28,485
Deferred financing costs, net	7,099	8,235
Deferred tax assets (Note 9)	1,973	1,286
Prepaid expenses and other assets	49,872	27,636
<b>Total assets</b>	<b>\$ 3,265,243</b>	<b>\$ 3,256,570</b>
<b>Liabilities:</b>		
Borrowings under credit facilities (Note 4)	\$ 180,000	\$ 153,000
Term loans (Note 4)	477,500	477,500
Bonds payable (Note 4)	42,500	42,500
Mortgage loans (including unamortized premium of \$82 and \$118, respectively) (Note 4)	516,782	579,220
Accounts payable and accrued expenses	106,248	101,365
Advance deposits	23,660	16,422
Accrued interest	3,849	4,319
Distributions payable	23,417	23,314
<b>Total liabilities</b>	<b>1,373,956</b>	<b>1,397,640</b>
Commitments and contingencies (Note 5)		
<b>Equity:</b>		
Shareholders' Equity:		
Preferred shares of beneficial interest, \$0.01 par value (liquidation preference of \$237,472 and \$227,472, respectively), 40,000,000 shares authorized, 9,498,888 and 9,098,888 shares issued and outstanding, respectively (Note 6)	95	91
Common shares of beneficial interest, \$0.01 par value, 200,000,000 shares authorized; 96,258,828 shares issued and 96,256,468 shares outstanding, and 95,480,358 shares issued and 95,445,444 shares outstanding, respectively (Note 6)	962	955
Treasury shares, at cost (Note 6)	(65)	(886)
Additional paid-in capital, net of offering costs of \$74,118 and \$71,640, respectively	2,148,243	2,118,705
Accumulated other comprehensive income (loss) (Note 4)	4,826	(7,735)
Distributions in excess of retained earnings	(268,636)	(258,004)
<b>Total shareholders' equity</b>	<b>1,885,425</b>	<b>1,853,126</b>
Noncontrolling Interests:		
Noncontrolling interests in consolidated entities	18	18
Noncontrolling interests of common units in Operating Partnership (Note 6)	5,844	5,786
<b>Total noncontrolling interests</b>	<b>5,862</b>	<b>5,804</b>
<b>Total equity</b>	<b>1,891,287</b>	<b>1,858,930</b>
<b>Total liabilities and equity</b>	<b>\$ 3,265,243</b>	<b>\$ 3,256,570</b>

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

**LASALLE HOTEL PROPERTIES**  
**Consolidated Statements of Operations and Comprehensive Income**  
*(in thousands, except share data)*  
*(unaudited)*

	For the three months ended		For the six months ended	
	June 30,		June 30,	
	2013	2012	2013	2012
<b>Revenues:</b>				
Hotel operating revenues:				
Room	\$ 179,089	\$ 167,186	\$ 306,077	\$ 281,878
Food and beverage	65,529	58,787	115,375	103,402
Other operating department	16,328	14,839	29,712	26,695
Total hotel operating revenues	<u>260,946</u>	<u>240,812</u>	<u>451,164</u>	<u>411,975</u>
Other income	2,614	1,283	4,100	2,439
Total revenues	<u>263,560</u>	<u>242,095</u>	<u>455,264</u>	<u>414,414</u>
<b>Expenses:</b>				
Hotel operating expenses:				
Room	42,294	38,688	79,878	72,541
Food and beverage	42,681	39,475	79,985	73,737
Other direct	5,998	5,558	11,020	10,184
Other indirect (Note 8)	59,189	55,152	112,924	103,193
Total hotel operating expenses	<u>150,162</u>	<u>138,873</u>	<u>283,807</u>	<u>259,655</u>
Depreciation and amortization	33,427	31,279	66,548	61,431
Real estate taxes, personal property taxes and insurance	12,780	10,865	25,134	21,676
Ground rent (Note 5)	2,791	2,210	5,286	3,986
General and administrative	5,564	4,849	10,711	9,463
Acquisition transaction costs (Note 3)	0	307	0	3,901
Other expenses	1,528	918	2,169	1,469
Total operating expenses	<u>206,252</u>	<u>189,301</u>	<u>393,655</u>	<u>361,581</u>
Operating income	57,308	52,794	61,609	52,833
Interest income	2,395	16	4,764	26
Interest expense	(13,763)	(12,503)	(27,780)	(24,281)
Income before income tax (expense) benefit	45,940	40,307	38,593	28,578
Income tax (expense) benefit (Note 9)	(4,934)	(4,969)	83	(1,977)
Net income	<u>41,006</u>	<u>35,338</u>	<u>38,676</u>	<u>26,601</u>
Net income attributable to noncontrolling interests:				
Noncontrolling interests in consolidated entities	(8)	0	(8)	0
Noncontrolling interests of common units in Operating Partnership (Note 6)	(135)	(130)	(135)	(108)
Net income attributable to noncontrolling interests	<u>(143)</u>	<u>(130)</u>	<u>(143)</u>	<u>(108)</u>
Net income attributable to the Company	40,863	35,208	38,533	26,493
Distributions to preferred shareholders	(4,107)	(5,999)	(9,172)	(13,401)
Issuance costs of redeemed preferred shares (Note 6)	(1,566)	(4,417)	(1,566)	(4,417)
Net income attributable to common shareholders	<u>\$ 35,190</u>	<u>\$ 24,792</u>	<u>\$ 27,795</u>	<u>\$ 8,675</u>

**LASALLE HOTEL PROPERTIES**  
**Consolidated Statements of Operations and Comprehensive Income - Continued**  
*(in thousands, except share data)*  
*(unaudited)*

	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
<b>Earnings per Common Share - Basic:</b>				
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.37	\$ 0.29	\$ 0.29	\$ 0.10
<b>Earnings per Common Share - Diluted:</b>				
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	\$ 0.37	\$ 0.29	\$ 0.29	\$ 0.10
<b>Weighted average number of common shares outstanding:</b>				
Basic	95,465,464	85,451,978	95,316,742	84,975,917
Diluted	95,630,066	85,617,851	95,473,859	85,137,833
<b>Comprehensive Income:</b>				
Net income	\$ 41,006	\$ 35,338	\$ 38,676	\$ 26,601
Other comprehensive income (loss):				
Unrealized gain (loss) on interest rate derivative instruments (Note 4)	11,081	(4,695)	12,600	(4,695)
Comprehensive income	52,087	30,643	51,276	21,906
Comprehensive income attributable to noncontrolling interests:				
Noncontrolling interests in consolidated entities	(8)	0	(8)	0
Noncontrolling interests of common units in Operating Partnership (Note 6)	(169)	(114)	(174)	(92)
Comprehensive income attributable to noncontrolling interests	(177)	(114)	(182)	(92)
Comprehensive income attributable to the Company	\$ 51,910	\$ 30,529	\$ 51,094	\$ 21,814

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

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LASALLE HOTEL PROPERTIES  
Consolidated Statements of Equity  
(in thousands, except per share/unit data)  
(unaudited)

	Preferred Shares of Beneficial Interest	Common Shares of Beneficial Interest	Treasury Shares	Additional Paid-In Capital	Accumulated Other Comprehensive Income (Loss)	Distributions in Excess of Retained Earnings	Total Shareholders' Equity	Noncontrolling Interests in Consolidated Entities	Noncontrolling Interests in Common Units in Operating Partnership	Total Noncontrolling Interests	Total Equity
Balance, December 31, 2011	\$ 158	\$ 851	\$ (24,543)	\$ 2,029,145	\$ 0	\$ (239,998)	\$ 1,765,613	\$ 17	\$ 5,613	\$ 5,630	\$ 1,771,243
Issuance of shares, net of offering costs	0	12	22,847	41,412	0	0	64,271	0	0	0	64,271
Redemption of preferred shares	(67)	0	0	(162,266)	0	(4,417)	(166,750)	0	0	0	(166,750)
Repurchase of common shares into treasury	0	0	(738)	0	0	0	(738)	0	0	0	(738)
Options exercised	0	0	0	74	0	0	74	0	0	0	74
Adjustments to issuance of units	0	0	0	0	0	0	0	0	(746)	(746)	(746)
Deferred compensation, net	0	0	2,434	(39)	0	0	2,395	0	0	0	2,395
Adjustments to noncontrolling interests	0	0	0	(778)	0	0	(778)	0	778	778	0
Distributions on issued long-term performance-based share awards	0	0	0	0	0	(56)	(56)	0	0	0	(56)
Distributions on common shares/units (\$0.31 per share/unit)	0	0	0	0	0	(26,710)	(26,710)	0	(92)	(92)	(26,802)
Distributions on preferred shares	0	0	0	0	0	(13,401)	(13,401)	(8)	0	(8)	(13,409)
Net income	0	0	0	0	0	26,493	26,493	0	108	108	26,601
Other comprehensive loss:											
Unrealized loss on interest rate derivative instruments	0	0	0	0	(4,679)	0	(4,679)	0	(16)	(16)	(4,695)
Balance, June 30, 2012	\$ 91	\$ 863	\$ 0	\$ 1,907,548	\$ (4,679)	\$ (258,089)	\$ 1,645,734	\$ 9	\$ 5,645	\$ 5,654	\$ 1,651,388
Balance, December 31, 2012	\$ 91	\$ 955	\$ (886)	\$ 2,118,705	\$ (7,755)	\$ (258,004)	\$ 1,853,126	\$ 18	\$ 5,786	\$ 5,804	\$ 1,858,930
Issuance of shares, net of offering costs	44	7	262	125,862	0	0	126,175	0	0	0	126,175
Redemption of preferred shares	(40)	0	0	(98,394)	0	(1,566)	(100,000)	0	0	0	(100,000)
Repurchase of common shares into treasury	0	0	(2)	0	0	0	(2)	0	0	0	(2)
Deferred compensation, net	0	0	561	2,073	0	0	2,634	0	0	0	2,634
Adjustments to noncontrolling interests	0	0	0	(3)	0	0	(3)	0	3	3	0
Distributions on issued long-term performance-based share awards	0	0	0	0	0	(20)	(20)	0	0	0	(20)
Distributions on common shares/units (\$0.40 per share/unit)	0	0	0	0	0	(38,407)	(38,407)	0	(119)	(119)	(38,526)
Distributions on preferred shares	0	0	0	0	0	(9,172)	(9,172)	(8)	0	(8)	(9,180)
Net income	0	0	0	0	0	38,533	38,533	8	135	143	38,676
Other comprehensive income:											
Unrealized gain on interest rate derivative instruments	0	0	0	0	12,561	0	12,561	0	39	39	12,600
Balance, June 30, 2013	\$ 95	\$ 962	\$ (65)	\$ 2,148,243	\$ 4,826	\$ (268,636)	\$ 1,885,425	\$ 18	\$ 5,844	\$ 5,862	\$ 1,891,287

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

**LASALLE HOTEL PROPERTIES**  
**Consolidated Statements of Cash Flows**  
*(in thousands)*  
*(unaudited)*

	For the six months ended	
	June 30,	
	2013	2012
<b>Cash flows from operating activities:</b>		
Net income	\$ 38,676	\$ 26,601
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	66,548	61,431
Amortization of deferred financing costs, mortgage premium and note receivable discount	(104)	791
Deferred compensation	2,634	2,395
Deferred income tax (benefit) expense	(687)	1,503
Allowance for doubtful accounts	185	136
Other	449	0
Changes in assets and liabilities:		
Restricted cash reserves	765	(846)
Hotel receivables	(13,398)	(12,932)
Prepaid expenses and other assets	(14,739)	(3,208)
Accounts payable and accrued expenses	8,903	10,881
Advance deposits	7,238	6,348
Accrued interest	(470)	(279)
Net cash provided by operating activities	<u>96,000</u>	<u>92,821</u>
<b>Cash flows from investing activities:</b>		
Improvements and additions to properties	(56,781)	(36,103)
Acquisition of properties	(3,000)	(142,944)
Purchase of office furniture and equipment	(32)	(59)
Restricted cash reserves	883	570
Property insurance proceeds	161	0
Net cash used in investing activities	<u>(58,769)</u>	<u>(178,536)</u>
<b>Cash flows from financing activities:</b>		
Borrowings under credit facilities	172,882	275,480
Repayments under credit facilities	(145,882)	(160,071)
Borrowings on term loans	0	177,500
Repayments of mortgage loans	(62,402)	(62,063)
Payment of deferred financing costs	(4)	(1,987)
Purchase of treasury shares	(2)	(738)
Proceeds from exercise of stock options	0	74
Proceeds from issuance of preferred shares	110,000	0
Payment of preferred offering costs	(3,648)	0
Proceeds from issuance of common shares	19,943	64,702
Payment of common offering costs	(521)	(888)
Distributions on issued long-term performance-based share awards	(20)	(56)
Redemption of preferred shares	(100,000)	(166,750)
Distributions on preferred shares	(9,239)	(16,645)
Distributions on common shares/units	(38,315)	(18,702)
Net cash (used in) provided by financing activities	<u>(57,208)</u>	<u>89,856</u>
Net change in cash and cash equivalents	(19,977)	4,141
Cash and cash equivalents, beginning of period	35,090	20,225
Cash and cash equivalents, end of period	<u>\$ 15,113</u>	<u>\$ 24,366</u>

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

**LASALLE HOTEL PROPERTIES**  
**Notes to Consolidated Financial Statements**  
*(in thousands, except share/unit data)*  
*(unaudited)*

**1. Organization**

LaSalle Hotel Properties (the "Company"), a Maryland real estate investment trust organized on January 15, 1998, primarily buys, owns, redevelops and leases upscale and luxury full-service hotels located in convention, resort and major urban business markets. The Company is a self-administered and self-managed real estate investment trust ("REIT") as defined in the Internal Revenue Code of 1986, as amended (the "Code"). As a REIT, the Company is generally not subject to federal corporate income tax on that portion of its net income that is currently distributed to its shareholders. The income of LaSalle Hotel Lessee, Inc. (together with its wholly owned subsidiaries, "LHL"), the Company's wholly owned taxable REIT subsidiary ("TRS"), is subject to taxation at normal corporate rates.

As of June 30, 2013, the Company owned interests in 40 hotels with over 10,600 guest rooms located in nine states and the District of Columbia. Each hotel is leased to LHL (see Note 8) under a participating lease that provides for rental payments equal to the greater of (i) a base rent or (ii) a participating rent based on hotel revenues. The LHL leases expire between December 2013 and December 2015. Lease revenue from LHL is eliminated in consolidation. A third-party non-affiliated hotel operator manages each hotel pursuant to a hotel management agreement.

Substantially all of the Company's assets are held directly or indirectly by, and all of its operations are conducted through, LaSalle Hotel Operating Partnership, LP (the "Operating Partnership"). The Company is the sole general partner of the Operating Partnership. The Company owned, through a combination of direct and indirect interests, 99.7% of the common units of the Operating Partnership at June 30, 2013. The remaining 0.3% is held by limited partners who held 296,300 common units of the Operating Partnership at June 30, 2013. See Note 6 for additional disclosures on common operating partnership units.

**2. Summary of Significant Accounting Policies**

The accompanying unaudited interim consolidated financial statements and related notes have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP") and in conformity with the rules and regulations of the Securities and Exchange Commission ("SEC") applicable to interim financial information. As such, certain information and disclosures normally included in financial statements prepared in accordance with GAAP have been omitted in accordance with the rules and regulations of the SEC. These unaudited consolidated financial statements, in the opinion of management, include all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation of the consolidated balance sheets, consolidated statements of operations and comprehensive income (loss), consolidated statements of equity and consolidated statements of cash flows for the periods presented. Operating results for the three and six months ended June 30, 2013 are not necessarily indicative of the results that may be expected for the year ending December 31, 2013 due to seasonal and other factors. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and accompanying notes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

***Basis of Presentation***

The consolidated financial statements include the accounts of the Company, the Operating Partnership, LHL and their subsidiaries in which they have a controlling interest, including joint ventures. All significant intercompany balances and transactions have been eliminated.

***Use of Estimates***

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

Substantially all of the Company's revenues and expenses are generated by the operations of the individual hotels. The Company records revenues and expenses that are estimated by the hotel operators to produce quarterly financial statements because the management contracts do not require the hotel operators to submit actual results within a time frame that permits the Company to use actual results when preparing its Quarterly Reports on Form 10-Q for filing by the deadline prescribed by the SEC. Generally, the Company records actual revenue and expense amounts for the first two months of each quarter and revenue and expense estimates for the last month of each quarter. Each quarter, the Company reviews the estimated revenue and expense amounts provided by the hotel operators for reasonableness based upon historical results for prior periods and internal Company forecasts.



The Company records any differences between recorded estimated amounts and actual amounts in the following quarter; historically, these differences have not been material. The Company believes the quarterly revenues and expenses, recorded on the Company's consolidated statements of operations and comprehensive income (loss) based on an aggregate estimate, are fairly stated.

#### *Share-Based Compensation*

From time to time, the Company awards nonvested shares under the 2009 Equity Incentive Plan ("2009 Plan"), which has approximately six years remaining, as compensation to officers, employees and non-employee trustees (see Note 7). The shares issued to officers and employees vest over three to nine years. The Company generally recognizes compensation expense for nonvested shares on a straight-line basis over the vesting period based upon the fair market value of the shares on the date of issuance, adjusted for forfeitures.

#### *Noncontrolling Interests*

The Company's financial statements include entities in which the Company has a controlling financial interest. Noncontrolling interest is the portion of equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent. Such noncontrolling interests are reported on the consolidated balance sheets within equity, separately from the Company's equity. On the consolidated statements of operations and comprehensive income (loss), revenues, expenses and net income or loss from less-than-wholly-owned subsidiaries are reported at the consolidated amounts, including both the amounts attributable to the Company and noncontrolling interests. Income or loss is allocated to noncontrolling interests based on their weighted average ownership percentage for the applicable period. Consolidated statements of equity include beginning balances, activity for the period and ending balances for shareholders' equity, noncontrolling interests and total equity.

However, the Company's securities that are redeemable for cash or other assets at the option of the holder, not solely within the control of the issuer, must be classified outside of permanent equity. The Company makes this determination based on terms in applicable agreements, specifically in relation to redemption provisions. Additionally, with respect to noncontrolling interests for which the Company has a choice to settle the contract by delivery of its own shares, the Company evaluates whether the Company controls the actions or events necessary to issue the maximum number of shares that could be required to be delivered under share settlement of the contract.

As of June 30, 2013, the consolidated results of the Company include the following ownership interests held by owners other than the Company: (i) the common units in the Operating Partnership held by third parties, (ii) the outside preferred ownership interests in a subsidiary and (iii) the outside ownership interest in a joint venture.

#### *Notes Receivable*

Notes receivable are carried at cost, net of any premiums or discounts which are recognized as an adjustment of yield over the remaining life of the note using the effective interest method. Interest income is recorded on the accrual basis consistent with the terms of the notes receivable. A note is deemed to be impaired when, based on current information and events, it is probable that the Company will be unable to collect all principal and interest contractually due. Interest previously accrued but not collected becomes part of the Company's recorded investment in the note receivable for purposes of assessing impairment. The Company applies interest payments received on non-accrual notes receivable first to accrued interest and then as interest income. Notes receivable return to accrual status when contractually current and the collection of future payments is reasonably assured.

### **3. Investment in Hotel Properties**

Investment in hotel properties as of June 30, 2013 and December 31, 2012 consists of the following:

	<u>June 30, 2013</u>	<u>December 31, 2012</u>
Land	\$ 480,705	\$ 480,705
Buildings and improvements	2,944,566	2,932,532
Furniture, fixtures and equipment	511,197	472,052
Investment in hotel properties, gross	<u>3,936,468</u>	<u>3,885,289</u>
Accumulated depreciation	(898,545)	(832,245)
Investment in hotel properties, net	<u>\$ 3,037,923</u>	<u>\$ 3,053,044</u>

Depreciation expense was \$33,322 and \$66,333 for the three and six months ended June 30, 2013, respectively, and \$31,135 and \$61,147 for the three and six months ended June 30, 2012, respectively.

In connection with the acquisition of Hotel Palomar, Washington, DC on March 8, 2012, the Company incurred acquisition transaction costs of zero and \$3,594 that were expensed as incurred during the three and six months ended June 30, 2012, respectively, which expenses are included in the accompanying consolidated statements of operations and comprehensive income.

During the first quarter of 2012, the Company finalized its determination of fair value of the real estate assets acquired of Park Central Hotel, upon receiving certain valuation-related information. The final determination resulted in a decrease of \$746 to investment in hotel properties and noncontrolling interests of common units in Operating Partnership.

In connection with the acquisition of Viceroy Santa Monica on March 16, 2011, the Company incurred acquisition transaction costs of \$100 during the three and six months ended June 30, 2012 related to the finalization of acquisition accounting, which expenses are included in the accompanying consolidated statements of operations and comprehensive income.

In connection with the acquisition of the mezzanine loan secured by pledges of ownership interests of the entities that own the underlying hotel properties, Shutters on the Beach and Casa Del Mar, in Santa Monica, CA, on July 13, 2012, the Company incurred acquisition transaction costs of \$207 during the three and six months ended June 30, 2012, which expenses are included in the accompanying consolidated statements of operations and comprehensive income.

**Condensed Pro Forma Financial Information**

The results of operations of acquired properties are included in the consolidated statements of operations and comprehensive income beginning on their respective acquisition dates. The following unaudited condensed pro forma financial information is presented as if the following 2012 acquisitions had been consummated prior to January 1, 2011, the beginning of the reporting period prior to acquisition. In addition, for purposes of the unaudited condensed pro forma financial information only, the February 1, 2012 through February 14, 2012 issuance of 1,714,939 common shares of beneficial interest, the May 18, 2012 through May 30, 2012 issuance of 641,069 common shares of beneficial interest, the August 8, 2012 issuance of 3,100 common shares of beneficial interest and the December 19, 2012 issuance of 9,200,000 shares of beneficial interest are presented as if the issuances had occurred as of January 1, 2011. No adjustments have been made to the unaudited condensed pro forma financial information presented below for the 2012 preferred share redemptions or the 2013 preferred share issuance and redemption, since those transactions have no relation to the 2012 acquisitions. The unaudited condensed pro forma financial information is for comparative purposes only and not necessarily indicative of what actual results of operations of the Company would have been had the 2012 acquisitions been consummated prior to January 1, 2011, nor does it purport to represent the results of operations for future periods. The unaudited condensed pro forma financial information has not been adjusted for property sales.

Adjustments have been made to the unaudited pro forma financial information for the following acquisitions:

Property	Acquisition Date
Hotel Palomar, Washington, DC	March 8, 2012
L'Auberge Del Mar	December 6, 2012
The Liberty Hotel	December 28, 2012

The unaudited condensed pro forma financial information for the three and six months ended June 30, 2012 is as follows:

	For the three months ended June 30, 2012 (unaudited)	For the six months ended June 30, 2012 (unaudited)
Total revenues	\$ 258,510	\$ 447,265
Net income	\$ 37,158	\$ 28,016
Net income attributable to common shareholders	\$ 26,612	\$ 10,090
Earnings per common share - basic	\$ 0.28	\$ 0.10
Earnings per common share - diluted	\$ 0.28	\$ 0.10
Weighted average number of common shares outstanding:		
Basic	95,043,286	95,040,678
Diluted	95,209,159	95,202,595

#### 4. Long-Term Debt

##### Debt Summary

Debt as of June 30, 2013 and December 31, 2012 consisted of the following:

Debt	Interest Rate	Maturity Date	Balance Outstanding as of	
			June 30, 2013	December 31, 2012
<b>Credit facilities</b>				
Senior unsecured credit facility	Floating <sup>(a)</sup>	January 2016 <sup>(a)</sup>	\$ 180,000	\$ 153,000
LHL unsecured credit facility	Floating <sup>(b)</sup>	January 2016 <sup>(b)</sup>	0	0
Total borrowings under credit facilities			180,000	153,000
<b>Term loans</b>				
First Term Loan	Floating <sup>(c)</sup>	May 2019	177,500	177,500
Second Term Loan	Floating <sup>(c)</sup>	August 2017	300,000	300,000
Total term loans			477,500	477,500
<b>Massport Bonds</b>				
Hyatt Boston Harbor (taxable)	Floating <sup>(d)</sup>	March 2018	5,400	5,400
Hyatt Boston Harbor (tax exempt)	Floating <sup>(d)</sup>	March 2018	37,100	37,100
Total bonds payable			42,500	42,500
<b>Mortgage loans</b>				
Hotel Solamar	5.49%	December 2013 <sup>(e)</sup>	0	60,134
Hotel Deca	6.28%	August 2014 <sup>(f)</sup>	8,961	9,111
Westin Copley Place	5.28%	September 2015	210,000	210,000
Westin Michigan Avenue	5.75%	April 2016	136,246	137,172
Indianapolis Marriott Downtown	5.99%	July 2016	99,510	100,142
Hotel Roger Williams	6.31%	August 2016	61,983	62,543
Mortgage loans at stated value			516,700	579,102
Unamortized loan premium <sup>(g)</sup>			82	118
Total mortgage loans			516,782	579,220
Total debt			\$ 1,216,782	\$ 1,252,220

<sup>(a)</sup> Borrowings bear interest at floating rates equal to, at the Company's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. As of June 30, 2013, the rate, including the applicable margin, for the Company's outstanding LIBOR borrowings of \$180,000 was 1.95%. As of December 31, 2012, the rate, including the applicable margin, for the Company's outstanding LIBOR borrowing of \$153,000 was 2.22%. The Company has the option, pursuant to certain terms and conditions, to extend the maturity date to January 2017.

<sup>(b)</sup> Borrowings bear interest at floating rates equal to, at LHL's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. There were no borrowings outstanding at June 30, 2013 or December 31, 2012. LHL has the option, subject to certain terms and conditions, to extend the maturity date to January 2017.

<sup>(c)</sup> Term loans bear interest at floating rates equal to LIBOR plus an applicable margin. The Company entered into separate interest rate swap agreements for the full seven-year term of the First Term Loan (as defined below) and the full five-year term, including a one-year extension subject to certain conditions, of the Second Term Loan (as defined below), resulting in fixed all-in interest rates at June 30, 2013 of 3.62% and 2.43%, respectively, and at December 31, 2012 of 3.87% and 2.68%, respectively, at the Company's current leverage ratio (as defined in the swap agreements).

<sup>(d)</sup> The Massport Bonds are secured by letters of credit issued by the Royal Bank of Scotland that expire in February 2014, pursuant to an amendment to the agreement governing the letters of credit. The Royal Bank of Scotland letters of credit also have three one-year extension options and are secured by the Hyatt Boston Harbor (formerly the Harborside Hyatt Conference Center & Hotel). The bonds bear interest based on weekly floating rates. The interest rates as of June 30, 2013 were 0.70% and 0.10% for the \$5,400 and \$37,100 bonds, respectively. The interest rates as of December 31, 2012 were 0.65% and 0.17% for the \$5,400 and \$37,100 bonds, respectively. The Company also incurs an annual letter of credit fee of a variable rate based on an applicable margin as defined in the Company's senior unsecured credit agreement.

- (e) The Company repaid the mortgage loan on June 3, 2013 through borrowings on its senior unsecured credit facility.
- (f) The Company intends to repay the mortgage loan through borrowings on its credit facilities upon maturity.
- (g) Mortgage debt includes an unamortized loan premium on the mortgage loan on Hotel Deca of \$82 as of June 30, 2013 and \$118 as of December 31, 2012.

A summary of the Company's interest expense and weighted average interest rates for variable rate debt for the three and six months ended June 30, 2013 and 2012 is as follows:

	For the three months ended		For the six months ended	
	June 30,		June 30,	
	2013	2012	2013	2012
Interest Expense:				
Interest incurred	\$ 13,444	\$ 12,104	\$ 27,071	\$ 23,685
Amortization of deferred financing costs	576	432	1,140	828
Capitalized interest	(257)	(33)	(431)	(232)
Interest expense	<u>\$ 13,763</u>	<u>\$ 12,503</u>	<u>\$ 27,780</u>	<u>\$ 24,281</u>
Weighted Average Interest Rates for Variable Rate Debt:				
Senior unsecured credit facility	<u>2.1%</u>	<u>2.1%</u>	<u>2.1%</u>	<u>2.1%</u>
LHL unsecured credit facility	<u>2.1%</u>	<u>2.0%</u>	<u>2.1%</u>	<u>2.0%</u>
Massport Bonds	<u>0.3%</u>	<u>0.3%</u>	<u>0.2%</u>	<u>0.3%</u>

#### Credit Facilities

The Company has a \$750,000 senior unsecured credit facility with a syndicate of banks. The credit facility matures on January 30, 2016, subject to a one-year extension that the Company may exercise at its option, pursuant to certain terms and conditions, including payment of an extension fee. The credit facility includes an accordion feature which, subject to certain conditions, entitles the Company to request additional lender commitments, allowing for total commitments up to \$1,000,000. Borrowings under the credit facility bear interest at floating rates equal to, at the Company's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. Additionally, the Company is required to pay a variable unused commitment fee of 0.30% or 0.40% of the unused portion of the credit facility, depending on the average daily unused portion of the credit facility.

LHL has a \$25,000 unsecured revolving credit facility to be used for working capital and general lessee corporate purposes. The LHL credit facility matures on January 30, 2016, subject to a one-year extension that LHL may exercise at its option, pursuant to certain terms and conditions, including payment of an extension fee. Borrowings under the LHL credit facility bear interest at floating rates equal to, at LHL's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. Additionally, LHL is required to pay a variable unused commitment fee of 0.30% or 0.40% of the unused portion of the credit facility, depending on the average daily unused portion of the LHL credit facility.

The Company's senior unsecured credit facility and LHL's unsecured credit facility contain certain financial covenants relating to net worth requirements, debt ratios and fixed charge coverage and other limitations that restrict the Company's ability to make distributions or other payments to its shareholders upon events of default.

#### Term Loans

On May 16, 2012, the Company entered into a \$177,500 unsecured loan with a seven-year term maturing on May 16, 2019 (the "First Term Loan"). The First Term Loan bears interest at a variable rate, but was hedged to a fixed interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 3.62% at June 30, 2013, for the full seven-year term (see "Derivative and Hedging Activities" below).

On August 2, 2012, the Company entered into a \$300,000 unsecured loan with a five-year term maturing on August 2, 2017, including a one-year extension subject to certain conditions (the "Second Term Loan"). The Second Term Loan bears interest at a variable rate, but was hedged to a fixed interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 2.43% at June 30, 2013, for the full five-year term (see "Derivative and Hedging Activities below").

The Company's term loans contain certain financial covenants relating to net worth requirements, debt ratios and fixed charge coverage and other limitations that restrict the Company's ability to make distributions or other payments to its shareholders upon events of default.

*Derivative and Hedging Activities*

The Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. Unrealized gains and losses on the effective portion of hedging instruments are reported in other comprehensive income (loss) ("OCI"). Ineffective portions of changes in the fair value of a cash flow hedge are recognized as interest expense. Amounts reported in accumulated other comprehensive income (loss) ("AOCI") related to currently outstanding derivatives are recognized as an adjustment to income (loss) as interest payments are made on the Company's variable rate debt. Effective May 16, 2012, the Company entered into three interest rate swap agreements with an aggregate notional amount of \$177,500 for the First Term Loan's full seven-year term, resulting in a fixed all-in interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 3.62% at June 30, 2013. Effective August 2, 2012, the Company entered into five interest rate swap agreements with an aggregate notional amount of \$300,000 for the Second Term Loan's full five-year term, including a one-year extension subject to certain conditions, resulting in a fixed all-in interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 2.43% at June 30, 2013. The Company has designated its pay-fixed, receive-floating interest rate swap derivatives as cash flow hedges.

The following tables present the effect of derivative instruments on the Company's consolidated statements of operations and comprehensive income, including the location and amount of unrealized gain (loss) on outstanding derivative instruments in cash flow hedging relationships, for the three and six months ended June 30, 2013 and 2012:

	Amount of Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)		Location of Loss Reclassified from AOCI into Income (Effective Portion)	Amount of Loss Reclassified from AOCI into Income (Effective Portion)	
	For the three months ended June 30,			For the three months ended June 30,	
	2013	2012		2013	2012
Derivatives in cash flow hedging relationships:					
Interest rate swaps	\$ 11,081	\$ (4,695)	Interest expense	\$ 1,049	\$ 302

	Amount of Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)		Location of Loss Reclassified from AOCI into Income (Effective Portion)	Amount of Loss Reclassified from AOCI into Income (Effective Portion)	
	For the six months ended June 30,			For the six months ended June 30,	
	2013	2012		2013	2012
Derivatives in cash flow hedging relationships:					
Interest rate swaps	\$ 12,600	\$ (4,695)	Interest expense	\$ 2,081	\$ 302

During the three and six months ended June 30, 2013 and 2012, the Company did not have any hedge ineffectiveness or amounts that were excluded from the assessment of hedge effectiveness recorded in earnings.

As of June 30, 2013, there was \$4,841 in cumulative unrealized gain, of which \$4,826 was included in AOCI and \$15 was attributable to noncontrolling interests. As of December 31, 2012, there was \$7,759 in cumulative unrealized loss, of which \$7,735 was included in AOCI and \$24 was attributable to noncontrolling interests. The Company expects that approximately \$4,223 will be reclassified from AOCI and noncontrolling interests and recognized as a reduction to income in the next 12 months, calculated as estimated interest expense using the interest rates on the derivative instruments as of June 30, 2013.

*Mortgage Loans*

The Company's mortgage loans are secured by the respective properties. The mortgages are non-recourse to the Company except for fraud or misapplication of funds.

On June 3, 2013, the Company repaid without fee or penalty the Hotel Solamar mortgage loan in the amount of \$59,789 plus accrued interest through borrowings on its senior unsecured credit facility. The loan was due to mature in December 2013.

The mortgage loans contain debt service coverage ratio tests related to the mortgaged properties. If the debt service coverage ratio for a specific property fails to exceed a threshold level specified in the mortgage, cash flows from that hotel may automatically be directed to the lender to (i) satisfy required payments, (ii) fund certain reserves required by the mortgage and (iii) fund additional cash reserves for future required payments, including final payment. Cash flows may be directed to the lender ("cash trap") until such time as the property again complies with the specified debt service coverage ratio or the mortgage is paid off.

### *Financial Covenants*

Failure to comply with our financial covenants contained in our credit facilities, term loans and non-recourse secured mortgages could result from, among other things, changes in our results of operations, the incurrence of additional debt or changes in general economic conditions.

If the Company violates the financial covenants contained in any of its credit facilities or term loans described above, the Company may attempt to negotiate waivers of the violations or amend the terms of the applicable credit facilities or term loans with the lenders thereunder; however, the Company can make no assurance that it would be successful in any such negotiations or that, if successful in obtaining waivers or amendments, such amendments or waivers would be on terms attractive to the Company. If a default under the credit facilities or term loans were to occur, the Company would possibly have to refinance the debt through additional debt financing, private or public offerings of debt securities, or additional equity financings. If the Company is unable to refinance its debt on acceptable terms, including at maturity of the credit facilities and term loans, it may be forced to dispose of hotel properties on disadvantageous terms, potentially resulting in losses that reduce cash flow from operating activities. If, at the time of any refinancing, prevailing interest rates or other factors result in higher interest rates upon refinancing, increases in interest expense would lower the Company's cash flow, and, consequently, cash available for distribution to its shareholders.

A cash trap associated with a mortgage loan may limit the overall liquidity for the Company as cash from the hotel securing such mortgage would not be available for the Company to use. If the Company is unable to meet mortgage payment obligations, including the payment obligation upon maturity of the mortgage borrowing, the mortgage securing the specific property could be foreclosed upon by, or the property could be otherwise transferred to, the mortgagee with a consequent loss of income and asset value to the Company.

As of June 30, 2013, the Company is in compliance with all debt covenants, current on all loan payments and not otherwise in default under the credit facilities, term loans, bonds payable or mortgage loans. One of the mortgaged properties is currently subject to a cash trap as a result of the impact of a recent renovation on hotel operations. This cash trap does not have a material impact on the cash flow or the operations of the property or the Company.

## **5. Commitments and Contingencies**

### *Ground, Land and Building, and Air Rights Leases*

Seven of the Company's hotels, San Diego Paradise Point Resort and Spa, Hyatt Boston Harbor (formerly Harborside Hyatt Conference Center & Hotel), Indianapolis Marriott Downtown, The Hilton San Diego Resort and Spa, Hotel Solamar, Viceroy Santa Monica and The Liberty Hotel are subject to ground leases under non-cancelable operating leases expiring from March 2026 to December 2102. The ground lease at Hyatt Boston Harbor expires in March 2026, but the Company has options to extend for over 50 years to 2077. None of the remaining ground leases expire prior to 2045. The Westin Copley Place is subject to a long term air rights lease which expires in December 2077 and requires no payments through maturity. The ground lease related to the Indianapolis Marriott Downtown requires future ground rent payments of one dollar per year. The ground leases at Viceroy Santa Monica and The Liberty Hotel are subject to minimum annual rent increases, resulting in noncash straight-line rent expense of \$327 and \$654 for the three and six months ended June 30, 2013, respectively, and \$114 and \$228 for the three and six months ended June 30, 2012, respectively, which is included in total ground rent expense below.

Hotel Roger Williams is subject to a capital lease of land and building which expires in December 2044. The fair value of the obligation at acquisition of \$4,892 is amortized and included in accounts payable and accrued expenses in the accompanying consolidated balance sheets.

Total ground rent expense for the three and six months ended June 30, 2013 was \$2,791 and \$5,286, respectively. Total ground rent expense for the three and six months ended June 30, 2012 was \$2,210 and \$3,986, respectively. Certain rent payments are based on the hotel's performance. Actual payments of rent may exceed the minimum required rent due to meeting specified thresholds.

Future minimum rent payments (without reflecting future applicable Consumer Price Index increases) are as follows:

2013	\$	3,525
2014		7,060
2015		7,087
2016		7,140
2017		7,153
Thereafter		362,977
	\$	<u>394,942</u>

***Reserve Funds for Future Capital Expenditures***

Certain of the Company's agreements with its hotel managers, franchisors and lenders have provisions for the Company to provide funds, generally 4.0% to 5.0% of hotel revenues, sufficient to cover the cost of (a) certain non-routine repairs and maintenance to the hotels and (b) replacements and renewals to the hotels' capital assets. Certain of the agreements require that the Company reserve this cash in separate accounts. As of June 30, 2013, \$9,912 was available in restricted cash reserves for future capital expenditures. The Company has sufficient cash on hand and availability on its credit facilities to cover capital expenditures under agreements that do not require that the Company separately reserve cash.

***Restricted Cash Reserves***

At June 30, 2013, the Company held \$15,766 in restricted cash reserves. Included in such amounts are (i) \$9,912 of reserve funds for future capital expenditures, (ii) \$4,378 deposited in mortgage escrow accounts pursuant to mortgage obligations to pre-fund a portion of certain operating expenses and debt payments and (iii) \$1,476 held by insurance and management companies on the Company's behalf to be refunded or applied to future liabilities.

***Litigation***

The nature of hotel operations exposes the Company and its hotels to the risk of claims and litigation in the normal course of their business. The Company is not presently subject to any material litigation nor, to the Company's knowledge, is any litigation threatened against the Company, other than routine actions for negligence or other claims and administrative proceedings arising in the ordinary course of business, some of which are expected to be covered by liability insurance and all of which collectively are not expected to have a material adverse effect on the liquidity, results of operations, business or financial condition of the Company.

**6. Equity**

***Common Shares of Beneficial Interest***

On January 1, 2013, the Company issued 10,332 common shares of beneficial interest and authorized an additional 7,921 deferred shares to the independent members of its Board of Trustees for their earned 2012 compensation pursuant to award arrangements existing on or before January 1, 2012. These common shares of beneficial interest were issued under the 2009 Plan.

On January 30, 2013, the Company issued 81,400 restricted common shares of beneficial interest to the Company's executives and employees. The restricted shares vest over three years, starting January 1, 2014, subject to continued employment. These common shares of beneficial interest were issued under the 2009 Plan.

On February 20, 2013, the Company entered into an equity distribution agreement (the "2013 Agreement") with Raymond James & Associates, Inc. (the "Manager"). Under the terms of the 2013 Agreement, the Company may issue from time to time through or to the Manager, as sales agent or principal, the Company's common shares of beneficial interest with aggregate gross proceeds totaling up to \$250,000. The 2013 Agreement replaced the Company's prior equity distribution agreement, under which \$146,024 of aggregate gross proceeds remained. During the six months ended June 30, 2013, the Company incurred offering costs of \$146 related to executing and maintaining the 2013 Agreement.

From May 24, 2013 through May 31, 2013, the Company sold 721,706 common shares of beneficial interest, par value \$0.01 per share, under the 2013 Agreement. After deducting the Manager's discounts and commissions of \$250, the Company raised net proceeds of \$19,693. The net proceeds were used to pay down amounts outstanding under the Company's senior unsecured credit facility and for general corporate purposes. As of June 30, 2013, the Company had availability under the 2013 Agreement to issue and sell common shares of beneficial interest having an aggregate offering price of up to \$230,057.

### *Common Dividends*

The Company paid the following dividends on common shares/units during the six months ended June 30, 2013:

Dividend per Share/Unit	For the Quarter Ended	Record Date	Payable Date
\$ 0.20	December 31, 2012	December 31, 2012	January 15, 2013
\$ 0.20	March 31, 2013	March 28, 2013	April 15, 2013

### *Treasury Shares*

Treasury shares are accounted for under the cost method. During the six months ended June 30, 2013, the Company received 2,414 common shares of beneficial interest related to employees surrendering shares to pay taxes at the time restricted shares vested and forfeiting restricted shares upon resignation.

On August 29, 2011, the Company's Board of Trustees authorized a share repurchase program (the "Repurchase Program") to acquire up to \$100,000 of the Company's common shares of beneficial interest, with repurchased shares recorded at cost in treasury. As of June 30, 2013, the Company had availability under the Repurchase Program to acquire up to \$75,498 of common shares of beneficial interest. However, the Company is not currently authorized by its Board of Trustees to repurchase or offer to repurchase any common shares. If authorized by its Board of Trustees, the Company may resume using the Repurchase Program on a future date.

During the six months ended June 30, 2013, the Company re-issued 10,332 treasury shares related to earned 2012 compensation for the Board of Trustees and 24,636 treasury shares related to the grants of restricted common shares of beneficial interest.

At June 30, 2013, there were 2,360 common shares of beneficial interest in treasury.

### *Preferred Shares*

On May 21, 2012, the Company redeemed all 3,170,000 outstanding 7 1/2% Series D Cumulative Redeemable Preferred Shares ("Series D Preferred Shares") and all 3,500,000 outstanding 8% Series E Cumulative Redeemable Preferred Shares ("Series E Preferred Shares") for \$79,250 and \$87,500 (\$25.00 per share), respectively, plus accrued distributions through May 21, 2012 of \$842 and \$992, respectively. The redemption values of the Series D Preferred Shares and Series E Preferred Shares exceeded their carrying values by \$2,273 and \$2,144, respectively, which are included in the determination of net income attributable to common shareholders for the three and six months ended June 30, 2012. The \$2,273 and \$2,144 represent the offering costs related to the Series D Preferred Shares and Series E Preferred Shares, respectively.

On March 4, 2013, the Company issued 4,000,000 6 3/8% Series I Cumulative Redeemable Preferred Shares (\$0.01 par value) ("Series I Preferred Shares") at a price of \$25.00 per share and received net proceeds, after costs, of \$96,667. On March 12, 2013, the underwriters exercised their rights to cover overallocments and purchased 400,000 additional Series I Preferred Shares, resulting in additional net proceeds to the Company of \$9,685. The net proceeds were used to redeem a portion of the Company's 7 1/4% Series G Cumulative Redeemable Preferred Shares ("Series G Preferred Shares") on April 5, 2013, to pay down amounts outstanding under the Company's senior unsecured credit facility, and for general corporate purposes.

On April 5, 2013, the Company redeemed 4,000,000 of the 6,348,888 outstanding Series G Preferred Shares for \$100,000 (\$25.00 per share) plus accrued distributions through April 5, 2013 of \$1,913. The redemption value of the Series G Preferred Shares exceeded their carrying value by \$1,566, which is included in the determination of net income attributable to common shareholders for the three and six months ended June 30, 2013. The \$1,566 represents the offering costs related to the redeemed Series G Preferred Shares.

The Series G Preferred Shares, 7 1/2% Series H Cumulative Redeemable Preferred Shares ("Series H Preferred Shares") and the Series I Preferred Shares (collectively, the "Preferred Shares") rank senior to the common shares of beneficial interest and on parity with each other with respect to payment of distributions; the Company will not pay any distributions, or set aside any funds



for the payment of distributions, on its common shares of beneficial interest unless it has also paid (or set aside for payment) the full cumulative distributions on the Preferred Shares for the current and all past dividend periods. The outstanding Preferred Shares do not have any maturity date, and are not subject to mandatory redemption. The difference between the carrying value and the redemption amount of the Preferred Shares are the offering costs. In addition, the Company is not required to set aside funds to redeem the Preferred Shares. The Company currently has the option to redeem the Series G Preferred Shares, in whole or from time to time in part, by payment of \$25.00 per share, plus any accumulated, accrued and unpaid distributions to and including the date of redemption. The Company may not optionally redeem the Series H Preferred Shares and Series I Preferred Shares prior to January 24, 2016 and March 4, 2018, respectively, except in limited circumstances relating to the Company's continuing qualification as a REIT or as discussed below. After those dates, the Company may, at its option, redeem the Series H Preferred Shares and Series I Preferred Shares, in whole or from time to time in part, by payment of \$25.00 per share, plus any accumulated, accrued and unpaid distributions to and including the date of redemption. In addition, upon the occurrence of a change of control (as defined in the Company's charter), the result of which the Company's common shares of beneficial interest and the common securities of the acquiring or surviving entity are not listed on the New York Stock Exchange, the NYSE MKT LLC or the NASDAQ Stock Market, or any successor exchanges, the Company may, at its option, redeem the Series H Preferred Shares and Series I Preferred Shares in whole or in part within 120 days after the change of control occurred, by paying \$25.00 per share, plus any accrued and unpaid distributions to and including the date of redemption. If the Company does not exercise its right to redeem the Series H Preferred Shares and Series I Preferred Shares upon a change of control, the holders of Series H Preferred Shares and Series I Preferred Shares have the right to convert some or all of their shares into a number of the Company's common shares of beneficial interest based on a defined formula subject to a cap of 4,680,500 common shares and 8,835,200 common shares, respectively.

The following Preferred Shares were outstanding as of June 30, 2013:

Security Type	Number of Shares
7 ¼% Series G Preferred Shares	2,348,888
7 ½% Series H Preferred Shares	2,750,000
6 ⅜% Series I Preferred Shares	4,400,000

#### *Preferred Dividends*

The Company paid the following dividends on preferred shares during the six months ended June 30, 2013:

Security Type	Dividend per Share <sup>(1)</sup>	For the Quarter Ended	Record Date	Payable Date
7 ¼% Series G	\$ 0.45	December 31, 2012	January 1, 2013	January 15, 2013
7 ½% Series H	\$ 0.47	December 31, 2012	January 1, 2013	January 15, 2013
7 ¼% Series G (redemption)	\$ 0.48	March 31, 2013	March 28, 2013	April 5, 2013
7 ¼% Series G	\$ 0.45	March 31, 2013	March 28, 2013	April 15, 2013
7 ½% Series H	\$ 0.47	March 31, 2013	March 28, 2013	April 15, 2013
6 ⅜% Series I	\$ 0.18	March 31, 2013	March 28, 2013	April 15, 2013

<sup>(1)</sup> Amounts are rounded to the nearest whole cent for presentation purposes.

#### *Noncontrolling Interests of Common Units in Operating Partnership*

As of June 30, 2013, the Operating Partnership had 296,300 common units of limited partnership interest outstanding, representing a 0.3% partnership interest held by the limited partners. As of June 30, 2013, approximately \$7,319 of cash or the equivalent value in common shares, at the Company's option, would be paid to the limited partners of the Operating Partnership if the partnership were terminated. The approximate value of \$7,319 is based on the Company's closing common share price of \$24.70 on June 30, 2013, which is assumed to be equal to the value provided to the limited partners upon liquidation of the Operating Partnership. The outstanding common units of limited partnership interest are subject to a required hold period that ends on December 28, 2013, after which they are convertible into a like number of common shares of beneficial interest of the Company.

The following schedule presents the effects of changes in the Company's ownership interest in the Operating Partnership on the Company's equity:

	For the six months ended	
	June 30,	
	2013	2012
Net income attributable to common shareholders	\$ 27,795	\$ 8,675
Decrease in additional paid-in capital from adjustments to noncontrolling interests of common units in Operating Partnership	(3)	(778)
Change from net income attributable to common shareholders and adjustments to noncontrolling interests	\$ 27,792	\$ 7,897

## 7. Equity Incentive Plan

The common shareholders approved the 2009 Plan, which permits the Company to issue equity-based awards to executives, employees, non-employee members of the Board of Trustees and any other persons providing services to or for the Company and its subsidiaries. The 2009 Plan provides for a maximum of 1,800,000 common shares of beneficial interest to be issued in the form of share options, share appreciation rights, restricted share awards, performance shares, phantom shares and other equity-based awards. In addition, the maximum number of common shares subject to awards of any combination that may be granted under the 2009 Plan during any fiscal year to any one individual is limited to 500,000 shares. The 2009 Plan terminates on January 28, 2019. The 2009 Plan authorized, among other things: (i) the grant of share options that qualify as incentive options under the Code, (ii) the grant of share options that do not so qualify, (iii) the grant of common shares in lieu of cash for trustees' fees, (iv) grants of common shares in lieu of cash compensation, and (v) the making of loans to acquire common shares in lieu of compensation (to the extent permitted by law and applicable provisions of the Sarbanes Oxley Act of 2002). The exercise price of share options is determined by the Compensation Committee of the Board of Trustees, but may not be less than 100% of the fair value of the common shares on the date of grant. Restricted share awards and options under the 2009 Plan vest over a period determined by the Compensation Committee of the Board of Trustees, generally a three to five year period, with certain awards vesting over periods of up to nine years. The duration of each option is also determined by the Compensation Committee, subject to applicable laws and regulations. There were no stock options outstanding as of June 30, 2013. At June 30, 2013, there were 1,068,681 common shares available for future grant under the 2009 Plan.

### *Service Condition Nonvested Share Awards*

From time to time, the Company awards nonvested shares under the 2009 Plan to members of the Board of Trustees, executives, and employees. The nonvested shares vest over three to nine years based on continued service or employment. The Company measures compensation costs for the nonvested shares based upon the fair value of its common shares at the date of grant. Compensation costs are recognized on a straight-line basis over the vesting period and are included in general and administrative expense in the accompanying consolidated statements of operations and comprehensive income.

A summary of the Company's service condition nonvested shares as of June 30, 2013 is as follows:

	Number of Shares	Weighted - Average Grant Date Fair Value
Nonvested at January 1, 2013	252,772	\$ 29.72
Granted	81,400	27.20
Vested	(165)	27.18
Forfeited	(2,360)	27.34
Nonvested at June 30, 2013 <sup>(1)</sup>	331,647	\$ 29.12

<sup>(1)</sup> Amount excludes 34,318 long-term performance-based shares which were earned but nonvested due to a service condition as of June 30, 2013.

As of June 30, 2013 and December 31, 2012, there were \$6,583 and \$5,919, respectively, of total unrecognized compensation costs related to nonvested share awards. As of June 30, 2013 and December 31, 2012, these costs were expected to be recognized over a weighted-average period of 2.4 and 2.7 years, respectively. The total fair value of shares vested (calculated as number of shares multiplied by vesting date share price) during the three and six months ended June 30, 2013 was zero and \$4, respectively, and during the three and six months ended June 30, 2012 was zero and \$1,635, respectively. The compensation costs (net of forfeitures) that have been included in general and administrative expenses in the accompanying consolidated statements of

operations and comprehensive income were \$710 and \$1,420 for the three and six months ended June 30, 2013, respectively, and \$703 and \$1,392 for the three and six months ended June 30, 2012, respectively.

**Long-Term Performance-Based Share Awards**

On January 30, 2013, the Company's Board of Trustees granted a target of 80,559 performance-based awards of nonvested shares to executives (the "January 30, 2013 Awards"). The actual amounts of the awards with respect to 40,280 of the 80,559 shares will be determined on January 1, 2016, based on the performance measurement period of January 1, 2013 through December 31, 2015, in accordance with the terms of the agreements. The actual amounts of the awards with respect to the remaining 40,279 of the 80,559 shares will be determined on July 1, 2016, based on the performance measurement period of July 1, 2013 through June 30, 2016, in accordance with the terms of the agreements. The actual amounts of the awards will range from 0% to 200% of the target amounts, depending on the performance analysis stipulated in the agreements, and none of the performance shares are outstanding until issued in accordance with award agreements based on performance. After the actual amounts of the awards are determined (or earned) at the end of the respective performance measurement period, all of the earned shares will be issued and outstanding on those dates. The executives will receive cash payments on the earned shares equal to the value of all dividends paid on common shares from the grant date through the respective determination date. Such amounts will be paid to the awardees on or about January 1, 2016 and July 1, 2016, respectively. Thereafter, the executives will be entitled to receive dividends as declared and paid on the earned shares and to vote the shares. Fair value of the January 30, 2013 Awards was estimated on the grant date, January 30, 2013, with revaluation on June 30, 2013 resulting from the return on invested capital (see below) measurement assumption being revised from 100% to 200%, and will be amortized into expense over the respective performance measurement period. With respect to 40,280 shares, amortization commenced on January 30, 2013, the beginning of the requisite service period, and, with respect to 40,279 shares, amortization will commence on July 1, 2013, the beginning of the requisite service period.

The fair values of the performance-based awards were determined by the Company using data under the Monte Carlo valuation method provided by a third-party consultant. The measurement of performance for the 2013 awards is substantially the same as the performance measurement for previously granted long-term performance-based share awards, except for "return on invested capital" discussed below. The capital market assumptions used in the valuations consisted of the following:

- Factors associated with the underlying performance of the Company's share price and shareholder returns over the term of the performance awards including total share return volatility and risk-free interest.
- Factors associated with the relative performance of the Company's share price and shareholder returns when compared to those companies which compose the index including beta as a means to breakdown total volatility into market-related and company specific volatilities.
- The valuation has been performed in a risk-neutral framework.
- Return on invested capital is a performance condition award measurement. The estimated value was calculated based on the initial face value at the date of grant. The valuation will be adjusted on a periodic basis as the estimated number of awards expected to vest is revised.

The assumptions used were as follows for each performance measure:

	Volatility	Interest Rates	Dividend Yield	Stock Beta	Fair Value of Components of Award	Weighting of Total Awards
<b>January 30, 2013 Awards (performance period starting January 1, 2013)</b>						
Target amounts	38.70%	0.42%	N/A	N/A	\$ 29.38	33.40%
Return on invested capital	N/A	N/A	N/A	N/A	\$ 27.20	33.30%
Peer companies	38.70%	0.42%	N/A	0.864	\$ 30.51	33.30%
<b>January 30, 2013 Awards (performance period starting July 1, 2013)</b>						
Target amounts	38.70%	0.42%	N/A	N/A	\$ 27.70	33.40%
Return on invested capital	N/A	N/A	N/A	N/A	\$ 27.20	33.30%
Peer companies	38.70%	0.42%	N/A	0.864	\$ 31.34	33.30%

A summary of the Company's long-term performance-based share awards as of June 30, 2013 is as follows:

	Number of Shares	Weighted- Average Grant Date Fair Value
Nonvested at January 1, 2013	208,986	\$ 34.61
Granted <sup>(2)</sup>	40,280	29.03
Vested	0	0.00
Forfeited	0	0.00
Nonvested at June 30, 2013 <sup>(1)(2)</sup>	249,266	\$ 33.71

(1) Amount excludes 50,000 shares that have been committed for future performance share grants. Fair value will be estimated at the beginning of the performance measurement period on July 1, 2014.

(2) Amount excludes 40,279 shares awarded on January 30, 2013 for which fair value has been estimated, but amortization into expense has not yet commenced. Amortization of fair value into expense will commence at the beginning of the requisite service period on July 1, 2013.

As of June 30, 2013 and December 31, 2012, there were \$5,204 and \$4,883, respectively, of total unrecognized compensation costs related to long-term performance-based share awards. As of June 30, 2013 and December 31, 2012, these costs were expected to be recognized over a weighted-average period of 2.4 and 2.6 years, respectively. As of June 30, 2013 and December 31, 2012, there were 153,943 long-term performance-based share awards vested. Additionally, there were 34,318 long-term performance-based awards earned but nonvested due to a service condition as of June 30, 2013 and December 31, 2012. The compensation costs (net of forfeitures) related to long-term performance-based share awards that have been included in general and administrative expenses in the accompanying consolidated statements of operations and comprehensive income were \$637 and \$1,214 for the three and six months ended June 30, 2013, respectively, and \$501 and \$1,003 for the three and six months ended June 30, 2012, respectively.

## 8. LHL

Substantially all of the Company's revenues are derived from operating revenues generated by the hotels, all of which are leased by LHL.

Other indirect hotel operating expenses consist of the following expenses incurred by the hotels:

	For the three months ended		For the six months ended	
	June 30,		June 30,	
	2013	2012	2013	2012
General and administrative	\$ 18,594	\$ 17,294	\$ 36,321	\$ 32,771
Sales and marketing	13,992	13,119	27,393	25,140
Repairs and maintenance	8,043	7,823	16,217	15,410
Utilities and insurance	6,582	6,350	13,561	12,664
Management and incentive fees	9,500	8,457	14,908	13,104
Franchise fees	2,148	1,772	3,839	3,340
Other expenses	330	337	685	764
Total other indirect expenses	\$ 59,189	\$ 55,152	\$ 112,924	\$ 103,193

As of June 30, 2013, LHL leased all 40 hotels owned by the Company as follows:

- |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ol style="list-style-type: none"> <li>1. Hyatt Boston Harbor (formerly Harborside Hyatt Conference Center &amp; Hotel)</li> <li>2. Hotel Viking</li> <li>3. Topaz Hotel</li> <li>4. Hotel Rouge</li> <li>5. Hotel Madera</li> <li>6. Hotel Helix</li> <li>7. The Liaison Capitol Hill</li> <li>8. Lansdowne Resort</li> <li>9. Hotel George</li> <li>10. Indianapolis Marriott Downtown</li> <li>11. Hilton Alexandria Old Town</li> <li>12. Chaminade Resort and Conference Center</li> <li>13. Hilton San Diego Gaslamp Quarter</li> <li>14. The Grafton on Sunset</li> <li>15. Onyx Hotel</li> <li>16. Westin Copley Place</li> <li>17. Hotel Deca</li> <li>18. The Hilton San Diego Resort and Spa</li> <li>19. Donovan House</li> <li>20. Le Parc Suite Hotel</li> </ol> | <ol style="list-style-type: none"> <li>21. Westin Michigan Avenue</li> <li>22. Hotel Sax Chicago</li> <li>23. Alexis Hotel</li> <li>24. Hotel Solamar</li> <li>25. Gild Hall</li> <li>26. Hotel Amarano Burbank</li> <li>27. San Diego Paradise Point Resort and Spa</li> <li>28. Le Montrose Suite Hotel</li> <li>29. Sofitel Washington, DC Lafayette Square</li> <li>30. Hotel Monaco San Francisco</li> <li>31. Westin Philadelphia</li> <li>32. Embassy Suites Philadelphia - Center City</li> <li>33. Hotel Roger Williams</li> <li>34. Chamberlain West Hollywood</li> <li>35. Viceroy Santa Monica</li> <li>36. Villa Florence</li> <li>37. Park Central Hotel</li> <li>38. Hotel Palomar, Washington, DC</li> <li>39. L'Auberge Del Mar</li> <li>40. The Liberty Hotel</li> </ol> |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

**9. Income Taxes**

Income tax expense (benefit) was comprised of the following for the three and six months ended June 30, 2013 and 2012:

	For the three months ended		For the six months ended	
	June 30,		June 30,	
	2013	2012	2013	2012
LHL's income tax expense (benefit)	\$ 4,615	\$ 5,434	\$ (645)	\$ 2,267
Operating Partnership's income tax expense (benefit)	319	(465)	562	(290)
Total income tax expense (benefit)	<u>\$ 4,934</u>	<u>\$ 4,969</u>	<u>\$ (83)</u>	<u>\$ 1,977</u>

The Company has estimated LHL's income tax benefit for the six months ended June 30, 2013 by applying an estimated combined federal and state tax rate of 38.2% to LHL's net loss of \$1,796. From time to time, the Company may be subject to federal, state or local tax audits in the normal course of business.

**10. Fair Value Measurements**

In evaluating fair value, GAAP outlines a valuation framework and creates a fair value hierarchy that distinguishes between market assumptions based on market data (observable inputs) and a reporting entity's own assumptions about market data (unobservable inputs). The hierarchy ranks the quality and reliability of inputs used to determine fair value, which are then classified and disclosed in one of the three categories. The three levels are as follows:

Level 1—Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

Level 2—Observable inputs, other than quoted prices included in level 1, such as interest rates, yield curves, quoted prices in active markets for similar assets and liabilities, and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3—Unobservable inputs that are supported by limited market activity. This includes certain pricing models, discounted cash flow methodologies and similar techniques when observable inputs are not available.

The Company estimates the fair value of its financial instruments using available market information and valuation methodologies the Company believes to be appropriate for these purposes. Considerable judgment and subjectivity are involved in developing these estimates and, accordingly, such estimates are not necessarily indicative of amounts that would be realized upon disposition.

*Recurring Measurements*

For assets and liabilities measured at fair value on a recurring basis, quantitative disclosure of their fair value is as follows:

Description	Consolidated Balance Sheet Location	Fair Value Measurements at	
		June 30, 2013	December 31, 2012
		Using Significant Other Observable Inputs (Level 2)	
Derivative interest rate instruments	Prepaid expenses and other assets	\$ 4,841	\$ 0
Derivative interest rate instruments	Accounts payable and accrued expenses	\$ 0	\$ 7,759

The fair value of each derivative instrument is based on a discounted cash flow analysis of the expected cash flows under each arrangement. This analysis reflects the contractual terms of the derivative instrument, including the period to maturity, and utilizes observable market-based inputs, including interest rate curves and implied volatilities, which is classified within level 2 of the fair value hierarchy. The Company also incorporates credit value adjustments to appropriately reflect each parties' nonperformance risk in the fair value measurement, which utilizes level 3 inputs such as estimates of current credit spreads. However, the Company has assessed that the credit valuation adjustments are not significant to the overall valuation of the derivatives. As a result, the Company has determined that its derivative valuations in their entirety are classified within level 2 of the fair value hierarchy.

*Financial Instruments Not Measured at Fair Value*

The following table represents the fair value, derived using level 2 inputs, of financial instruments presented at carrying value in the Company's consolidated financial statements as of June 30, 2013 and December 31, 2012:

	June 30, 2013		December 31, 2012	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Note receivable	\$ 69,698	\$ 69,698	\$ 68,490	\$ 68,490
Borrowings under credit facilities	\$ 180,000	\$ 179,535	\$ 153,000	\$ 153,719
Term loans	\$ 477,500	\$ 470,438	\$ 477,500	\$ 475,752
Bonds payable	\$ 42,500	\$ 42,500	\$ 42,500	\$ 42,500
Mortgage loans	\$ 516,782	\$ 536,513	\$ 579,220	\$ 607,109

The Company estimates the fair value of its borrowings under credit facilities, term loans, bonds payable and mortgage loans using a weighted average effective interest rate of 2.9% as of June 30, 2013 and December 31, 2012. The assumptions reflect the terms currently available on similar borrowings to borrowers with credit profiles similar to the Company's. The Company estimates that the fair value of its note receivable approximates its carrying value due to the relatively short period until maturity.

At June 30, 2013 and December 31, 2012, the carrying amounts of certain of the Company's financial instruments, including cash and cash equivalents, restricted cash, accounts receivable and accounts payable and accrued expenses were representative of their fair values due to the short-term nature of these instruments and the recent acquisition of these items.

**11. Earnings Per Common Share**

The limited partners' outstanding common units in the Operating Partnership (which may be converted to common shares of beneficial interest) have been excluded from the diluted earnings per share calculation as there would be no effect on the amounts since the limited partners' share of income or loss would also be added back to net income or loss. Any anti-dilutive shares have been excluded from the diluted earnings per share calculation. Unvested share-based payment awards that contain nonforfeitable 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. Accordingly, distributed and undistributed earnings attributable to unvested restricted shares (participating securities) have been excluded, as applicable, from net income or loss attributable to

common shareholders used in the basic and diluted earnings per share calculations. Net income or loss figures are presented net of noncontrolling interests in the earnings per share calculations.

The computation of basic and diluted earnings per common share is as follows:

	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
<b>Numerator:</b>				
Net income attributable to common shareholders	\$ 35,190	\$ 24,792	\$ 27,795	\$ 8,675
Dividends paid on unvested restricted shares	(73)	(87)	(147)	(135)
Undistributed earnings attributable to unvested restricted shares	(61)	(38)	0	0
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	<u>\$ 35,056</u>	<u>\$ 24,667</u>	<u>\$ 27,648</u>	<u>\$ 8,540</u>
<b>Denominator:</b>				
Weighted average number of common shares - basic	95,465,464	85,451,978	95,316,742	84,975,917
Effect of dilutive securities:				
Stock options and compensation-related shares	164,602	165,873	157,117	161,916
Weighted average number of common shares - diluted	<u>95,630,066</u>	<u>85,617,851</u>	<u>95,473,859</u>	<u>85,137,833</u>
<b>Earnings per Common Share - Basic:</b>				
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	<u>\$ 0.37</u>	<u>\$ 0.29</u>	<u>\$ 0.29</u>	<u>\$ 0.10</u>
<b>Earnings per Common Share - Diluted:</b>				
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	<u>\$ 0.37</u>	<u>\$ 0.29</u>	<u>\$ 0.29</u>	<u>\$ 0.10</u>

12. Supplemental Information to Statements of Cash Flows

	For the six months ended June 30,	
	2013	2012
Interest paid, net of capitalized interest	\$ 27,110	\$ 23,732
Interest capitalized	431	232
Income taxes paid, net	1,317	1,189
Increase in distributions payable on common shares	162	8,066
Decrease in distributions payable on preferred shares	(59)	(3,236)
Write-off of fully amortized deferred financing costs	203	162
Increase (decrease) in accrued capital expenditures	4,090	(1,007)
Grant of restricted shares and awards to employees and executives, net	3,749	4,744
Issuance of common shares for Board of Trustees compensation	277	494
In conjunction with the acquisition of properties, the Company assumed assets and liabilities as follows:		
Investment in properties (after credits at closing)	\$ 0	\$ (143,721)
Deposits on potential acquisitions	(3,000)	0
Other assets	0	(565)
Liabilities	0	1,342
Acquisition of properties	<u>\$ (3,000)</u>	<u>\$ (142,944)</u>

**13. Subsequent Events**

The Company paid the following common and preferred dividends subsequent to June 30, 2013:

Security Type	Dividend per Share/Unit <sup>(1)</sup>	For the Quarter Ended	Record Date	Payable Date
Common Shares/Units	\$ 0.20	June 30, 2013	June 28, 2013	July 15, 2013
7 ¼% Series G Preferred Shares	\$ 0.45	June 30, 2013	July 1, 2013	July 15, 2013
7 ½% Series H Preferred Shares	\$ 0.47	June 30, 2013	July 1, 2013	July 15, 2013
6 ¾% Series I Preferred Shares	\$ 0.40	June 30, 2013	July 1, 2013	July 15, 2013

<sup>(1)</sup> Amounts are rounded to the nearest whole cent for presentation purposes.

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

The following should be read in conjunction with the consolidated financial statements and notes thereto appearing in Part I - Item 1 of this report.

**Forward-Looking Statements**

This report, together with other statements and information publicly disseminated by LaSalle Hotel Properties (the "Company"), contains certain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. The Company intends such forward-looking statements to be covered by the safe harbor provisions for forward-looking statements contained in the Private Securities Litigation Reform Act of 1995 and includes this statement for purposes of complying with these safe harbor provisions. Forward-looking statements, which are based on certain assumptions and describe the Company's future plans, strategies and expectations, are generally identifiable by use of the words "believe," "expect," "intend," "anticipate," "estimate," "project," "may," "plan," "seek," "should," "will" or similar expressions. Forward-looking statements in this report include, among others, statements about the Company's business strategy, including its acquisition and development strategies, industry trends, estimated revenues and expenses, ability to realize deferred tax assets and expected liquidity needs and sources (including capital expenditures and the ability to obtain financing or raise capital). You should not rely on forward-looking statements since they involve known and unknown risks, uncertainties and other factors that are, in some cases, beyond the Company's control and which could materially affect actual results, performances or achievements. Factors that may cause actual results to differ materially from current expectations include, but are not limited to:

- risks associated with the hotel industry, including competition, increases in wages, energy costs and other operating costs, potential unionization, actual or threatened terrorist attacks, any type of flu or disease-related pandemic and downturns in general and local economic conditions;
- the availability and terms of financing and capital and the general volatility of securities markets;
- the Company's dependence on third-party managers of its hotels, including its inability to implement strategic business decisions directly;
- risks associated with the real estate industry, including environmental contamination and costs of complying with the Americans with Disabilities Act of 1990, as amended, and similar laws;
- interest rate increases;
- the possible failure of the Company to maintain its qualification as a real estate investment trust ("REIT") and the risk of changes in laws affecting REITs;
- the possibility of uninsured losses;
- risks associated with redevelopment and repositioning projects, including delays and cost overruns; and
- the risk factors discussed in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, as updated elsewhere in this report.

Accordingly, there is no assurance that the Company's expectations will be realized. Any forward-looking statement speaks only as of the date on which it is made. New risks and uncertainties arise over time, and it is not possible for the Company to predict those events or how they may affect the Company. Except as otherwise required by law, the Company disclaims any obligations or undertaking to publicly release any updates or revisions to any forward-looking statement contained herein (or



elsewhere) to reflect any change in the Company's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based. Accordingly, investors should use caution in relying on past forward-looking statements, which were based on results and trends at the time they were made, to anticipate future events or trends.

### **Overview**

The Company measures hotel performance by evaluating financial metrics such as room revenue per available room ("RevPAR"), funds from operations ("FFO") and earnings before interest, taxes, depreciation and amortization ("EBITDA"). The Company evaluates the hotels in its portfolio and potential acquisitions using these metrics to determine each portfolio hotel's contribution or acquisition hotel's potential contribution toward reaching the Company's goals of providing income to its shareholders through increases in distributable cash flow and increasing long-term total returns to shareholders through appreciation in the value of its common shares. The Company invests in capital improvements throughout the portfolio to continue to increase the competitiveness of its hotels and improve their financial performance. The Company actively seeks to acquire hotel properties, but continues to face significant competition for acquisitions that meet its investment criteria.

During the second quarter of 2013, the hotel industry continued its trend of positive RevPAR growth. The economic indicators that the Company tracks are generally positive. Consumer confidence increased to its highest level in five years. Unemployment did not increase and remained at 7.6%. However, airline enplanement results were mixed for the quarter and it is too early to see a trend from corporate profits. In this context, the U.S. lodging industry experienced increases in demand and improvements in average daily rate ("ADR") during the quarter. Industry-wide RevPAR increased during each month of the quarter. The Company's hotel portfolio increased in ADR and experienced a 0.4% occupancy decline compared to the second quarter of 2012. The decline in occupancy was driven by the renovation underway at the Company's Park Central Hotel and WestHouse in New York City. The project consists of the full renovation and splitting of the original 934-room Park Central Hotel into two distinct hotels: the newly renovated 761-room Park Central Hotel and the upgraded 172-room premium WestHouse. While RevPAR improved 0.9% for the entire portfolio, RevPAR increased 6.7% for the portfolio excluding Park Central Hotel.

For the second quarter of 2013, the Company had net income attributable to common shareholders of \$35.2 million, or \$0.37 per diluted share. FFO was \$68.7 million, or \$0.72 per diluted share/unit (based on 95,926,366 weighted average shares and units outstanding during the three months ended June 30, 2013), and EBITDA was \$91.6 million. RevPAR for the hotel portfolio increased 0.9%, due to ADR growth of 1.3%, partially offset by an occupancy decline of 0.4%. However, excluding the Park Central Hotel, the portfolio's RevPAR was \$191.00, which was an increase of 6.7% compared to the second quarter of 2012.

Please refer to "Non-GAAP Financial Measures" for a detailed discussion of the Company's use of FFO and EBITDA and a reconciliation of FFO and EBITDA to net income or loss, a GAAP measurement.

### **Critical Accounting Estimates**

Substantially all of the Company's revenues and expenses are generated by the operations of the individual hotels. The Company records revenues and expenses that are estimated by the hotel operators to produce quarterly financial statements because the management contracts do not require the hotel operators to submit actual results within a time frame that permits the Company to use actual results when preparing its Quarterly Reports on Form 10-Q for filing by the deadline prescribed by the SEC. Generally, the Company records actual revenue and expense amounts for the first two months of each quarter and revenue and expense estimates for the last month of each quarter. Each quarter, the Company reviews the estimated revenue and expense amounts provided by the hotel operators for reasonableness based upon historical results for prior periods and internal Company forecasts. The Company records any differences between recorded estimated amounts and actual amounts in the following quarter; historically, these differences have not been material. The Company believes the quarterly revenues and expenses, recorded on the Company's consolidated statements of operations and comprehensive income (loss) based on an aggregate estimate, are fairly stated.

The Company's management has discussed the policy of using estimated hotel operating revenues and expenses with the Audit Committee of its Board of Trustees. The Audit Committee has reviewed the Company's disclosure relating to the estimates in this Management's Discussion and Analysis of Financial Conditions and Results of Operations section.

See "Critical Accounting Policies" in the "Management's Discussion and Analysis of Financial Conditions and Results of Operations" section of the Company's Annual Report on Form 10-K for the year ended December 31, 2012 for other critical accounting policies and estimates of the Company.

### **Comparison of the Three Months Ended June 30, 2013 to the Three Months Ended June 30, 2012**

Lodging industry performance improved during each month of the second quarter of 2013. The U.S. lodging industry continued to operate in an environment of low supply, which has a positive impact on industry occupancy. Additionally, industry-

wide ADR improved, as operators continued to gain more confidence in pricing and improved business mix within U.S. hotels. Within the Company's hotel portfolio, ADR increased 1.3% over the prior year, while occupancy declined 0.4%, resulting in RevPAR improvement of 0.9% compared to the second quarter of 2012. The decline in occupancy was driven by the renovation underway at the Company's Park Central Hotel and WestHouse in New York City. Excluding the Park Central Hotel, the portfolio's occupancy improved 4.9% while ADR increased 1.8%.

#### *Hotel Operating Revenues*

Hotel operating revenues including room, food and beverage and other operating department revenues increased \$20.1 million from \$240.8 million in 2012 to \$260.9 million in 2013. This increase is due primarily to the hotel operating revenues generated from the fourth quarter 2012 hotel acquisitions, which consist of the acquisitions of L'Auberge Del Mar and The Liberty Hotel (collectively, the "Fourth Quarter 2012 Acquisition Properties"). The Fourth Quarter 2012 Acquisition Properties, which are not comparable year-over-year, contributed \$17.6 million to the increase in hotel operating revenues. Additionally, the effects of the slowly improving economic environment, which resulted in a 0.9% increase in RevPAR across the portfolio, attributable to a 1.3% increase in ADR, partially offset by a 0.4% decrease in occupancy, contributed to the increase in hotel operating revenues. Excluding the Park Central Hotel, the portfolio's RevPAR increased 6.7%.

The following hotels experienced significant increases in total room, food and beverage and other operating department revenues primarily as a result of the effects of the improving economy:

- \$1.3 million increase from Indianapolis Marriott Downtown;
- \$0.8 million increase from Villa Florence;
- \$0.8 million increase from Sofitel Washington, DC Lafayette Square;
- \$0.8 million increase from Hotel Sax Chicago;
- \$0.8 million increase from Chaminade Resort and Conference Center;
- \$0.7 million increase from San Diego Paradise Point Resort and Spa;
- \$0.7 million increase from Donovan House;
- \$0.6 million increase from Lansdowne Resort; and
- \$0.6 million increase from Westin Michigan Avenue.

Additionally, total room, food and beverage and other operating department revenues increased \$2.4 million at the Hotel Roger Williams and \$1.6 million at the Le Montrose Suite Hotel resulting from the completion of the hotel renovations in 2012.

These increases are partially offset by a decrease of \$10.2 million from the Park Central Hotel as the property is undergoing a hotel renovation in the 2013 period.

Hotel operating revenues across the remainder of the portfolio remained relatively constant, increasing a net \$1.6 million across 26 additional hotels in the portfolio.

#### *Other Income*

Other income increased \$1.3 million from \$1.3 million in 2012 to \$2.6 million in 2013 primarily due to increased gains from insurance proceeds recognized in the 2013 period.

#### *Hotel Operating Expenses*

Hotel operating expenses increased \$11.3 million from \$138.9 million in 2012 to \$150.2 million in 2013. This overall increase is primarily due to \$9.4 million from the results of the Fourth Quarter 2012 Acquisition Properties, which are not comparable year-over-year. To a lesser extent, the increase is a result of increased operating costs associated with higher occupancies at certain properties in the portfolio attributable to the slowly improving economic environment and two completed hotel renovations.

The following hotels experienced significant increases in total room, food and beverage, other direct and other indirect expenses primarily as a result of increased occupancies at the hotels:

- \$0.9 million increase from Hotel Roger Williams (due to completion of the 2012 hotel renovation);
- \$0.6 million increase from Indianapolis Marriott Downtown; and
- \$0.6 million increase from Westin Michigan Avenue;

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These increases are partially offset by a decrease of \$3.0 million from the Park Central Hotel as a result of the 2013 hotel renovation.

Hotel operating expenses across the remainder of the portfolio remained relatively constant, increasing a net \$2.8 million across 34 additional hotels in the portfolio.

### *Depreciation and Amortization*

Depreciation and amortization expense increased \$2.1 million from \$31.3 million in 2012 to \$33.4 million in 2013. The increase is primarily due to \$2.0 million from the Fourth Quarter 2012 Acquisition Properties, which are not comparable year-over-year. Depreciation and amortization expense increased a net \$0.1 million across the remaining hotels in the portfolio due to the depreciation of new assets placed into service, particularly at the Hotel Roger Williams resulting from the completion of the 2012 hotel renovation, exceeding a portion of furniture, fixtures and equipment becoming fully depreciated.

### *Real Estate Taxes, Personal Property Taxes and Insurance*

Real estate taxes, personal property taxes and insurance expenses increased \$1.9 million from \$10.9 million in 2012 to \$12.8 million in 2013. This increase is primarily due to \$1.0 million from the Fourth Quarter 2012 Acquisition Properties, which are not comparable year-over-year. Real estate taxes and personal property taxes increased a net \$0.8 million across the remaining hotels in the portfolio primarily due to increased assessed property values or tax rates at certain properties, partially offset by real estate taxes capitalized as part of renovations. Insurance expense for the remaining hotels in the portfolio held relatively constant, increasing a net \$0.1 million due to property insurance placed on the hotels securing the mezzanine loan.

### *Ground Rent*

Ground rent increased \$0.6 million from \$2.2 million in 2012 to \$2.8 million in 2013. Certain hotels are subject to ground rent under operating leases which call for either fixed or variable payments based on the hotel's performance. The Liberty Hotel, which is not comparable year-over-year, accounted for all \$0.6 million of the increase. The operating results of the other hotels subject to ground leases were comparable for both periods.

### *General and Administrative*

General and administrative expense increased \$0.8 million from \$4.8 million in 2012 to \$5.6 million in 2013 due primarily to increased compensation costs, partially due to additional staffing as a result of portfolio growth.

### *Acquisition Transaction Costs*

There were no acquisitions or resulting acquisition transaction costs in the 2013 period. Acquisition transaction costs in 2012 of \$0.2 million relate to the acquisition of a mezzanine loan, which closed in July 2012, and \$0.1 million relate to the finalization of acquisition accounting for Viceroy Santa Monica, which closed in March 2011.

### *Other Expenses*

Other expenses increased \$0.6 million from \$0.9 million in 2012 to \$1.5 million in 2013 due primarily to greater losses from property damage, which were largely covered by insurance proceeds, slightly offset by lower pre-opening and management transition costs.

### *Interest Income*

Interest income increased \$2.4 million from an immaterial amount in 2012 to \$2.4 million in 2013 primarily as a result of the interest income earned on the mezzanine loan, which was acquired in July 2012.

### *Interest Expense*

Interest expense increased \$1.3 million from \$12.5 million in 2012 to \$13.8 million in 2013 due to an increase in the Company's weighted average debt outstanding. The Company's weighted average debt outstanding increased from \$1.1 billion in 2012 to \$1.2 billion in 2013 due primarily to the following borrowings:

- additional borrowings to purchase the Fourth Quarter 2012 Acquisition Properties;
- additional borrowings to redeem the 7 ½% Series D Cumulative Redeemable Preferred Shares (the "Series D Preferred Shares") and the 8% Series E Cumulative Redeemable Preferred Shares (the "Series E Preferred Shares") in May 2012;
- additional borrowings to acquire a performing mezzanine loan in July 2012;

- additional borrowings to redeem 4,000,000 of the 6,348,888 7¼% Series G Cumulative Redeemable Preferred Shares (the "Series G Preferred Shares") in April 2013; and
- additional borrowing to finance other capital improvements during 2012 and 2013.

The above borrowings were partially offset by paydowns with proceeds from the following:

- the March 2013 issuance of the 6<sup>3</sup>/<sub>8</sub>% Series I Cumulative Redeemable Preferred Shares (the "Series I Preferred Shares");
- the issuance of common shares under the Company's equity distribution agreements during 2012 and 2013;
- the December 2012 common share offering; and
- positive operating results from the hotel properties.

The Company's weighted average interest rate, including the impact of capitalized interest, remained the same at 4.1% for both periods. Interest capitalized on renovations increased from an immaterial amount in 2012 to \$0.3 million in 2013 primarily due to the renovation of the Park Central Hotel during the 2013 period.

#### *Income Tax Expense*

Income tax expense decreased \$0.1 million from \$5.0 million in 2012 to \$4.9 million in 2013. This slight decrease is primarily due to a decrease in LHL's net income before income tax expense of \$3.1 million from \$14.2 million in 2012 to \$11.1 million in 2013 due in part to the renovation of the Park Central Hotel in 2013, partially offset by the reversal of accruals resulting from the resolution of a previously disclosed uncertain tax position in 2012. For the quarter ended June 30, 2013, LHL's income tax expense was calculated using an estimated federal and state tax rate of 38.2%.

#### *Noncontrolling Interests in Consolidated Entities*

Noncontrolling interests in consolidated entities represent the allocation of income or loss to the outside preferred ownership interests in a subsidiary and the outside ownership interest in a joint venture.

#### *Noncontrolling Interests of Common Units in Operating Partnership*

Noncontrolling interests of common units in Operating Partnership represent the allocation of income or loss of the Operating Partnership to the common units held by third parties based on their weighted average percentage ownership throughout the period. At June 30, 2013, third party limited partners held 0.3% of the common units in the Operating Partnership.

#### *Distributions to Preferred Shareholders*

Distributions to preferred shareholders decreased \$1.9 million from \$6.0 million in 2012 to \$4.1 million in 2013 due to decreased distributions on the Series D Preferred Shares and Series E Preferred Shares, which were redeemed on May 21, 2012, and the Series G Preferred Shares, which were partially redeemed on April 5, 2013, partially offset by increased distributions on the Series I Preferred Shares, which were issued on March 4, 2013 and March 12, 2013.

#### *Issuance Costs of Redeemed Preferred Shares*

Issuance costs of redeemed preferred shares of \$1.6 million in 2013 represent the offering costs related to the Series G Preferred Shares, which were partially redeemed on April 5, 2013, and \$4.4 million in 2012 represent the offering costs related to the Series D Preferred Shares and Series E Preferred Shares, which were redeemed on May 21, 2012. The excess of fair value over carrying value (i.e. offering costs) is included in the determination of net income attributable to common shareholders.

#### *Comparison of the Six Months Ended June 30, 2013 to the Six Months Ended June 30, 2012*

Industry travel was stronger during the six months ended June 30, 2013 compared to the same period of the prior year. Demand improvements and limited supply growth led to occupancy growth, which has encouraged operators to increase pricing and resulted in ADR growth during the same period. With respect to the Company's hotels, ADR grew 2.4% during the six months ended June 30, 2013, while occupancy decreased 0.5%, which resulted in RevPAR improvement of 1.9% year-over-year. The decline in occupancy was driven by the renovation underway at the Company's Park Central Hotel and WestHouse in New York City. Excluding the Park Central Hotel, the portfolio's occupancy improved 4.2% while ADR increased 1.9%, resulting in a RevPAR improvement of 6.1%.

*Hotel Operating Revenues*

Hotel operating revenues including room, food and beverage and other operating department revenues increased \$39.2 million from \$412.0 million in 2012 to \$451.2 million in 2013. This increase is due primarily to the hotel operating revenues generated from the 2012 hotel acquisitions, which consist of the acquisitions of the Hotel Palomar, Washington, DC, L'Auberge Del Mar and The Liberty Hotel (collectively, the "2012 Acquisition Properties"). The 2012 Acquisition Properties, which are not comparable year-over-year, contributed \$35.1 million to the increase in hotel operating revenues. Additionally, the effects of the slowly improving economic environment, which resulted in a 1.9% increase in RevPAR across the portfolio, attributable to a 2.4% increase in ADR, partially offset by a 0.5% decrease in occupancy, contributed to the increase in hotel operating revenues. Excluding the Park Central Hotel, the portfolio's RevPAR increased 6.1%.

The following hotels experienced significant increases in total room, food and beverage and other operating department revenues primarily as a result of the effects of the improving economy:

- \$2.7 million increase from San Diego Paradise Point Resort and Spa; and
- \$2.0 million increase from Westin Michigan Avenue.

Additionally, total room, food and beverage and other operating department revenues increased \$3.4 million at the Company's eight other properties located in Washington, DC as a result of the 2013 Presidential inauguration as well as improved operating results in the 2013 second quarter, and \$3.8 million at the Hotel Roger Williams and \$1.9 million at Le Montrose Suite Hotel resulting from the completion of the hotel renovations in 2012.

These increases are partially offset by decreases of \$13.0 million from the Park Central Hotel as a result of the 2013 hotel renovation and \$1.2 million from the Indianapolis Marriott Downtown as a result of the first quarter comparative effects of the 2012 Super Bowl hosted by the City of Indianapolis.

Hotel operating revenues across the remainder of the portfolio held relatively constant, increasing a net \$4.5 million across 23 additional hotels in the portfolio.

*Other Income*

Other income increased \$1.7 million from \$2.4 million in 2012 to \$4.1 million in 2013 due primarily to increased gains from insurance proceeds recognized in the 2013 period and, to a lesser extent, to a \$0.2 million gain from the sale of land significantly below ground level at the Alexis Hotel to the state, which had no effect on hotel operations, recognized in the 2013 period.

*Hotel Operating Expenses*

Hotel operating expenses increased \$24.1 million from \$259.7 million in 2012 to \$283.8 million in 2013. This overall increase is primarily due to \$21.1 million from the results of the 2012 Acquisition Properties, which are not comparable year-over-year. To a lesser extent, the increase is a result of increased operating costs associated with higher occupancies at certain properties in the portfolio attributable to the slowly improving economic environment, two completed hotel renovations and the 2013 Presidential inauguration.

The following hotels experienced significant increases in total room, food and beverage, other direct and other indirect expenses primarily as a result of increased occupancies at the hotels:

- \$1.6 million increase from Westin Michigan Avenue;
- \$1.6 million increase from Hotel Roger Williams (due to completion of the 2012 hotel renovation);
- \$1.3 million increase from San Diego Paradise Point Resort and Spa; and
- \$1.1 million increase from the eight Washington, DC properties (primarily due to the positive effects of the 2013 Presidential inauguration).

These increases are partially offset by a decrease of \$4.8 million from the Park Central Hotel as a result of the 2013 hotel renovation.

Hotel operating expenses across the remainder of the portfolio held relatively constant, increasing a net \$2.2 million across 25 additional hotels in the portfolio.

*Depreciation and Amortization*

Depreciation and amortization expense increased \$5.1 million from \$61.4 million in 2012 to \$66.5 million in 2013. The increase is primarily due to \$4.7 million from the 2012 Acquisition Properties, which are not comparable year-over-year. Depreciation and amortization expense increased a net \$0.4 million across the remaining hotels in the portfolio due to the depreciation of new assets placed into service, particularly at the Hotel Roger Williams resulting from the completion of the 2012 hotel renovation, exceeding a portion of furniture, fixtures and equipment becoming fully depreciated.

*Real Estate Taxes, Personal Property Taxes and Insurance*

Real estate taxes, personal property taxes and insurance expenses increased \$3.4 million from \$21.7 million in 2012 to \$25.1 million in 2013. This increase is primarily due to \$2.1 million from the 2012 Acquisition Properties, which are not comparable year-over-year. Real estate taxes and personal property taxes increased a net \$1.1 million across the remaining hotels in the portfolio primarily due to increased assessed property values or tax rates at certain properties, partially offset by real estate taxes capitalized as part of renovations. Insurance expense for the remaining hotels in the portfolio held relatively constant, increasing a net \$0.2 million due to property insurance placed on the hotels securing the mezzanine loan.

*Ground Rent*

Ground rent increased \$1.3 million from \$4.0 million in 2012 to \$5.3 million in 2013. Certain hotels are subject to ground rent under operating leases which call for either fixed or variable payments based on the hotel's performance. The Liberty Hotel, which is not comparable year-over-year, contributed \$1.1 million to the 2013 increase. The other hotels subject to ground leases contributed a net \$0.2 million to the increase due to improved operating results.

*General and Administrative*

General and administrative expense increased \$1.2 million from \$9.5 million in 2012 to \$10.7 million in 2013 due primarily to increased compensation costs, partially due to additional staffing as a result of portfolio growth, and professional fees.

*Acquisition Transaction Costs*

There were no acquisitions or resulting acquisition transaction costs in the 2013 period. Acquisition transaction costs in 2012 of \$3.6 million relate to the purchase of the Hotel Palomar, Washington, DC, which closed in March 2012, \$0.2 million relate to the acquisition of a mezzanine loan, which closed in July 2012, and \$0.1 million relate to the finalization of acquisition accounting for Viceroy Santa Mónica, which closed in March 2011.

*Other Expenses*

Other expenses increased \$0.7 million from \$1.5 million in 2012 to \$2.2 million in 2013 due primarily to greater losses from property damage, which were largely covered by insurance proceeds.

*Interest Income*

Interest income increased \$4.8 million from an immaterial amount in 2012 to \$4.8 million in 2013 primarily as a result of the interest income earned on the mezzanine loan, which was acquired in July 2012.

*Interest Expense*

Interest expense increased \$3.5 million from \$24.3 million in 2012 to \$27.8 million in 2013 due to an increase in the Company's weighted average debt outstanding, partly offset by a decrease in the weighted average interest rate. The Company's weighted average debt outstanding increased from \$1.1 billion in 2012 to \$1.2 billion in 2013 due primarily to the following borrowings:

- additional borrowings to purchase the 2012 Acquisition Properties;
- additional borrowings to redeem the Series D Preferred Shares and the Series E Preferred Shares in May 2012;
- additional borrowings to acquire a performing mezzanine loan in July 2012;
- additional borrowings to redeem 4,000,000 of the 6,348,888 Series G Preferred Shares in April 2013; and
- additional borrowing to finance other capital improvements during 2012 and 2013.

The above borrowings were partially offset by paydowns with proceeds from the following:

- the March 2013 issuance of the Series I Preferred Shares;

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- the issuance of common shares under the Company's equity distribution agreements during 2012 and 2013;
- the December 2012 common share offering; and
- positive operating results from the hotel properties.

The Company's weighted average interest rate, including the impact of capitalized interest, decreased from 4.3% in 2012 to 4.2% in 2013. Interest capitalized on renovations increased from \$0.2 million in 2012 to \$0.4 million in 2013 primarily due to the renovation of the Park Central Hotel during the 2013 period.

### *Income Tax Benefit*

Income taxes changed \$2.1 million from an income tax expense of \$2.0 million in 2012 to an income tax benefit of \$0.1 million in 2013. This change is primarily due to a decrease in LHL's income/loss before income taxes of \$7.5 million from income before income tax expense of \$5.7 million in 2012 to loss before income tax benefit of \$1.8 million in 2013 due in part to the renovation of the Park Central Hotel in 2013, partially offset by the reversal of accruals resulting from the resolution of a previously disclosed uncertain tax position in 2012. For the six months ended June 30, 2013, LHL's income tax benefit was calculated using an estimated federal and state tax rate of 38.2%.

### *Noncontrolling Interests in Consolidated Entities*

Noncontrolling interests in consolidated entities represent the allocation of income or loss to the outside preferred ownership interests in a subsidiary and the outside ownership interest in a joint venture.

### *Noncontrolling Interests of Common Units in Operating Partnership*

Noncontrolling interests of common units in Operating Partnership represent the allocation of income or loss of the Operating Partnership to the common units held by third parties based on their weighted average percentage ownership throughout the period. At June 30, 2013, third party limited partners held 0.3% of the common units in the Operating Partnership.

### *Distributions to Preferred Shareholders*

Distributions to preferred shareholders decreased \$4.2 million from \$13.4 million in 2012 to \$9.2 million in 2013 due to decreased distributions on the Series D Preferred Shares and Series E Preferred Shares, which were redeemed on May 21, 2012, and the Series G Preferred Shares, which were partially redeemed on April 5, 2013, partially offset by increased distributions on the Series I Preferred Shares, which were issued on March 4, 2013 and March 12, 2013.

### *Issuance Costs of Redeemed Preferred Shares*

Issuance costs of redeemed preferred shares of \$1.6 million in 2013 represent the offering costs related to the Series G Preferred Shares, which were partially redeemed on April 5, 2013, and \$4.4 million in 2012 represent the offering costs related to the Series D Preferred Shares and Series E Preferred Shares, which were redeemed on May 21, 2012. The excess of fair value over carrying value (i.e. offering costs) is included in the determination of net income attributable to common shareholders.

## *Non-GAAP Financial Measures*

### *FFO and EBITDA*

The Company considers the non-GAAP measures of FFO and EBITDA to be key supplemental measures of the Company's performance and should be considered along with, but not as alternatives to, net income or loss as a measure of the Company's operating performance. Historical cost accounting for real estate assets implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, most real estate industry investors consider FFO and EBITDA to be helpful in evaluating a real estate company's operations.

The White Paper on FFO approved by the National Association of Real Estate Investment Trusts ("NAREIT") in April 2002 defines FFO as net income or loss (computed in accordance with GAAP), excluding gains or losses from sales of properties and items classified by GAAP as extraordinary, plus real estate-related depreciation and amortization (excluding amortization of deferred finance costs) and after comparable adjustments for the Company's portion of these items related to unconsolidated entities and joint ventures. In October 2011 and November 2011, NAREIT issued guidance reaffirming its view that impairment write-downs of depreciable real estate should be excluded from the computation of FFO. The Company computes FFO consistent with standards established by NAREIT, which may not be comparable to FFO reported by other REITs that do not define the term in accordance with the current NAREIT definition or that interpret the current NAREIT definition differently than the Company.

With respect to FFO, the Company believes that excluding the effect of extraordinary items, real estate-related depreciation and amortization, and the portion of these items related to unconsolidated entities, all of which are based on historical cost accounting

and which may be of limited significance in evaluating current performance, can facilitate comparisons of operating performance between periods and between REITs, even though FFO does not represent an amount that accrues directly to common shareholders. However, FFO may not be helpful when comparing the Company to non-REITs.

With respect to EBITDA, the Company believes that excluding the effect of non-operating expenses and non-cash charges, and the portion of these items related to unconsolidated entities, all of which are also based on historical cost accounting and may be of limited significance in evaluating current performance, can help eliminate the accounting effects of depreciation and amortization, and financing decisions and facilitate comparisons of core operating profitability between periods and between REITs, even though EBITDA also does not represent an amount that accrues directly to common shareholders.

FFO and EBITDA do not represent cash generated from operating activities as determined by GAAP and should not be considered as alternatives to net income, cash flows from operations or any other operating performance measure prescribed by GAAP. FFO and EBITDA are not measures of the Company's liquidity, nor are FFO and EBITDA indicative of funds available to fund the Company's cash needs, including its ability to make cash distributions. These measurements do not reflect cash expenditures for long-term assets and other items that have been and will be incurred. FFO and EBITDA may include funds that may not be available for management's discretionary use due to functional requirements to conserve funds for capital expenditures, property acquisitions and other commitments and uncertainties. To compensate for this, management considers the impact of these excluded items to the extent they are material to operating decisions or the evaluation of the Company's operating performance.

The following is a reconciliation between net income attributable to common shareholders and FFO for the three and six months ended June 30, 2013 and 2012 (in thousands, except share and unit data):

	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
Net income attributable to common shareholders	\$ 35,190	\$ 24,792	\$ 27,795	\$ 8,675
Depreciation	33,322	31,135	66,333	61,147
Amortization of deferred lease costs	86	88	174	174
Noncontrolling interests:				
Noncontrolling interests in consolidated entities	8	0	8	0
Noncontrolling interests of common units in Operating Partnership	135	130	135	108
<b>FFO</b>	<b>\$ 68,741</b>	<b>\$ 56,145</b>	<b>\$ 94,445</b>	<b>\$ 70,104</b>
<b>Weighted Average number of common shares and units outstanding:</b>				
Basic	95,761,764	85,748,278	95,613,042	85,272,217
Diluted	95,926,366	85,914,151	95,770,159	85,434,133

The following is a reconciliation between net income attributable to common shareholders and EBITDA for the three and six months ended June 30, 2013 and 2012 (in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2013	2012	2013	2012
Net income attributable to common shareholders	\$ 35,190	\$ 24,792	\$ 27,795	\$ 8,675
Interest expense	13,763	12,503	27,780	24,281
Income tax expense (benefit)	4,934	4,969	(83)	1,977
Depreciation and amortization	33,427	31,279	66,548	61,431
Noncontrolling interests:				
Noncontrolling interests in consolidated entities	8	0	8	0
Noncontrolling interests of common units in Operating Partnership	135	130	135	108
Distributions to preferred shareholders	4,107	5,999	9,172	13,401
<b>EBITDA</b>	<b>\$ 91,564</b>	<b>\$ 79,672</b>	<b>\$ 131,355</b>	<b>\$ 109,873</b>



***Off-Balance Sheet Arrangements***

***Reserve Funds for Future Capital Expenditures***

Certain of the Company's agreements with its hotel managers, franchisors and lenders have provisions for the Company to provide funds, generally 4.0% to 5.0% of hotel revenues, sufficient to cover the cost of (a) certain non-routine repairs and maintenance to the hotels and (b) replacements and renewals to the hotels' capital assets. Certain of the agreements require that the Company reserve this cash in separate accounts. As of June 30, 2013, the Company held a total of \$15.8 million of restricted cash reserves, \$9.9 million of which was available for future capital expenditures. The Company has sufficient cash on hand and availability on its credit facilities to cover capital expenditures under agreements that do not require that the Company separately reserve cash.

The Company has no other off-balance sheet arrangements.

***Liquidity and Capital Resources***

The Company's principal source of cash to meet its cash requirements, including distributions to shareholders, is the operating cash flow from the Company's hotels. Additional sources of cash are the Company's senior unsecured credit facility, LHL's unsecured credit facility, additional unsecured financing, secured financing on one or all of the Company's 34 unencumbered properties as of June 30, 2013, the sale of one or more properties, equity issuances available under the Company's shelf registration statement and the issuance of up to \$230.1 million of common shares from time to time under the 2013 Agreement (see "Equity Issuances and Redemptions" below).

LHL is a wholly owned subsidiary of the Operating Partnership. Payments to the Operating Partnership are required pursuant to the terms of the lease agreements between LHL and the Operating Partnership relating to the properties owned by the Operating Partnership and leased by LHL. LHL's ability to make rent payments to the Operating Partnership and the Company's liquidity, including its ability to make distributions to shareholders, are dependent on the lessees' ability to generate sufficient cash flow from the operation of the hotels.

## Debt Summary

Debt as of June 30, 2013 and December 31, 2012 consisted of the following (in thousands):

Debt	Interest Rate	Maturity Date	Balance Outstanding as of	
			June 30, 2013	December 31, 2012
<b>Credit facilities</b>				
Senior unsecured credit facility	Floating <sup>(a)</sup>	January 2016 <sup>(a)</sup>	\$ 180,000	\$ 153,000
LHL unsecured credit facility	Floating <sup>(b)</sup>	January 2016 <sup>(b)</sup>	0	0
Total borrowings under credit facilities			180,000	153,000
<b>Term loans</b>				
First Term Loan	Floating <sup>(c)</sup>	May 2019	177,500	177,500
Second Term Loan	Floating <sup>(c)</sup>	August 2017	300,000	300,000
Total term loans			477,500	477,500
<b>Massport Bonds</b>				
Hyatt Boston Harbor (taxable)	Floating <sup>(d)</sup>	March 2018	5,400	5,400
Hyatt Boston Harbor (tax exempt)	Floating <sup>(d)</sup>	March 2018	37,100	37,100
Total bonds payable			42,500	42,500
<b>Mortgage loans</b>				
Hotel Solamar	5.49%	December 2013 <sup>(e)</sup>	0	60,134
Hotel Deca	6.28%	August 2014 <sup>(f)</sup>	8,961	9,111
Westin Copley Place	5.28%	September 2015	210,000	210,000
Westin Michigan Avenue	5.75%	April 2016	136,246	137,172
Indianapolis Marriott Downtown	5.99%	July 2016	99,510	100,142
Hotel Roger Williams	6.31%	August 2016	61,983	62,543
Mortgage loans at stated value			516,700	579,102
Unamortized loan premium <sup>(g)</sup>			82	118
Total mortgage loans			516,782	579,220
<b>Total debt</b>			<b>\$ 1,216,782</b>	<b>\$ 1,252,220</b>

- <sup>(a)</sup> Borrowings bear interest at floating rates equal to, at the Company's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. As of June 30, 2013, the rate, including the applicable margin, for the Company's outstanding LIBOR borrowings of \$180,000 was 1.95%. As of December 31, 2012, the rate, including the applicable margin, for the Company's outstanding LIBOR borrowing of \$153,000 was 2.22%. The Company has the option, pursuant to certain terms and conditions, to extend the maturity date to January 2017.
- <sup>(b)</sup> Borrowings bear interest at floating rates equal to, at LHL's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. There were no borrowings outstanding at June 30, 2013 or December 31, 2012. LHL has the option, subject to certain terms and conditions, to extend the maturity date to January 2017.
- <sup>(c)</sup> Term loans bear interest at floating rates equal to LIBOR plus an applicable margin. The Company entered into separate interest rate swap agreements for the full seven-year term of the First Term Loan (as defined below) and the full five-year term, including a one-year extension subject to certain conditions, of the Second Term Loan (as defined below), resulting in fixed all-in interest rates at June 30, 2013 of 3.62% and 2.43%, respectively, and at December 31, 2012 of 3.87% and 2.68%, respectively, at the Company's current leverage ratio (as defined in the swap agreements).
- <sup>(d)</sup> The Massport Bonds are secured by letters of credit issued by the Royal Bank of Scotland that expire in February 2014, pursuant to an amendment to the agreement governing the letters of credit. The Royal Bank of Scotland letters of credit also have three one-year extension options and are secured by the Hyatt Boston Harbor (formerly the Harborside Hyatt Conference Center & Hotel). The bonds bear interest based on weekly floating rates. The interest rates as of June 30, 2013 were 0.70% and 0.10% for the \$5,400 and \$37,100 bonds, respectively. The interest rates as of December 31, 2012 were 0.65% and 0.17% for the \$5,400 and \$37,100 bonds, respectively. The Company also incurs an annual letter of credit fee of a variable rate based on an applicable margin as defined in the Company's senior unsecured credit agreement.
- <sup>(e)</sup> The Company repaid the mortgage loan on June 3, 2013 through borrowings on its senior unsecured credit facility.
- <sup>(f)</sup> The Company intends to repay the mortgage loan through borrowings on its credit facilities upon maturity.

- (g) Mortgage debt includes an unamortized loan premium on the mortgage loan on Hotel Deca of \$82 as of June 30, 2013 and \$118 as of December 31, 2012.

A summary of the Company's interest expense and weighted average interest rates for variable rate debt for the three and six months ended June 30, 2013 and 2012 is as follows (in thousands):

	For the three months ended		For the six months ended	
	June 30,		June 30,	
	2013	2012	2013	2012
Interest Expense:				
Interest incurred	\$ 13,444	\$ 12,104	\$ 27,071	\$ 23,685
Amortization of deferred financing costs	576	432	1,140	828
Capitalized interest	(257)	(33)	(431)	(232)
Interest expense	<u>\$ 13,763</u>	<u>\$ 12,503</u>	<u>\$ 27,780</u>	<u>\$ 24,281</u>
<b>Weighted Average Interest Rates for Variable Rate Debt:</b>				
Senior unsecured credit facility	<u>2.1%</u>	<u>2.1%</u>	<u>2.1%</u>	<u>2.1%</u>
LHL unsecured credit facility	<u>2.1%</u>	<u>2.0%</u>	<u>2.1%</u>	<u>2.0%</u>
Massport Bonds	<u>0.3%</u>	<u>0.3%</u>	<u>0.2%</u>	<u>0.3%</u>

### *Credit Facilities*

The Company has a \$750.0 million senior unsecured credit facility with a syndicate of banks. The credit facility matures on January 30, 2016, subject to a one-year extension that the Company may exercise at its option, pursuant to certain terms and conditions, including payment of an extension fee. The credit facility includes an accordion feature which, subject to certain conditions, entitles the Company to request additional lender commitments, allowing for total commitments up to \$1.0 billion. Borrowings under the credit facility bear interest at floating rates equal to, at the Company's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. Additionally, the Company is required to pay a variable unused commitment fee of 0.30% or 0.40% of the unused portion of the credit facility, depending on the average daily unused portion of the credit facility.

LHL has a \$25.0 million unsecured revolving credit facility to be used for working capital and general lessee corporate purposes. The LHL credit facility matures on January 30, 2016, subject to a one-year extension that LHL may exercise at its option, pursuant to certain terms and conditions, including payment of an extension fee. Borrowings under the LHL credit facility bear interest at floating rates equal to, at LHL's option, either (i) LIBOR plus an applicable margin, or (ii) an Adjusted Base Rate plus an applicable margin. Additionally, LHL is required to pay a variable unused commitment fee of 0.30% or 0.40% of the unused portion of the credit facility, depending on the average daily unused portion of the LHL credit facility.

The Company's senior unsecured credit facility and LHL's unsecured credit facility contain certain financial covenants relating to net worth requirements, debt ratios and fixed charge coverage and other limitations that restrict the Company's ability to make distributions or other payments to its shareholders upon events of default.

### *Term Loans*

On May 16, 2012, the Company entered into a \$177.5 million unsecured loan with a seven-year term maturing on May 16, 2019 (the "First Term Loan"). The First Term Loan bears interest at a variable rate, but was hedged to a fixed interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 3.62% at June 30, 2013, for the full seven-year term (see "Derivative and Hedging Activities" below).

On August 2, 2012, the Company entered into a \$300.0 million unsecured loan with a five-year term maturing on August 2, 2017, including a one-year extension subject to certain conditions (the "Second Term Loan"). The Second Term Loan bears interest at a variable rate, but was hedged to a fixed interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 2.43% at June 30, 2013, for the full five-year term (see "Derivative and Hedging Activities" below).

The Company's term loans contain certain financial covenants relating to net worth requirements, debt ratios and fixed charge coverage and other limitations that restrict the Company's ability to make distributions or other payments to its shareholders upon events of default.

*Derivative and Hedging Activities*

The Company primarily uses interest rate swaps as part of its interest rate risk management strategy. Interest rate swaps designated as cash flow hedges involve the receipt of variable-rate amounts from a counterparty in exchange for the Company making fixed-rate payments over the life of the agreements without exchange of the underlying notional amount. Unrealized gains and losses on the effective portion of hedging instruments are reported in other comprehensive income (loss) ("OCI"). Ineffective portions of changes in the fair value of a cash flow hedge are recognized as interest expense. Amounts reported in accumulated other comprehensive income (loss) ("AOCI") related to currently outstanding derivatives are recognized as an adjustment to income (loss) as interest payments are made on the Company's variable rate debt. Effective May 16, 2012, the Company entered into three interest rate swap agreements with an aggregate notional amount of \$177.5 million for the First Term Loan's full seven-year term, resulting in a fixed all-in interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 3.62% at June 30, 2013. Effective August 2, 2012, the Company entered into five interest rate swap agreements with an aggregate notional amount of \$300.0 million for the Second Term Loan's full five-year term, including a one-year extension subject to certain conditions, resulting in a fixed all-in interest rate based on the Company's current leverage ratio (as defined in the swap agreements), which interest rate was 2.43% at June 30, 2013. The Company has designated its pay-fixed, receive-floating interest rate swap derivatives as cash flow hedges.

The following tables present the effect of derivative instruments on the Company's consolidated statements of operations and comprehensive income, including the location and amount of unrealized gain (loss) on outstanding derivative instruments in cash flow hedging relationships, for the three and six months ended June 30, 2013 and 2012 (in thousands):

	Amount of Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)		Location of Loss Reclassified from AOCI into Income (Effective Portion)	Amount of Loss Reclassified from AOCI into Income (Effective Portion)	
	For the three months ended June 30,			For the three months ended June 30,	
	2013	2012		2013	2012
Derivatives in cash flow hedging relationships:					
Interest rate swaps	\$ 11,081	\$ (4,695)	Interest expense	\$ 1,049	\$ 302

	Amount of Gain (Loss) Recognized in OCI on Derivative Instruments (Effective Portion)		Location of Loss Reclassified from AOCI into Income (Effective Portion)	Amount of Loss Reclassified from AOCI into Income (Effective Portion)	
	For the six months ended June 30,			For the six months ended June 30,	
	2013	2012		2013	2012
Derivatives in cash flow hedging relationships:					
Interest rate swaps	\$ 12,600	\$ (4,695)	Interest expense	\$ 2,081	\$ 302

During the three and six months ended June 30, 2013 and 2012, the Company did not have any hedge ineffectiveness or amounts that were excluded from the assessment of hedge effectiveness recorded in earnings.

As of June 30, 2013, there was \$4.8 million in cumulative unrealized gain, of which \$4.8 million was included in AOCI and an immaterial amount was attributable to noncontrolling interests. As of December 31, 2012, there was \$7.8 million in cumulative unrealized loss, of which \$7.7 million was included in AOCI and an immaterial amount was attributable to noncontrolling interests. The Company expects that approximately \$4.2 million will be reclassified from AOCI and noncontrolling interests and recognized as a reduction to income in the next 12 months, calculated as estimated interest expense using the interest rates on the derivative instruments as of June 30, 2013.

*Mortgage Loans*

The Company's mortgage loans are secured by the respective properties. The mortgages are non-recourse to the Company except for fraud or misapplication of funds.

On June 3, 2013, the Company repaid without fee or penalty the Hotel Solamar mortgage loan in the amount of \$59.8 million plus accrued interest through borrowings on its senior unsecured credit facility. The loan was due to mature in December 2013.

The mortgage loans contain debt service coverage ratio tests related to the mortgaged properties. If the debt service coverage ratio for a specific property fails to exceed a threshold level specified in the mortgage, cash flows from that hotel will automatically be directed to the lender to (i) satisfy required payments, (ii) fund certain reserves required by the mortgage and (iii) fund additional cash reserves for future required payments, including final payment. Cash flows will be directed to the lender ("cash trap") until such time as the property again complies with the specified debt service coverage ratio or the mortgage is paid off.

#### *Financial Covenants*

Failure to comply with our financial covenants contained in our credit facilities, term loans and non-recourse secured mortgages could result from, among other things, changes in our results of operations, the incurrence of additional debt or changes in general economic conditions.

If the Company violates the financial covenants contained in any of its credit facilities or term loans described above, the Company may attempt to negotiate waivers of the violations or amend the terms of the applicable credit facilities or term loans with the lenders thereunder; however, the Company can make no assurance that it would be successful in any such negotiations or that, if successful in obtaining waivers or amendments, such amendments or waivers would be on terms attractive to the Company. If a default under the credit facilities or term loans were to occur, the Company would possibly have to refinance the debt through additional debt financing, private or public offerings of debt securities, or additional equity financings. If the Company is unable to refinance its debt on acceptable terms, including at maturity of the credit facilities and term loans, it may be forced to dispose of hotel properties on disadvantageous terms, potentially resulting in losses that reduce cash flow from operating activities. If, at the time of any refinancing, prevailing interest rates or other factors result in higher interest rates upon refinancing, increases in interest expense would lower the Company's cash flow, and, consequently, cash available for distribution to its shareholders.

A cash trap associated with a mortgage loan may limit the overall liquidity for the Company as cash from the hotel securing such mortgage would not be available for the Company to use. If the Company is unable to meet mortgage payment obligations, including the payment obligation upon maturity of the mortgage borrowing, the mortgage securing the specific property could be foreclosed upon by, or the property could be otherwise transferred to, the mortgagee with a consequent loss of income and asset value to the Company.

As of June 30, 2013, the Company is in compliance with all debt covenants, current on all loan payments and not otherwise in default under the credit facilities, term loans, bonds payable or mortgage loans. One of the mortgaged properties is currently subject to a cash trap as a result of the impact of a recent renovation on hotel operations. This cash trap does not have a material impact on the cash flow or the operations of the property or the Company.

#### *Fair Value Measurements*

In evaluating fair value, GAAP outlines a valuation framework and creates a fair value hierarchy that distinguishes between market assumptions based on market data (observable inputs) and a reporting entity's own assumptions about market data (unobservable inputs). The hierarchy ranks the quality and reliability of inputs used to determine fair value, which are then classified and disclosed in one of the three categories. The three levels are as follows:

Level 1—Inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity has the ability to access at the measurement date.

Level 2—Observable inputs, other than quoted prices included in level 1, such as interest rates, yield curves, quoted prices in active markets for similar assets and liabilities, and quoted prices for identical or similar assets or liabilities in markets that are not active.

Level 3—Unobservable inputs that are supported by limited market activity. This includes certain pricing models, discounted cash flow methodologies and similar techniques when observable inputs are not available.

The Company estimates the fair value of its financial instruments using available market information and valuation methodologies the Company believes to be appropriate for these purposes. Considerable judgment and subjectivity are involved in developing these estimates and, accordingly, such estimates are not necessarily indicative of amounts that would be realized upon disposition.

*Recurring Measurements*

For assets and liabilities measured at fair value on a recurring basis, quantitative disclosure of their fair value is as follows (in thousands):

Description	Consolidated Balance Sheet Location	Fair Value Measurements at	
		June 30, 2013	December 31, 2012
		Using Significant Inputs (Level 2)	Other Observable Inputs (Level 2)
Derivative interest rate instruments	Prepaid expenses and other assets	\$ 4,841	\$ 0
Derivative interest rate instruments	Accounts payable and accrued expenses	\$ 0	\$ 7,759

The fair value of each derivative instrument is based on a discounted cash flow analysis of the expected cash flows under each arrangement. This analysis reflects the contractual terms of the derivative instrument, including the period to maturity, and utilizes observable market-based inputs, including interest rate curves and implied volatilities, which is classified within level 2 of the fair value hierarchy. The Company also incorporates credit value adjustments to appropriately reflect each parties' nonperformance risk in the fair value measurement, which utilizes level 3 inputs such as estimates of current credit spreads. However, the Company has assessed that the credit valuation adjustments are not significant to the overall valuation of the derivatives. As a result, the Company has determined that its derivative valuations in their entirety are classified within level 2 of the fair value hierarchy.

*Financial Instruments Not Measured at Fair Value*

The following table represents the fair value, derived using level 2 inputs, of financial instruments presented at carrying value in the Company's consolidated financial statements as of June 30, 2013 and December 31, 2012 (in thousands):

	June 30, 2013		December 31, 2012	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Note receivable	\$ 69,698	\$ 69,698	\$ 68,490	\$ 68,490
Borrowings under credit facilities	\$ 180,000	\$ 179,535	\$ 153,000	\$ 153,719
Term loans	\$ 477,500	\$ 470,438	\$ 477,500	\$ 475,752
Bonds payable	\$ 42,500	\$ 42,500	\$ 42,500	\$ 42,500
Mortgage loans	\$ 516,782	\$ 536,513	\$ 579,220	\$ 607,109

The Company estimates the fair value of its borrowings under credit facilities, term loans, bonds payable and mortgage loans using a weighted average effective interest rate of 2.9% as of June 30, 2013 and December 31, 2012. The assumptions reflect the terms currently available on similar borrowings to borrowers with credit profiles similar to the Company's. The Company estimates that the fair value of its note receivable approximates its carrying value due to the relatively short period until maturity.

At June 30, 2013 and December 31, 2012, the carrying amounts of certain of the Company's financial instruments, including cash and cash equivalents, restricted cash, accounts receivable and accounts payable and accrued expenses were representative of their fair values due to the short-term nature of these instruments and the recent acquisition of these items.

*Equity Issuances and Redemptions*

On February 20, 2013, the Company entered into an equity distribution agreement (the "2013 Agreement") with Raymond James & Associates, Inc. (the "Manager"). Under the terms of the 2013 Agreement, the Company may issue from time to time through or to the Manager, as sales agent or principal, the Company's common shares of beneficial interest with aggregate gross proceeds totaling up to \$250.0 million. The 2013 Agreement replaced the Company's prior equity distribution agreement, under which \$146.0 million of aggregate gross proceeds remained.

On March 4, 2013, the Company issued 4,000,000 Series I Preferred Shares (\$0.01 par value) at a price of \$25.00 per share and received net proceeds, after costs, of \$96.7 million. On March 12, 2013, the underwriters exercised their rights to cover overallotments and purchased 400,000 additional Series I Preferred Shares, resulting in additional net proceeds to the Company of \$9.7 million. The net proceeds were used to redeem a portion of the Company's Series G Preferred Shares on April 5, 2013, to pay down amounts outstanding under the Company's senior unsecured credit facility, and for general corporate purposes.

On April 5, 2013, the Company redeemed 4,000,000 of the 6,348,888 outstanding Series G Preferred Shares for \$100.0 million (\$25.00 per share) plus accrued distributions through April 5, 2013 of \$1.9 million. The redemption value of the Series G Preferred Shares exceeded their carrying value by \$1.6 million, which is included in the determination of net income attributable to common shareholders for the three and six months ended June 30, 2013. The \$1.6 million represents the offering costs related to the redeemed Series G Preferred Shares.

From May 24, 2013 through May 31, 2013, the Company sold 721,706 common shares of beneficial interest, par value \$0.01 per share, under the 2013 Agreement. After deducting the Manager's discounts and commissions of \$0.2 million, the Company raised net proceeds of \$19.7 million. The net proceeds were used to pay down amounts outstanding under the Company's senior unsecured credit facility and for general corporate purposes. As of June 30, 2013, the Company had availability under the 2013 Agreement to issue and sell common shares of beneficial interest having an aggregate offering price of up to \$230.1 million.

### *Sources and Uses of Cash*

As of June 30, 2013, the Company had \$15.1 million of cash and cash equivalents and \$15.8 million of restricted cash reserves, \$9.9 million of which was available for future capital expenditures. Additionally, the Company had \$568.0 million available under the Company's senior unsecured credit facility, with \$2.0 million reserved for outstanding letters of credit, and \$25.0 million available under LHL's unsecured credit facility.

Net cash provided by operating activities was \$96.0 million for the six months ended June 30, 2013 primarily due to the operations of the hotels, which were partially offset by payments for real estate taxes, personal property taxes, insurance and ground rent.

Net cash used in investing activities was \$58.8 million for the six months ended June 30, 2013 primarily due to outflows for improvements and additions at the hotels and deposits on potential future acquisitions, partially offset by net proceeds from restricted cash reserves.

Net cash used in financing activities was \$57.2 million for the six months ended June 30, 2013 primarily due to payment for the redemption of preferred shares, mortgage loan repayments, payment of distributions to the common shareholders and unitholders and payment of distributions to preferred shareholders, partially offset by net proceeds from the preferred share offering, net proceeds from the credit facilities and net proceeds from the common share offerings.

On July 17, 2013, the Company's Board of Trustees increased the common dividend for the third quarter of 2013 by 40% to \$0.28 per share, an annualized rate of \$1.12 per share.

The Company has considered its short-term (one year or less) liquidity needs and the adequacy of its estimated cash flow from operations and other expected liquidity sources to meet these needs. The Company believes that its principal short-term liquidity needs are to fund normal recurring expenses, debt service requirements, distributions on the preferred shares and the minimum distribution required to maintain the Company's REIT qualification under the Code. The Company anticipates that these needs will be met with available cash on hand, cash flows provided by operating activities, borrowings under the Company's senior unsecured credit facility or LHL's unsecured credit facility, additional unsecured financing, secured financing on any of the Company's 34 unencumbered properties, potential property sales, equity issuances available under the Company's shelf registration statement and the issuance of up to \$230.1 million of common shares from time to time under the 2013 Agreement. The Company also considers capital improvements, including the ongoing 2013 renovation of the Park Central Hotel in which the Company expects to invest between \$60.0 million and \$70.0 million, and property acquisitions as short-term needs that will be funded either with cash flows provided by operating activities, utilizing availability under the Company's senior unsecured credit facility or LHL's unsecured credit facility, additional unsecured financing, secured financing on any of the Company's 34 unencumbered properties, potential property sales or the issuance of additional equity securities.

The Company expects to meet long-term (greater than one year) liquidity requirements such as property acquisitions, scheduled debt maturities, major renovations, expansions and other nonrecurring capital improvements utilizing availability under the Company's senior unsecured credit facility or LHL's unsecured credit facility, additional unsecured financing, secured financing on any of the Company's 34 unencumbered properties, potential property sales, estimated cash flows from operations, equity issuances available under the Company's shelf registration statement and the issuance of up to \$230.1 million of common shares from time to time under the 2013 Agreement. The Company expects to acquire or develop additional hotel properties only as suitable opportunities arise, and the Company will not undertake acquisition or development of properties unless stringent acquisition or development criteria have been achieved.

### Reserve Funds

The Company is obligated to maintain reserve funds for capital expenditures at the hotels (including the periodic replacement or refurbishment of furniture, fixtures and equipment) as determined pursuant to the operating agreements. Please refer to "Off-Balance Sheet Arrangements" for a discussion of the Reserve Funds.

### Contractual Obligations

The following is a summary of the Company's obligations and commitments as of June 30, 2013 (in thousands):

Obligations and Commitments	Total Amounts Committed	Amount of Commitment Expiration Per Period			
		Less than 1 year	1 to 3 years	4 to 5 years	Over 5 years
Mortgage loans <sup>(1)</sup>	\$ 595,211	\$ 34,329	\$ 406,158	\$ 154,724	\$ 0
Borrowings under credit facilities <sup>(2)</sup>	189,194	3,559	185,635	0	0
Rents <sup>(3)</sup>	394,942	7,054	14,187	14,306	359,395
Massport Bonds <sup>(1)</sup>	42,875	75	150	42,650	0
Term loans <sup>(4)</sup>	546,027	13,906	27,850	321,073	183,198
Purchase commitments <sup>(5)</sup>					
Purchase orders and letters of commitment	46,026	46,026	0	0	0
<b>Total obligations and commitments</b>	<b>\$1,814,275</b>	<b>\$ 104,949</b>	<b>\$ 633,980</b>	<b>\$ 532,753</b>	<b>\$ 542,593</b>

(1) Amounts include principal and interest.

(2) Amounts include principal and interest. Interest expense is calculated based on the variable rate as of June 30, 2013. It is assumed that the outstanding debt as of June 30, 2013 will be repaid upon maturity with interest-only payments until then.

(3) Amounts calculated based on the annual minimum future lease payments that extend through the term of the lease. Rents may be subject to adjustments based on future interest rates and hotel performance.

(4) Amounts include principal and interest. The term loans bear interest at floating rates equal to LIBOR plus applicable margins. The Company entered into separate interest rate swap agreements for the full seven-year term of the First Term Loan and the full five-year term, including a one-year extension subject to certain conditions, of the Second Term Loan, resulting in fixed all-in interest rates of 3.62% and 2.43%, respectively, at the Company's current leverage ratio (as defined in the swap agreements). It is assumed that the outstanding debt as of June 30, 2013 will be repaid upon maturity with fixed interest-only payments until then.

(5) As of June 30, 2013, purchase orders and letters of commitment totaling approximately \$46.0 million had been issued for renovations at the properties. The Company has committed to these projects and anticipates making similar arrangements in the future with the existing properties or any future properties that it may acquire.

### The Hotels

The following table sets forth historical comparative information with respect to occupancy, ADR and RevPAR for the total hotel portfolio for the three and six months ended June 30, 2013 and 2012:

	For the three months ended			For the six months ended		
	2013	2012	Variance	2013	2012	Variance
Occupancy	83.5%	83.9%	-0.4%	77.5%	77.9%	-0.5%
ADR	\$ 221.88	\$ 219.00	1.3%	\$ 205.49	\$ 200.65	2.4%
RevPAR	\$ 185.35	\$ 183.69	0.9%	\$ 159.26	\$ 156.36	1.9%

The above hotel statistics include adjustments made for presentation of comparable information.

### Inflation

The Company relies entirely on the performance of the hotels and their ability to increase revenues to keep pace with inflation. The hotel operators can change room rates quickly, but competitive pressures may limit the hotel operators' abilities to raise rates faster than inflation or even at the same rate.



The Company's expenses (primarily real estate taxes, property and casualty insurance, administrative expenses and hotel operating expenses) are subject to inflation. These expenses are expected to grow at the general rate of inflation, except for energy costs, liability insurance, property taxes (due to increased rates and periodic reassessments), employee benefits and some wages, which are expected to increase at rates higher than inflation.

### **Seasonality**

The Company's hotels' operations historically have been seasonal. Taken together, the hotels maintain higher occupancy rates during the second and third quarters of each year. These seasonality patterns can be expected to cause fluctuations in the quarterly hotel operations.

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The Company is exposed to market risk from changes in interest rates. The Company seeks to limit the impact of interest rate changes on earnings and cash flows and to lower the overall borrowing costs by closely monitoring the Company's variable rate debt and converting such debt to fixed rates when the Company deems such conversion advantageous. From time to time, the Company may enter into interest rate swap agreements or other interest rate hedging contracts. While these agreements are intended to lessen the impact of rising interest rates, they also expose the Company to the risks that the other parties to the agreements will not perform, the Company could incur significant costs associated with the settlement of the agreements, the agreements will be unenforceable and the underlying transactions will fail to qualify as highly effective cash flow hedges under GAAP guidance. As of June 30, 2013, \$222.5 million of the Company's aggregate indebtedness (18.3% of total indebtedness) was subject to variable interest rates, excluding amounts outstanding under the First Term Loan and Second Term Loan since the Company hedged their variable interest rates to fixed interest rates.

If market rates of interest on the Company's variable rate long-term debt fluctuate by 0.25%, interest expense would increase or decrease, depending on rate movement, future earnings and cash flows by \$0.6 million annually. This assumes that the amount outstanding under the Company's variable rate debt remains at \$222.5 million, the balance as of June 30, 2013.

### **Item 4. Controls and Procedures**

Based on the most recent evaluation, the Company's Chief Executive Officer and Chief Financial Officer believe the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) were effective as of June 30, 2013. There were no changes to the Company's internal control over financial reporting during the second quarter ended June 30, 2013 that materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II. Other Information**

### **Item 1. Legal Proceedings**

The nature of hotel operations exposes the Company and its hotels to the risk of claims and litigation in the normal course of their business. The Company is not presently subject to any material litigation nor, to the Company's knowledge, is any litigation threatened against the Company, other than routine actions for negligence or other claims and administrative proceedings arising in the ordinary course of business, some of which are expected to be covered by liability insurance and all of which collectively are not expected to have a material adverse effect on the liquidity, results of operations, business or financial condition of the Company.

### **Item 1A. Risk Factors**

Other than the following, there have been no material changes from the risk factors disclosed in the "Risk Factors" section of the Company's Annual Report on Form 10-K for the year ended December 31, 2012.

***The Company and its hotel managers rely on information technology in the Company's operations, and any material failure, inadequacy, interruption or security failure of that technology could harm the Company's business.***

The Company and its hotel managers rely on information technology networks and systems, including the Internet, to process, transmit and store electronic information, and to manage or support a variety of business processes, including financial transactions and records, personal identifying information, reservations, billing and operating data. The Company and its hotel managers purchase some of the Company's information technology from vendors, on whom the Company's systems depend, and the Company relies on commercially available systems, software, tools and monitoring to provide security for processing, transmission and storage of confidential customer information, such as individually identifiable information, including information relating to

financial accounts. Although the Company has taken steps to protect the security of its information systems and the data maintained in those systems, it is possible that the Company's safety and security measures will not be able to prevent the systems' improper functioning or damage, or the improper access or disclosure of personally identifiable information, such as in the event of cyber attacks, which are rapidly evolving and becoming increasingly sophisticated. Security breaches, including physical or electronic break-ins, computer viruses, attacks by hackers and similar breaches, can create system disruptions, shutdowns or unauthorized disclosure of confidential information. Any failure to maintain proper function, security and availability of the Company's information systems could interrupt the Company's operations; damage the Company's reputation; result in misstated financial reports, violations of loan covenants and/or missed reporting deadlines; result in the Company's inability to properly monitor its compliance with the rules and regulations regarding its qualification as a REIT; require significant management attention and resources to remedy any damages that result; subject the Company to liability claims or regulatory penalties; and have a material adverse effect on the Company's business, financial condition and results of operations.

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

None.

**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

Not applicable.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

<b>Exhibit Number</b>	<b>Description of Exhibit</b>
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes – Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes – Oxley Act of 2002
32.1	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes – Oxley Act of 2002
101	The following financial statements from LaSalle Hotel Properties' Quarterly Report on Form 10-Q for the quarter ended June 30, 2013, filed on July 17, 2013, formatted in XBRL: (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Operations and Comprehensive Income, (iii) Consolidated Statements of Equity, (iv) Consolidated Statements of Cash Flows and (v) Notes to Consolidated Financial Statements

**SIGNATURE**

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.

**LASALLE HOTEL PROPERTIES**

Date: July 17, 2013

BY: /s/ BRUCE A. RIGGINS

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**Bruce A. Riggins**

*Executive Vice President  
and Chief Financial Officer (Principal Financial Officer  
and Principal Accounting Officer)*

**Exhibit Index**

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## Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Michael D. Barnello, certify that:

1. I have reviewed this quarterly report on Form 10-Q of LaSalle Hotel Properties;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 17, 2013

/s/ MICHAEL D. BARNELLO

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**Michael D. Barnello**

*President and Chief Executive Officer*

## Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Bruce A. Riggins, certify that:

1. I have reviewed this quarterly report on Form 10-Q of LaSalle Hotel Properties;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 17, 2013

/s/ BRUCE A. RIGGINS

**Bruce A. Riggins**

*Executive Vice President  
and Chief Financial Officer*

**Certification Pursuant To  
18 U.S.C. Section 1350,  
as Adopted Pursuant to  
Section 906 of The Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report of LaSalle Hotel Properties ("LHO") on Form 10-Q for the period ended June 30, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Michael D. Barnello, President and Chief Executive Officer of LHO, and I, Bruce A. Riggins, Executive Vice President and Chief Financial Officer of LHO, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) the Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of LHO.

Date: July 17, 2013

/s/ MICHAEL D. BARNELLO

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**Michael D. Barnello**

*President and Chief Executive Officer*

/s/ BRUCE A. RIGGINS

---

**Bruce A. Riggins**

*Executive Vice President  
and Chief Financial Officer*

RESOLUTION NO. 09-110

**A RESOLUTION OF THE CITY COMMISSION OF THE  
CITY OF KEY WEST, FLORIDA, AUTHORIZING A LEASE  
RENEWAL FOR SOUTHERNMOST BEACH CAFE; PROVIDING  
FOR AN EFFECTIVE DATE**

NOW THEREFORE, BE IT RESOLVED BY THE CITY COMMISSION OF THE  
CITY OF KEY WEST, FLORIDA, AS FOLLOWS:

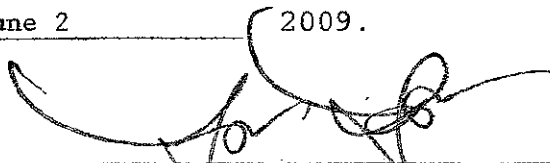
Section 1: That the attached lease agreement for the  
Southernmost Beach Café is approved.

Section 2: That this Resolution shall go into effect  
immediately upon its passage and adoption and authentication by the  
signature of the presiding officer and the Clerk of the Commission.

Passed and adopted by the City Commission at a meeting held  
this 5th day of May 2009.

Authenticated by the presiding officer and Clerk of the  
Commission on June 2, 2009.

Filed with the Clerk June 2 2009.

  
\_\_\_\_\_  
MORGAN MCPHERSON, MAYOR

ATTEST:

  
\_\_\_\_\_  
CHERYL SMITH, CITY CLERK



# EXECUTIVE SUMMARY



**CITY OF KEY WEST  
CITY MANAGERS OFFICE**

**TO: Jim Scholl  
City Commission**

**CC: Mark Finigan, Shawn D. Smith**

**FR: Marilyn Willbarger, RPA, CCIM**

**DT: April 27, 2009**

**RE: SMB Restaurant, LLC DBA Southernmost Beach Café Lease Renewal**

**ACTION:** This is a request to approve a lease renewal for the property located at 1405 Duval Street in accordance with City Ordinance 05-15, Sec 2-941 which provides for the negotiation of a lease renewal with an existing tenant one year prior to expiration. The negotiations have been completed and the proposed lease renewal is presented for your consideration.

**BACKGROUND:** The lease for the Southernmost Beach Café will expire in January of 2010 and pursuant to City Ordinance we provided public notice and entered into lease renewal negotiations with the current tenant.

There is no change in use anticipated in the lease renewal and the tenant will continue to operate an open air casual beach restaurant with alcoholic beverages which is the permitted use in the current ten year lease. Additionally, pursuant to City of Key West Code of Ordinances, Article II, Division 3, Section 18-88, 1405 Duval is excepted from the open container provision and the lease contemplates that Tenant's patrons may consume alcohol at this location in accordance with this ordinance.

The lease also states that the tenant will not to use any amplified music or other noise making devices that violate the City of Key West's Noise Ordinance and that the tenant will have the right to request special events permits in accordance with City Ordinance governing such events. The beach will remain open to the public and governed by rules for all public beaches in Key West.

The proposed renewal brings the base rental rate up to market and provides for percentage rent in addition to the increased base rent. The new rate is comparable to the base rents of other City owned properties leased to restaurant/ bar tenants. The new agreement also terminates the rent credit for beach and restroom cleaning therefore effectively raises the base rent from \$68,250 to \$150,000 per year. A comparison of the current and proposed lease is attached for your reference.

**FINANCIALS:**

As security for the payment of all amounts due under the lease, the Tenant has posted an irrevocable letter of credit in the amount of \$70,000.00 which may drawn upon by the City Attorney without any additional legal action. This Tenant has an excellent payment history and is not in default of any amounts currently due.

**RECOMMENDATION:**

Staff recommends approval of the action requested.

**ATTACHMENTS:**

Draft Lease

Lease Comparison

**SMB, LLC****CITY LEASE RENEWAL PROPOSAL****TENANT'S CURRENT LEASE**

<b>Demised Premises:</b>	Existing building containing approximately 4981 square feet, outdoor storage and waiting areas. The beach is a separate parcel and not included in the leased premises.	Entire parcel including beach and building area per the legal description in the lease.
<b>Use:</b>	No change in the existing permitted uses; Operation of a 150 seat open air casual beach restaurant/bar, sale and rental of beach accessories including chairs, umbrellas, snorkel gear, rafts etc. but excluding any motorized watercraft, which are the Tenant's permitted uses in the existing ten year lease and pre-date the commencement of that lease.	Operation of a restaurant, sale and rental of beach accessories
<b>Adjacent Beach:</b>	Beach shall remain open to the public for public purposes during hours established for public beaches in Key West and subject to all rules established for public beaches in Key West.	Beach shall remain open to the public for public purposes
Per City Ordinance Article II, Division 3, Sec. 18-88	Tenant's patrons may consume alcoholic beverages, after noon, in plastic containers not to exceed 16 ounces, one drink per patron at a time. Tenant may serve alcoholic beverages at special events held on the adjacent beach with permits/licenses.	Tenant may not serve alcohol on the beach.
Tenant to clean and maintain the beach area and public restrooms daily and Landlord will pay for the cost of the seaweed removal	Tenant to clean and maintain the beach area and public restrooms daily and Landlord will pay for the cost of the seaweed removal	Tenant to clean and maintain the beach area and public restrooms daily and Landlord will pay for the cost of the seaweed removal
<b>Term:</b>	Ten Years, effective May 1, 2009	Ten years expiring January 2010
<b>Base Rent:</b>	\$150,000 per year in year one, no cleaning credits	Currently \$97,255.70 less \$29,000 annual beach and restroom cleaning credit for a base rent of \$68,255.70
<b>Increase:</b>	5% Annually	Annual CPI
<b>Additional Rent:</b>	Tenant shall pay taxes including ad valorem tax, insurance and maintenance and repair costs (NNNN)	Tenant shall pay taxes including ad valorem tax, insurance and maintenance and repair costs (NNNN)
<b>Percentage Rent:</b>	6.5% in excess of the percentage rent base amount which will be established by dividing the then current base rent by 6.5%	6.5 % of sales over \$1,500,000
<b>Utilities:</b>	Tenant pays for all utility usage	Tenant pays for all utility usage
<b>Improvements:</b>	Tenant accepts the space in its current condition. Any structural improvements contemplated are subject to FEMA restrictions.	Major improvements were completed by the city and the tenant several years ago after hurricane destruction including the addition of ADA public restrooms



THE  
**RANKAUF**  
COMPANY

121 W. Long Lake Road, Third Floor – Suite 310  
Bloomfield Hills, Michigan 48304-2720  
248-645-1600  
Fax: 248 645-8939

May 15, 2009

**VIA FEDEX**

City of Key West  
Attn: Marilyn D. Wilbarger  
525 Angela Street  
Key West, FL 33041

Re: SMB Restaurant LLC

Dear Marilyn:

Enclosed are four copies of the Lease which have been executed by the Tenant per your request.

Very truly yours,



Stuart M. Kaufman

/lh  
Enclosures

City of Key West  
525 Angela Street  
Key West, FL 33041  
Attn: Marilyn Wilbarger

Dear Marilyn

Because the lease between SMB Restaurant LLC as assignee of Island Renovations Inc. (Tenant) and The City of Key West (Landlord) dated February 1, 2000 and covering the premises at 1405 Duval Street, Key West, FL. (the "Original Lease") is being terminated as of May 1, 2009 which is only three months into the last Lease Year of the Original Lease, Landlord and Tenant have agreed to a method of calculating the Percentage Rent that should be paid for said three month period (the "Prorated Percentage Rent") as follows:

The Prorated Percentage Rent shall be paid in February of 2010 based on the following calculation:

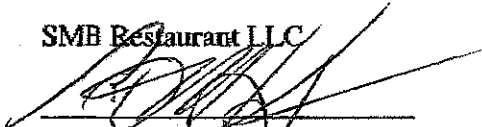
In February of 2010, the parties shall calculate the annual Percentage Rent for the period from February 1, 2009 to January 31, 2010 that would have been paid under the Original Lease had it not been terminated. Tenant shall then pay, prior to the end of February 2010, 3/12<sup>th</sup> of the amount so determined as the Prorated Percentage Rent.

The mathematical formula for the Prorated Percentage Rent calculation is as follows:

$$(((\text{Tenants Gross Sales for the period from February 1, 2009 to January 31, 2010}) - \$1,500,000.00)) \times .065) / 12) * 3$$

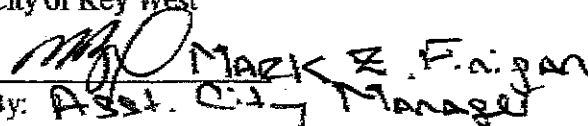
If this letter accurately sets forth our agreement, please so indicate by executing and returning the enclosed counter counterpart hereof.

SMB Restaurant LLC

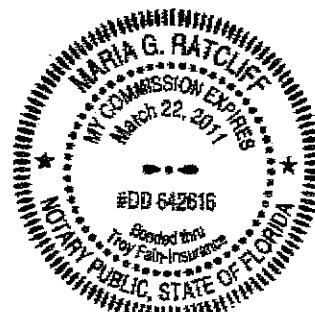
  
By: Stuart M. Kaufman  
Its: Managing Member

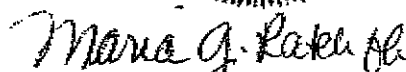
Confirmed and Agreed by:

City of Key West

  
By: Asst. City Manager  
Its: 5-13-09

✓ PL





# BRANCH BANKING AND TRUST COMPANY

ADDRESS: 1010 KENNEDY DRIVE KEY WEST, FL 34040-4134

PHONE NUMBER: 305-292-3806

CONTACT NAME: JAMES W HALL

## IRREVOCABLE STANDBY LETTER OF CREDIT

LETTER OF CREDIT NO. 9660970859 00002

DATE 05/21/2009

ADVISING BANK  CITY OF KEY WEST 525 ANGELA STREET KEY WEST, FL 33040-0000	APPLICANT  SMB RESTAURANT LLC 1405 DUVAL ST KEY WEST, FL 33040-3133
BENEFICIARY  City of Key West 525 Angela Street KEY WEST, FL 33040-0000	AMOUNT  \$150,000.00  EXPIRY DATE 05/21/2010 (FOR PRESENTATION AT OUR COUNTERS)

GENTLEMEN:

WE HEREBY ESTABLISH OUR IRREVOCABLE STANDBY LETTER OF CREDIT IN YOUR FAVOR

AVAILABLE BY YOUR DRAFT(S) Sight

DRAWN ON: "BRANCH BANKING & TRUST CO."

DRAFT(S) MUST BE MARKED - "DRAWN UNDER BRANCH BANKING AND TRUST COMPANY CREDIT NO. 9660970859 00002"

WHICH MUST BE ACCOMPANIED BY THIS LETTER AND THE FOLLOWING DOCUMENTATION:

Conditions for the City to draw upon this credit are:

1. That at the time of presentment, the city shall execute a draft that refers to this letter of credit and;
2. The draft presented by the City shall be payable solely to the City in the amount claimed by the City as due to the City for damages, costs, and/or attorneys' fees arising from default or non-payment pursuant to that certain lease agreement dated May 1, 2009, by and between the City of Key West, as Lessor, and SMB Restaurant, LLC, as Lessee; and
3. The City shall present along with this letter of credit and with the City's draft, the City's written certificate describing the default and/or non-payment for which the City makes draw against this letter of credit, which certificate shall be signed by the City Attorney and the City Manager, and which certificate shall state the specific amount of damages, interest, costs, penalties, and attorneys' fees of City, with regard to the lease agreement referred to herein above; and
4. No person or entity other than the City may make claim or present a draw under this letter of credit. No person or entity other than City is an intended beneficiary with rights to enforce this letter of credit. Issuing bank shall be entitled to assume as true the statement of default or non-payment in the certificate presented to Bank with any draws on this letter of credit; and
5. The City's presentment pursuant to this letter of credit shall not affect the City's right to pursue any and all remedies against Lessee contained in the lease agreement referred to herein above, including eviction; and
6. It is a condition of this letter of credit that it will be automatically extended up to June 30, 2010 unless we (BB&T) send written notification at least 30 days prior to the expiration date hereof that we (BB&T) elect not to extend this letter of credit for such additional period.

---

**Lease Agreement**

between

**CITY OF KEY WEST**

as Landlord

and

**SMB RESTAURANT, LLC**

as Tenant

Dated 15 of MAY 1, 2009

THIS LEASE is made as of the 1st day of May, 2009 by and between the LANDLORD and TENANT identified below:

**1. INFORMATION PROVISIONS:**

1.1 LANDLORD'S NAME & MAILING ADDRESS:  
CITY OF KEY WEST  
525 ANGELA STREET  
KEY WEST, FL 33040

1.2 TENANT'S NAME & MAILING ADDRESS:  
SMB Restaurant, LLC  
121 West Long Lake Road, 3<sup>rd</sup> Floor  
Bloomfield Hills, MI 48304

TENANT'S TRADE NAME: **Southernmost Beach Cafe**

1.3 GUARANTOR (S) AND ADDRESS: The Rankauf Company, LLC, 121 West Long Lake Road, 3<sup>rd</sup> Floor, Bloomfield Hills, MI 48304

1.4 DEMISED PREMISES (Section 2): as per EXHIBIT "A" located at 1405 Duval Street (hereinafter referred to as the "Property").

NET USABLE SQUARE FEET CONSISTING OF A 4981 SQUARE FOOT BUILDING, AN OUTDOOR COVERED STORAGE AREA, AND WAITING AREA AS CROSSHATCHED ON EXHIBIT "A"

EXPANSION/RIGHT OF FIRST REFUSAL: None

1.5 TERM (Section 3.): TEN (10) YEARS

1.5.1 COMMENCEMENT DATE: May 1, 2009 as acknowledged by TENANT'S written statement

1.5.2 RIGHT TO TERMINATE: None

1.5.3 RIGHT TO RENEW: Per Key West Code of Ordinances Sec.2-941. Leases or as amended

1.6 MINIMUM RENT FOR TERM (Section 4): The base rent and base rent increases for the term and any renewals thereof as per EXHIBIT "B" attached hereto and incorporated herein.

1.6.1 ADDITIONAL RENT: (Section 4.4 (e): Tenant shall pay Real Estate Taxes, Insurance, Sales, Use or Excise Taxes together with Administrative fees and any and all other sums of money or charges required to be paid by TENANT pursuant to the provisions of this lease.

1.6.2 RENT PAYMENT DUE DATE: Payable in advance on the first (1<sup>st</sup>) of each and every month of the term hereof.

1.6.3 LATE CHARGE: 15% of the amount in arrears if received after the fifth day of each and every month together with an administrative fee of \$50.00 for processing late payments.



- 1.6.4 **PERCENTAGE RENT:** Six and One Half Percent 6.5% of TENANT'S Gross Sales in excess of the "Percentage Rent Base Amount" as per EXHIBIT "B".
- 1.6.5 **HOLD OVER RENT:** 150% of the Minimum Base rent during the last year of the expiring term.
- 1.6.6 **RENT CONCESSIONS:** None
- 1.7 **SECURITY DEPOSIT (Section 5):** Tenant shall maintain an irrevocable letter of credit in the amount of \$150,000 throughout the term of this lease and until such time as the tenant has vacated the Demise Premises and the LANDLORD has determined that the TENANT has no outstanding amounts due under this lease.
- 1.8 **PERMITTED USE (Section 6):** The principal business is the operation of a 150 seat open air casual beach restaurant with accessory alcohol sales. Additionally, the sale and rental of beach accessories such as chairs, umbrellas, snorkel gear, inflatable rafts but excluding any motorized watercraft is permitted. TENANT may hold events on the beach that are not subject to special events permits and do not materially interfere with the public access and use of the beach. TENANT shall have the right to hold five (5) special events per year. The maximum of five (5) special events pursuant to City Ordinance is applicable to both the demised premises and the adjacent public beach. Tenant shall clean and maintain the beach and public restrooms daily however TENANT shall have no obligation for beach sand re-nourishment.
- 1.9 **INSURANCE: (Section 9)** \$1,000,000 commercial liability minimum per occurrence, all all risk property insurance, including property damage, hazard and theft coverage and workers compensation coverage as required by the provisions of Florida statute.
- 1.10 **ASSIGNMENT OR SUBLETTING: (Section 10)** Permitted with LANDLORD'S approval
- 1.11 **UTILITIES: (Section 17)** TENANT shall pay for all utilities including garbage, electricity, gas, water and sewer serving the Demised Premises and the public restrooms.

INITIALS: LANDLORD \_\_\_\_\_

TENANT \_\_\_\_\_

WITNESSETH:

That the LANDLORD and the TENANT, for and in consideration of the keeping by the parties of their respective obligations hereinafter contained, as well as for one dollar (\$1.00) and other good and valuable consideration by each of the parties unto the other, in hand paid simultaneously with the execution and delivery of these presents, the receipt of which is hereby acknowledged, have agreed as follows:

2. **DEMISED PREMISES** - Upon the terms and conditions hereinafter set forth, and in consideration of the payment from time to time by the TENANT of the rents hereinafter set forth, and in consideration of the performance continuously by the TENANT of each and every one of the covenants and agreements hereinafter contained by the TENANT to be kept and performed, the LANDLORD does hereby lease, let, and demise unto the TENANT, and the TENANT does hereby

lease of and from the LANDLORD, the following Demised Premises situated, lying, and being in Monroe County, Florida: That portion of the Property outlined and/or crosshatched on Exhibit "A" which depicts the Net Usable Square Feet of the Demised Premises. The Net Usable Square Feet is defined as all interior floor space, any second floor space, storage, covered dining areas and commercially used outdoor areas or any other area set aside for the exclusive use and economic benefit of the Tenant and containing the approximate dimensions and area. It is agreed that the Net Usable Square Feet for the purpose of any calculations which are based on Net Usable Square Feet is as stated in Section 1.4. LANDLORD reserves the right to re-measure the Demised Premises from time to time, measured in accordance with the applicable published ANSI standards for measurement performed by a professional engineering firm, and to adjust the TENANT'S Net Usable Square Feet if applicable. TENANT accepts the Demised Premises in an "as is", "where is" condition and acknowledges that LANDLORD has no obligations for any construction or improvements in connection with TENANT'S occupancy of the Demised Premises. TENANT also acknowledges that any additional improvements to the Demised Premises are subject to applicable FEMA regulations regarding the same.

Expansion/Right of First Refusal -None

3. **TERM** - The term of this Lease shall be for ten (10) years which shall commence on May 1, 2009 and shall end at midnight on April 30, 2019 unless sooner terminated as provided for herein. Upon occupancy TENANT shall furnish LANDLORD a written statement stating the TENANT has accepted the Demised Premises for occupancy and setting forth the actual commencement and expiration dates of the Lease. TENANT'S written statement shall become attached to and incorporated into this lease Exhibit "D". In the absence of TENANT'S written statement the lease term shall remain as stated above A Lease Year is the twelve-month period beginning on the commencement date of each year and ending at the conclusion of the same date one year later. If possession of the Demised Premises shall for any reason not be delivered to Tenant on the Commencement Date, this Lease shall nevertheless continue in full force and effect, and no liability whatsoever shall arise against LANDLORD out of any delay other than the abatement of rent.

Right to Terminate -None

Right to Renew - Per Key West Code of Ordinances Sec.2-941 Leases

4. **RENT** - All rentals provided for herein shall be payable in advance, without prior demand therefore and without deductions or setoffs for any reason whatsoever on the first day of each and every month of the term hereof.

4.1 **Late Charges.** Any monthly rental not received by the fifth day of the month shall incur a late fee equal to fifteen percent 15% of the amount in arrears. In addition, all payments received after the due date shall incur a \$50.00 administrative fee to cover the costs of collecting and processing late payments. LANDLORD shall have no obligation to accept less than the full amount of all installments of rental, additional rental or other amounts due hereunder and interest thereon which are due and owing by TENANT to LANDLORD. If LANDLORD accepts less than the full amount owing, LANDLORD may apply the sums received toward such TENANT'S obligations, as LANDLORD shall determine in its sole discretion, without waiving LANDLORD'S remedies for default.

4.2 **Interest on Rent.** Rent and additional rent not paid within fifteen (15) days of when due shall bear interest from the date due until paid at the highest rate permitted by law.

4.3 **Obligation to Survive.** TENANT'S obligation to pay rent that is accrued and unpaid hereunder shall survive the expiration or termination of the Lease.

4.4 The rent reserved under this Lease for the term hereof shall be and consist of:

(a) Beginning with the commencement date and throughout the term of this Lease, TENANT agrees to pay to the LANDLORD as and for minimum rent for the Demised Premises the annual amount, in equal monthly instalments, in advance, on the first day of each and every calendar month, as per EXHIBIT "B". In the event the rent commencement date is other than the first day of a calendar month, the rent for the partial first calendar month of the term will be prorated on a daily basis and payable on the commencement date.

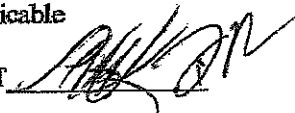
(b) Simultaneously with each such payment, TENANT agrees to pay to LANDLORD any sales, use or excise tax imposed or levied against rent or any other charge or payment required hereunder to be made by TENANT which tax has been imposed or levied by any governmental agency having jurisdiction thereof, this shall include any new taxes imposed during the term of this Lease which are in addition to or in substitution for any such tax which is presently imposed.

Commencing with the 1st day of the Term, TENANT agrees to pay, as Additional Rent, the Real Estate Tax Expense which shall include all real estate taxes and assessments both general and special imposed by federal, state or local governmental authority or any other taxing authority having jurisdiction over the Property against the land, buildings, store rooms, and all other improvements together with any and all expenses incurred by LANDLORD in negotiations, appealing or contesting such taxes and assessments Ad valorem real property taxes for each calendar year hereunder shall be paid by the TENANT directly to the taxing authority in the month of November of that calendar year and proof of payment of same shall be delivered to LANDLORD promptly after payment.

Should any governmental taxing authority acting under any present or future law, ordinance or regulation, levy, assess or impose a tax, excise and/or assessment (other than an income or franchise tax) upon or against the rentals payable by TENANT to LANDLORD, whether by way of substitution for, or in addition to, any existing tax on land and buildings or otherwise, or any other substitute tax, the proceeds of which are to be used to fund the same governmental functions as were funded by ad valorem taxes, TENANT shall be responsible for the amount thereof, as the case may be, as additional rent, the same shall be payable in the manner provided for in the preceding paragraphs. Substitute taxes as referred to above in this Section shall include, without limitation, any surtax on parking spaces.

Initial here if applicable

TENANT



LANDLORD



(d) In addition to the foregoing rent, TENANT agrees to pay LANDLORD as Percentage Rent a sum equal to six and one half percent (6.5%) multiplied by an annual Gross Sales per Lease Year in excess of the Percentage Rent Base Amount. The Percentage Rent Base Amount is calculated by dividing the current annual Base Rent by six and half percent (6.5%). Within twenty (20) days following the end of each month of each Lease Year, TENANT shall forward to LANDLORD a statement of Gross Sales together with an accurate and complete copy of the State of Florida Department of Revenue, Sales and Use Return Form DR-15 (or such forms as the State of Florida shall hereafter substitute for said form) showing the full amount of TENANT'S Gross Receipts

derived from the Demised Premises during the previous month. The statement of Gross Sales must be in affidavit form. TENANT is subject to a fifty-dollar (\$50.00) late submission penalty should TENANT not furnish to LANDLORD copies of Form DR-15 by the twentieth (20th) day of each month. Failure of Tenant to timely submit any monthly report shall entitle LANDLORD to estimate Gross Sales based upon available data (with a reconciliation upon receipt of the final report), and TENANT shall be obligated to pay percentage rent on such estimated Gross Sales. If by the end of any such preceding month the Gross Sales in the Demised Premises during such Lease Year shall exceed the Percentage Base Rent Amount, TENANT shall pay to LANDLORD, at the time of delivery of said Statement, an amount equal to the Percentage Rent times the Gross Sales exceeding the Percentage Rent Base Amount, less the Percentage Rent, if any, previously paid by TENANT to LANDLORD during that Lease Year. TENANT shall also furnish to LANDLORD within thirty (30) days after the expiration of each full Lease Year, a complete statement, certified by an independent certified public accountant, showing in all reasonable detail the amount of Gross Sales made by TENANT from the Demised Premises during the preceding Lease Year.

"Gross Sales" shall mean the amount of sales of all merchandise or services sold or rendered at or from the Demised Premises by TENANT or any sub-TENANT, licensee, etc. TENANT may deduct from Gross Sales: (i) any refunds to customers, provided they have been included in Gross Sales; and (ii) the amount of any sales tax levied upon retail sales and payable over to the appropriate governmental authority. TENANT agrees to keep, at its principal office, records in accordance with generally accepted accounting practices, in which said Gross Sales shall be recorded. Such records shall be open for inspection by LANDLORD or its agents, including accountants retained for that purpose, during reasonable business hours for the Term and for at least 3 years thereafter. If any audit shows that the amount of Gross Sales on the statement was understated by more than 1% for any year, then TENANT (in addition to paying the Percentage Rent due for such understatement) shall pay to LANDLORD the reasonable cost of the audit within ten (10) days after TENANT'S receipt of LANDLORD'S invoice. If such understatement is willful and/or fraudulent, LANDLORD shall have the option, upon ten (10) days notice to TENANT, to terminate this Lease on the date specified in such notice and Tenant shall remain liable for all rent and other charges under this lease for the full term hereof.

(e) **Additional Rent.** Any and all other sums of money or charges required to be paid by Tenant pursuant to the provisions of this Lease, whether or not the same be so designated, shall be considered as "Additional Rent", and shall be payable and recoverable in the same manner as Rent. However, such Additional Rent shall be due upon demand and failure to pay such additional rent within seven (7) days shall be deemed a material breach of this lease. If Landlord shall make any expenditure for which Tenant is liable under this Lease and for which Tenant has not paid, the amount thereof shall be deemed Additional Rent due and payable by as indicated above. The LANDLORD shall have the same remedies for TENANT'S failure to pay said additional rental the same as for non-payment of rent. LANDLORD, at its election, shall have the right to pay or do any act which requires the expenditure of any sums of money by reason of the failure or neglect of TENANT to perform any of the provisions of this Lease, and in the event LANDLORD shall, at its election, pay such sums or do such acts requiring the expenditure of monies, TENANT agrees to pay LANDLORD, upon demand, all such sums, and the sums so paid by LANDLORD and any expenses incurred by LANDLORD in the payment of such sums together with interest thereon at the highest rate permitted by law from their due date through the date they are paid by TENANT shall be deemed additional rent and shall be payable and collectible as such. Rent shall be made payable to the LANDLORD as stated in Section 1.1 hereof.

(f) **Holding Over.** It is agreed that in the event of TENANT holding over after the termination of this lease, thereafter the tenancy shall be from month to month in the absence of a written agreement

to the contrary; the TENANT shall pay to LANDLORD a monthly occupancy charge equal to One Hundred Fifty (150%) Percent of the monthly rental for the last lease year for each month from the termination or expiration of this Lease until the Demised Premises are delivered to the LANDLORD in the condition required herein, and LANDLORD'S right to damages for such illegal occupancy shall survive. In addition, TENANT shall pay all other charges payable by TENANT under this Lease

(g) Rent Concessions. None

5. **SECURITY - TENANT will maintain an irrevocable letter of credit for the benefit of the LANDLORD and in accordance with the LANDLORD'S requirements for such letter of credit, in a sum equal to \$150,000.00 USD throughout the term of this lease and until such time as the tenant has vacated the Demise Premises and the LANDLORD has determined that the TENANT has no outstanding amounts due under this lease, the receipt of which is hereby acknowledged as security for the payment by TENANT of the rents herein agreed to be paid by TENANT and for the faithful performance by TENANT of the terms, conditions and covenants of this Lease. It is agreed that LANDLORD, at LANDLORD'S option, may at any time apply said sum or any part thereof toward the payment of the rents and any other sum payable by TENANT under this Lease, and/or toward the performance of each and every covenant under this Lease, but such covenants and TENANT'S liability under this Lease shall thereby be discharged only pro tanto; that TENANT shall remain liable for any amounts that such sum shall be insufficient to pay; that LANDLORD may exhaust any or all rights and remedies against TENANT before resorting to said sum, but nothing herein contained shall require or be deemed to require LANDLORD to do so.**

6. **USE OF THE DEMISED PREMISES -TENANT shall use the Demised Premises for the purposes of:**

The principal business is the operation of a 150 seat open air casual beach restaurant with accessory alcohol sales. Restaurant sales, excluding alcohol, must generate at least 51 % of the revenue and the sale of food must occur during all hours the restaurant is open for business.

Sale and rental of beach accessories including chairs, umbrellas, snorkel gear, inflatable rafts but excluding any motorized watercraft

It is the intent of the parties that the beach and restrooms shall remain open to the public for public purposes during hours established for public beaches in Key West and subject to all rules established for public beaches in Key West with any exceptions provided for by specific ordinance.

TENANT may hold events on the beach that are not subject to special events permits and do not materially interfere with the public access and use of the beach. TENANT shall have the right to hold five (5) special events per year. The maximum of five (5) special events pursuant to City Ordinance is applicable to both the demised premises and the adjacent public beach. TENANT shall notify LANDLORD of its intended date of use and seek permits and/or licenses necessary in accordance with City Ordinance governing special events. TENANT may serve alcoholic beverages at special events held on the adjacent beach in accordance with the requirements of the special event permit.

TENANT will clean and maintain the beach area and public restrooms daily however TENANT shall have no obligation for beach sand re-nourishment.

TENANT further agrees:

(a) To operate 100% of the Demised Premises for the entire term of this lease for a minimum of

eight (8) hours per day, seven days per week pursuant to the highest reasonable standards of its business category, with sufficient personnel to service its trade.

(b) With respect to the Property, not to display any merchandise, solicit business or distribute advertising material beyond the Demised Premises, nor in any manner use any other areas for purposes other than for their intended common use and not to obstruct any part thereof.

(c) Not to display any banners, pennants, searchlights, window signs, balloons, or similar temporary advertising media on the exterior of the Demised Premises.

(d) Not to commit waste in the Demised Premises or Common Areas and to keep the Demised Premises and immediate adjacent areas including, without limitation, adjacent sidewalks, in a safe, neat, clean and orderly condition and to maintain and repair any lighting or signs under any canopy immediately in front of the Demised Premises.

(e) Not to use the Demised Premises or permit the same to be used in any manner which violates any law, ordinance or constitutes a nuisance; for lodging purposes; that may injure the reputation of the Property or annoy, inconvenience or damage its patrons or other TENANT'S; or that would constitute an extra-hazardous use or violate any insurance policy of TENANT, LANDLORD or any other TENANT in the Property or increase the cost thereof.

(f) To keep all garbage, refuse and solid waste inside the Demised Premises in the kind of containers specified by LANDLORD, or to place the same outside the Demised Premises, prepared for collection, in the manner and at the times and places designated by LANDLORD or the appropriate disposal company. TENANT agrees not to burn or permit any burning of garbage or refuse on the Demised Premises or any part of the Property. TENANT further agrees that, upon LANDLORD'S instruction, TENANT shall separate garbage for recycling and deposit the separate garbage in the receptacle designated by LANDLORD. TENANT further agrees to make every effort to recycle all glass, metal, paper and plastic refuse and solid waste. TENANT agrees to collect the seaweed and debris from the beach and deposit in a refuse container and LANDLORD will pay for the cost of the disposal thereof.

(g) TENANT shall contract directly with the pertinent governmental authority or disposal company and shall be responsible for all fees and costs of removal and disposal of solid waste, garbage, and refuse, including but not limited to, impact fees and dumpster rental, with the exception of seaweed and beach debris. TENANT shall indemnify, save harmless and defend LANDLORD from and against any loss, claim, injury, damage or expense arising out of or related to the generation, storage, or removal or disposal of TENANT'S garbage, refuse or solid waste.

(h) To use its best efforts to cause all trucks serving the Demised Premises to load and unload from the hours of 7:00 a.m. to 11:00 a.m. and not to permit such trucks to service through the front entrance of the Demised Premises except when no other entrance is available.

(i) To take no action that would: (i) violate LANDLORD'S contracts if any, affecting the Property or (ii) cause any work stoppage, picketing or cause any manner or interference with LANDLORD or, occupants, customers or any person lawfully in and upon the Property.

(j) Not to use amplified music or any other noise making machinery or devices that are in violation of the City of Key West Noise ordinance.

(k) To abide by and observe all reasonable rules and regulations established from time to time by

LANDLORD and LANDLORD'S insurance carrier with respect to the operation of the Property and its Common Areas. Rules and regulation are attached and incorporated herein as EXHIBIT "C".

(l) Not to conduct any auction, fire, bankruptcy or selling-out sale on or about the Demised Premises except in strict compliance with City Code Chapter 18.

(m) TENANT shall not (either with or without negligence) cause or permit the escape, disposal or release of any biologically or chemically active or other hazardous substances or materials which TENANT or its agents brought onto the Property. TENANT shall not allow storage or use of such materials or substances in any manner not sanctioned by law or by the highest standards prevailing in the industry for the storage and use of such substances or materials, nor allow to be brought into the Demised Premises or the Property any such materials or substances except to use in the ordinary course of TENANT'S business, and then only after written notice is given to LANDLORD of the identity of such substances or materials. Without limitation, hazardous substances and materials shall include those described in the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended, 42 U.S.C. Section 9601 et seq., the Resource Conservation and Recovery Act, as amended, 42 U.S.C. Section 6901 et seq., any applicable state or local law and the regulations adopted under these acts. In addition, TENANT shall execute affidavits, representations and the like from time to time at LANDLORD'S request concerning TENANT'S best knowledge and belief regarding the presence of hazardous substances or materials in the Demised Premises. In all events, TENANT shall indemnify LANDLORD in the manner elsewhere provided for in this Lease against any liability resulting from any release of hazardous substances or materials in the Demised Premises or Property by TENANT or its agents, while TENANT is in possession or caused by TENANT or persons acting under TENANT which is due to hazardous substances that TENANT or its agents brought onto the Demised Premises or Property.

7. **COVENANT OF QUIET POSSESSION** - So long as TENANT pays all of the rent and charges due herein, TENANT shall peaceably and quietly have, hold, and enjoy the Demised Premises throughout the term of this Lease without interference or hindrance by LANDLORD or any person claiming by, through, or under LANDLORD.

8. **INDEMNIFICATION** - TENANT does hereby agree to indemnify, defend and save LANDLORD harmless from and against any and all liability for any injury to or death of any person or persons or damage to property (including adjoining property for environmental damage) in any way arising out of or connected with the conditions, use or occupancy of the Demised Premises, or in any way arising out of the activities of TENANT, its agents, employees, licensees or invitees on the Demised Premises and/or the adjacent public beach and from reasonable attorney's fees, incurred by LANDLORD in connection therewith, excepting, however, liability caused by LANDLORD'S gross negligence in its failure to perform any of LANDLORD'S covenants, obligations or agreements of this Lease.

9. **TENANT'S INSURANCE** - TENANT covenants and agrees with LANDLORD that TENANT shall:

(a) At TENANT'S sole cost and expense, during the entire Term hereof, procure, pay for and keep in full force and effect; (i) an occurrence form commercial general liability policy, covering the Demised Premises and the operations of Tenant and any person conducting business in, on or about the Demised Premises or TENANT'S permitted uses on the adjacent public beach in which the limits with respect to liability and property damage shall not be less than One Million (\$1,000,00.00) Dollars per occurrence (ii) all risk property insurance, including property damage, hazard and theft coverage, written at replacement cost value and a replacement cost endorsement insuring the

Property, TENANT'S improvements and betterments, fixtures, furnishings, equipment and any other property belonging to TENANT; and (iii) workers compensation coverage as required by the provisions of Florida statute. Any consignment agreement used by TENANT must provide that consignor acknowledge that the LANDLORD does not have any liability whatsoever for any damage which may be done to items left in the Demised Premises on consignment. The TENANT must provide the LANDLORD with a copy of any consignment agreement used by TENANT regarding Demised Premises. LANDLORD shall not be responsible for damage to any property belonging to TENANT or consignor. TENANT completely indemnifies the LANDLORD with regard to any claims made by any consignor for any reason. From time to time during this Lease, at LANDLORD'S request, TENANT shall (i) procure, pay for and keep in full force and effect such other insurance as LANDLORD shall require and (ii) increase the limits of such insurance as LANDLORD may reasonably require.

(b) All policies of insurance required to be carried by TENANT pursuant to this lease shall be written by responsible insurance companies authorized to do business in Florida with an AM Best rating of A-VI or better. Any such insurance required to be carried by TENANT hereunder may be furnished by TENANT under any blanket policy carried by it or under a separate policy therefore. A copy of each paid up policy evidencing such insurance or a certificate of the insurer, certifying that such policy has been issued, providing the coverage required by this Lease and containing provisions specified herein, shall be delivered to LANDLORD prior to the commencement of the Term of this Lease and, upon renewals, but not less than sixty (60) days prior to the expiration of such coverage. In the event TENANT shall fail to procure such insurance, LANDLORD may, at its option, procure the same for the account of TENANT, and the cost thereof shall be paid to LANDLORD as an additional charge upon receipt by TENANT of bills therefore, together with an administrative fee equal to fifteen (15%) percent to cover the cost of the LANDLORD'S efforts to procure such policy.

(c) Each policy evidencing insurance required to be carried by TENANT pursuant to this Lease shall contain the following provisions and/or clauses: (i) a provision that such policy and the coverage evidenced thereby shall be primary and non-contributing with respect to any policies carried by LANDLORD; (ii) a provision naming LANDLORD and any other parties in interest as designated by LANDLORD as an additional insured (except with respect to worker's compensation insurance); and (iii) a provision that the insurer will not cancel, materially change or fail to renew the coverage provided by such policy without first giving LANDLORD thirty (30) days prior written notice.

Any general liability or other policy insuring the LANDLORD does not provide any contributing or excess coverage for TENANT. The policies TENANT procures for TENANT'S exposure are the only coverage available to TENANT.

**10. ASSIGNMENT AND HYPOTHECATION** - This Lease is not transferable or assignable and may not be hypothecated nor sublet without the prior written consent of the LANDLORD which may be withheld and shall be at the sole discretion of the LANDLORD.

Any assignment or sub-letting, even with LANDLORD'S consent shall not relieve TENANT from liability for payment of Rent or from the obligation to keep and be bound by the agreements of this Lease. The acceptance of Rent from any other person shall not be deemed to be a waiver of any of the agreements of this Lease or to be consent to the assignment for the benefit of creditors or by operation of law and shall not be effective to transfer any rights to any assignee without prior consent of LANDLORD. In the event TENANT wishes to assign this Lease and LANDLORD consents to such assignment, LANDLORD may charge a reasonable fee, not to exceed \$500.00 to help offset any costs LANDLORD may have in preparing such assignment, or in examining the information, financial statements, operating history, references, etc., necessary to effectuate same. Any



assignment, transfer, hypothecation, mortgage, or subletting without LANDLORD'S written consent shall give LANDLORD the right to terminate this Lease and to re-enter and repossess the Demised Premises and the LANDLORD'S right to damages shall survive.

If the TENANT is a corporation, then a sale or transfer of a controlling interest in the corporation by sale of stock or otherwise shall constitute an assignment for purposes of this provision.

**11. SUBORDINATION** - This Lease, and all rights of TENANT hereunder, are and shall be subject and subordinate to all mortgages, bond indentures and any other financing instrument (hereinafter referred to as security agreements) which may now or hereafter affect the Demised Premises and to each and every advance made or hereafter to be made under such security agreements and to all renewals, modifications, replacements and extensions of such security agreements and spreaders and consolidations of such security agreements. This paragraph shall be self operative and no further instrument of subordination shall be required to make it effective, however, TENANT shall promptly execute and deliver any instrument reasonably requested to evidence such subordination.

If the holder of any such security instrument shall succeed to the rights of LANDLORD under this Lease, then at the request of such party so succeeding to the LANDLORD'S rights and upon such successor LANDLORD'S written agreement to accept TENANT'S attornment, TENANT shall attorn to such successor LANDLORD and will execute such instruments as may be necessary or appropriate to evidence such attornment. Upon such attornment, this Lease shall continue in full force and effect as if it were a direct Lease between the successor LANDLORD and TENANT upon all the terms, conditions, and covenants as are set forth in this Lease and shall be applicable after such attornment.

TENANT shall deliver to LANDLORD or the holder of any such security instrument or auditors, or prospective purchaser or the owner of the fee, when requested by LANDLORD, a certificate to the effect that this Lease is in full force and that LANDLORD is not in default therein, or stating specifically any exceptions thereto. Failure to give such a certificate within ten business days after written request shall be conclusive evidence that the Lease is in full force and effect and LANDLORD is not in default and in such event, TENANT shall be stopped from asserting any defaults known to TENANT at that time.

## **12. CONDEMNATION**

(a) It is further understood and agreed that if at any time during the continuance of this Lease the legal title to the Demised real estate or the improvements or buildings located thereon or any portion thereof be taken or appropriated or condemned by reason of eminent domain, there shall be such division of the proceeds and awards in such condemnation proceedings and such abatement of the fixed rent and other adjustments made as shall be just and equitable under the circumstances. If the LANDLORD and the TENANT are unable to agree upon what division of the condemnation award, abatement of fixed rent, or other adjustments are just and equitable within thirty (30) days after such award has been made, then the matters in dispute shall, by appropriate proceedings, be submitted to a court having jurisdiction of the subject matter of such controversy for its decision and determination of the matters in dispute. If the legal title to the entire Demised Premises be wholly taken by condemnation, or if the portion taken will prevent the Demised Premises from being used for the purpose the TENANT intends, this Lease shall be canceled.

(b) In general, it is the intent and agreement of the parties that upon condemnation, the parties hereto shall share in the condemnation award to the extent that they would be entitled to receive compensation and damages under the Florida law for the depreciation, damage, or destruction of their interests by the exercise of the right of eminent domain. In no event shall TENANT be permitted to

receive a share based on the value of the land or buildings, and/or improvements.

### 13. TENANT'S DEFAULT

(a) If the TENANT shall fail to pay any of the taxes or assessments herein provided for, or in case of the sale of or forfeiture of the Demised Premises or any part thereof during the demised term for non-payment of any tax or assessment; or in case the TENANT shall fail to keep insured the building or improvements which are now or which may at any time hereafter be upon the Demised Premises, as herein provided for; or shall fail to spend insurance money, as herein provided for; or if the TENANT shall fail to perform any of the covenants of this Lease by it to be kept and performed; then, in any of such events, except in the event of non payment of rent, upon ten (10) business days written notice, within which the TENANT may cure, and upon its failure to cure, it shall and may be lawful for the LANDLORD, at its election, to declare the demised term ended and to re-enter upon said Demised Premises, building, and improvements situated thereon, or any part hereof, either with or without process of law, the TENANT hereby waiving any demand for possession of the Demised Premises and any and all buildings and improvements then situated thereon. In the event of nonpayment of rent, LANDLORD may assert its right of notice and eviction pursuant to Chapter 83, Florida Statutes.

(b) Or, the LANDLORD may have such other remedies as the law and this instrument afford, and the TENANT covenants and agrees that upon the termination of said demised term, at such election of the said LANDLORD, or in any other way, TENANT will surrender and deliver up the Demised Premises and property (real and personal) peaceably to the LANDLORD, its agent, or attorneys, immediately upon the termination of the said demised term. If the TENANT, its agents, attorneys, or shall hold the Demised Premises or any part thereof, one (1) day after the same should be surrendered according to the terms of this Lease, it shall be deemed guilty of forcible detainer of the Demised Premises under the statute and shall be subject to eviction or removal, forcibly or otherwise, with or without process of law.

**(c) BANKRUPTCY OF TENANT. IN THE EVENT TENANT FILES ANY FORM OF BANKRUPTCY, LANDLORD SHALL BE ENTITLED TO IMMEDIATE TERMINATION OF THE AUTOMATIC STAY PROVISIONS OF 11 U.S.C. §362, GRANTING THE LANDLORD COMPLETE RELIEF AND ALLOWING THE LANDLORD TO EXERCISE ALL OF HIS LEGAL AND EQUITABLE RIGHTS AND REMEDIES, INCLUDING, WITHOUT LIMITATION, THE RIGHT TO TERMINATE THIS LEASE AND DISPOSSESS TENANT FROM THE DEMISED PREMISES IN ACCORDANCE WITH FLORIDA LAW. ADDITIONALLY, TENANT AGREES NOT TO DIRECTLY OR INDIRECTLY OPPOSE OR OTHERWISE DEFEND AGAINST THE LANDLORD'S EFFORT TO GAIN RELIEF FROM ANY AUTOMATIC STAY. THE LANDLORD SHALL BE ENTITLED AS AFORESAID TO THE LIFTING OF THE AUTOMATIC STAY WITHOUT THE NECESSITY OF AN EVIDENTIARY HEARING AND WITHOUT THE NECESSITY OR REQUIREMENT OF THE LANDLORD TO ESTABLISH OR PROVE THE VALUE OF THE LEASEHOLD, THE LACK OF ADEQUATE PROTECTION OF HIS INTEREST IN THE LEASEHOLD, OR THE LACK OF EQUITY IN THE SAME. TENANT SPECIFICALLY AGREES AND ACKNOWLEDGES THAT THE LIFTING OF THE AUTOMATIC STAY HEREUNDER BY THE APPROPRIATE BANKRUPTCY COURT SHALL BE DEEMED TO BE "FOR CAUSE" PURSUANT TO SECTION 362(D)(1).**

(d) Where the alleged default consists of some alleged violation of any term of this Lease, other than the payments of money, including rent, the LANDLORD may not declare this Lease in default until such violation shall have continued for ten (10) days after the LANDLORD shall have given the

TENANT written notice of such violation, and TENANT shall not have undertaken, during said ten (10) day notice period, to cure said violation by vigorous and affirmative action, provided, however, that nothing herein contained shall be construed as precluding the LANDLORD from having such remedy as may be and become necessary in order to preserve the LANDLORD'S right and interest of the LANDLORD in the Demised Premises and in this Lease, even before the expiration of the grace or notice periods provided for in this paragraph, if, under particular circumstances then existing, the allowance of such grace or the giving of such notice would prejudice or endanger the rights and estate of the LANDLORD in this Lease and in the Demised Premises. With respect to the payment of the insurance premiums, the same must be paid at least fifteen (15) days prior to the time when the policies would lapse for the failure to pay premiums thereon, and evidence of such payment given to the LANDLORD without any written notice being required to be served upon the TENANT in connection therewith.

(e) All default and grace periods shall be deemed to run concurrently and not consecutively.

(f) It is mutually covenanted and agreed that the various rights, powers, options, elections, privileges, and remedies of the LANDLORD contained in this Lease shall be construed as cumulative and no one of them shall be construed as being exclusive of the other or exclusive of any rights or priorities allowed by law.

(g) It is further covenanted and agreed by and between the parties hereto that the right given to the LANDLORD in this Lease to collect the rent that may be due under the terms of this Lease by any proceeding under same, or the right to collect any additional rent, money, or payments due under the terms of this Lease by any proceedings under same, or the right given the LANDLORD to enforce any of the terms and provisions of this Lease shall not in any way affect the right of such LANDLORD to declare this Lease void and the terms ended hereby, as herein provided, when default is made in the payment of said rent or when default is made by the TENANT in any of the terms and provisions of this Lease.

(h) If at any time, by reason of the failure of the TENANT to keep and perform any covenant or agreement which, under the terms of this Lease, the TENANT is bound and obligated to keep and perform, it becomes necessary for LANDLORD to employ an attorney to protect the rights and interests of the LANDLORD in the property demised or to enforce the Lease or proceed under it in any particular, then in any of such events, the TENANT will owe and will pay unto LANDLORD all costs of Court and reasonable attorneys fees incurred or expended by the LANDLORD in taking such actions, including actions taken in all trial and appellate courts.

14. **TENANT'S REPAIRS** - The TENANT covenants and agrees with the LANDLORD that during the continuance of this Lease, the TENANT shall be solely responsible for maintaining the Demised Premises in a clean, sanitary and safe condition in accordance with the laws of the State of Florida and in accordance with all directions, rules and regulations of all inspectors, governmental departments and agencies having jurisdiction over the Demised Premises to ensure a good state of repair of the Demised Premises and all furnishings, including any special equipment brought, placed, or installed upon the Demised Premises by TENANT; nor will the TENANT suffer or permit any strip, waste, or neglect of any building or such personal property to be committed; and the TENANT will repair, replace, and renovate the said real and personal property as often as it may be necessary in order to keep the building or buildings and the personal property which is subject to the LANDLORD'S lien, in good repair and condition. In the event that improvements or repairs are contemplated prior to or at the beginning of or during TENANT'S occupancy, then this provision shall apply to the condition of the property as of the last repair, improvement or renovation.

In the event that LANDLORD shall deem it necessary or be required by any governmental authority to repair, alter, remove, reconstruct or improve any part of the Demised Premises or of the property (unless the same result from TENANT'S act, neglect, default or mode of operation, in which event LANDLORD shall make all such repairs, alterations or improvements at TENANT'S sole cost and expense), then the same shall be made by LANDLORD with reasonable dispatch, and should the making of such repairs, alterations and improvements cause any interference with TENANT'S use of the Demised Premises, such interference shall not relieve TENANT from the performance of its obligations hereunder nor shall such interference be deemed an actual or constructive eviction or partial eviction or result in abatement of rental.

## 15. ALTERATIONS

TENANT shall not make any alterations, additions or improvements to the Demised Premises (whether or not the same may be structural in nature) without LANDLORD'S prior written consent. All alterations, additions, or improvements made to the Demised Premises, except movable furniture and equipment installed at TENANT'S expense, shall be the property of the LANDLORD and remain upon and be surrendered with the Demised Premises at the expiration of the term of this Lease; provided, however, that LANDLORD may require TENANT to remove any additions made at TENANT'S request to the Demised Premises and to repair any damage caused by such removal, and provide further, that if TENANT has not removed its property and equipment within ten (10) days after the expiration or termination of this Lease, LANDLORD may elect to retain the same as abandoned property.

In the event TENANT shall request LANDLORD'S permission, and LANDLORD shall permit TENANT to perform any alterations, additions, improvements or repairs to the Demised Premises, TENANT shall (i) submit its plans and specifications to LANDLORD for its approval prior to the commencement of any construction, (ii) obtain all necessary permits prior to the commencement of any construction, (iii) only use contractors approved by LANDLORD, (iv) not permit any construction liens to be placed or remain on the Demised Premises. In the event a construction lien shall be filed against the Demised Premises as a result of work undertaken by TENANT, TENANT shall within ten (10) days of receiving notice of such lien, discharge the lien of record either by payment of the indebtedness to the lien claimant or by filing a bond as security therefore. All such work made by or on behalf of TENANT shall be performed in such manner as LANDLORD may designate and in accordance with all applicable laws and regulations of governmental authorities having jurisdiction over the same. All such work by TENANT or its contractors shall not interfere with, impede or delay any work by LANDLORD or its contractors, tenants or TENANT'S contractors. All contractors engaged by TENANT shall be licensed contractors, possessing good labor relations, and capable of performing quality workmanship.

## 16. EQUIPMENT, FIXTURES AND SIGNS

(a) All furnishings, fixtures, trade fixtures, equipment, and signs used on the Demised Premises by TENANT but provided by LANDLORD, will, at all times, be, and remain, the property of LANDLORD. Provided that this Lease is in good standing and subject to the LANDLORD'S lien for rent, TENANT will have the right to remove any furniture or fixtures provided by TENANT, or any part thereof, from the Demised Premises during the term of this Lease, at the expiration thereof, or within a reasonable time thereafter, provided, however, that TENANT, in so doing, does not cause any irreparable damage to the Demised Premises, and provided further, that TENANT will pay or reimburse LANDLORD for the reasonable expense of repairing damage caused by such removal.

(b) All TENANT signs shall be approved by the LANDLORD and must meet all applicable

codes. The exact location, style, text, and color(s) of the sign shall be agreed upon by the LANDLORD, in writing, prior to TENANT'S installation. LANDLORD'S approval shall not be unreasonably withheld or delayed.

#### **17. ADDITIONAL COVENANTS OF THE TENANT**

(a) The TENANT shall pay for all utilities associated with the use of the Demised Premises including, but not limited to, water, electricity, sewer, gas and waste, (if applicable). In the event that a separate bill for the Demised Premises is not available for one or more of the utility services required by the Demised Premises, then the TENANT shall pay a pro-rated share of that particular utility bill based on a calculation of the ratio of the square footage of the Demised Premises and the total square footage of the area covered by that particular utility expense. In the event that the TENANT shall be billed for a pro-rated share, the LANDLORD shall provide TENANT a utility bill each month and TENANT shall pay the amount due to LANDLORD within ten (10) days of its receipt.

(b) The TENANT covenants and agrees with the LANDLORD that no damage or destruction to any building or improvement by fire, windstorm, or any other casualty shall be deemed to entitle the TENANT to surrender possession of the Demised Premises or to terminate this Lease or to violate any of its provisions or to cause any abatement or rebate in the rent then due or thereafter becoming due under the terms hereof, unless otherwise specifically provided for herein. If the Lease be canceled for the TENANT'S default at any time while there remains outstanding any obligation from any insurance company to pay for the damage or any part thereof, then the claim against the insurance company shall, upon the cancellation of the within-Lease, be deemed immediately to become absolute and unconditional property of the LANDLORD. In the event of destruction to the Demised Premises by casualty or hazard, LANDLORD will have the option of canceling the Lease, or repairing the building, and in the event that the LANDLORD elects to repair the building, an appropriate abatement of rent will occur.

(c) The TENANT shall be responsible for the HVAC and all air conditioning systems together with the plumbing and electrical system.

(d) The TENANT shall be responsible for maintaining the roof and exterior of the building

(e) The TENANT covenants and agrees with the LANDLORD that nothing in this Lease contained shall ever be construed as empowering the TENANT to encumber or cause the LANDLORD to encumber the title or interest of the LANDLORD.

(f) The TENANT covenants and agrees with the LANDLORD that, at the termination of this Lease, the TENANT will peaceably and quietly deliver unto the LANDLORD, possession of the Demised Premises and all buildings and improvements located thereon, as well as the TENANT'S interest in all fixtures and equipment appertaining thereto.

(g) The TENANT agrees not to make any internal changes or exterior changes or alterations without written approval of the LANDLORD. This provision does not apply to TENANT'S trade fixtures and/or other non-permanent fixtures on the interior of the Demised Premises.

(h) TENANT agrees to maintain the exterior landscaping including any new landscaping installed with LANDLORD'S approval, in areas adjacent to the Demised Premises or in an effort to enhance the adjacent beach area, at TENANT'S sole cost and expense. LANDLORD agrees to trim the trees located on the public beach and remove coconuts on an annual basis.

**18. LANDLORD'S RIGHT OF ENTRY** - The LANDLORD or its agents shall have the right to enter upon the Demised Premises at all reasonable times to examine the condition and use thereof, provided only that such right shall be exercised in such manner as not to interfere with the TENANT in the conduct of the TENANT'S business on said Demised Premises. If the said Demised Premises are damaged by fire, windstorm, or by any other casualty which caused the Demised Premises to be exposed to the elements, then the LANDLORD may enter upon the Demised Premises to make emergency repairs. LANDLORD may enter upon the Demised Premises to make renovations and repairs of a non-emergency nature by giving reasonable notice to the TENANT, and in such a manner as to minimize any inconvenience to both parties.

**19. TENANT'S ACCEPTANCE** - The TENANT accepts the Demised Premises and improvements thereon in an as is condition and all improvements and additions shall be at the sole expense of the TENANT except as may be otherwise provided for in this Lease.

**20. MISCELLANEOUS PROVISIONS** - It is mutually covenanted and agreed by and between the parties as follows:

(a) That no waiver of a breach of any of the covenants in this Lease contained shall be construed to be a waiver of all succeeding breach of the same covenant.

(b) That time is of the essence in every particular and particularly where the obligation to pay money is involved.

(c) That all arrearages in the payment of rent or in the repayment to the LANDLORD of any sums which the LANDLORD may have paid in order to cure a default of the TENANT (as elsewhere herein provided for), shall bear interest from the date when due and payable at the highest rate permitted by law until paid.

(d) That no modification, release, discharge, or waiver of any provision hereof shall be of any force, effect, or value unless in writing and signed by the persons who are then LANDLORD and TENANT.

(e) That all covenants, promises, conditions, and obligations contained herein or implied by law, or covenants running with the land, shall attach to and be binding upon the heirs, executors, administrators, successors, legal representatives, and assigns of each of the parties to this Lease.

(f) That this instrument contains the entire agreement between the parties as of this date, and that the execution hereof has not been induced by either of the parties by representations, promises or understandings not expressed herein, and that there are not collateral agreements, stipulations, promises, or understandings whatsoever between the respective parties in any way touching the subject matter of this instrument which are not expressly contained in this instrument.

(g) That when either of the parties desire to give notice to the other or others in connection with and according to the terms of this Lease, such notice shall be deemed given when it shall have been deposited in the U.S. Registered or Certified mail with sufficient postage pre-paid thereon to carry it to its addressed destination. Said notice shall be addressed as follows:

AS TO LANDLORD: PROPERTY MANAGEMENT  
CITY OF KEY WEST  
525 ANGELA STREET

KEY WEST, FL 33040

AS TO TENANT: MATTHEW BABICH  
SMB RESTAURANT, LLC  
1319 DUVAL STREET  
KEY WEST, FL 33040

WITH A COPY TO: STUART KAUFMAN  
THE RANKAUF COMPANY  
121 WEST LONG LAKE ROAD, 3<sup>RD</sup> FLOOR  
BLOOMFIELD HILLS, MI 48304

When the parties on either side (LANDLORD or TENANT) consists of more than one person, notice or default by one of the persons on that side shall constitute notice or default by all of the persons on that side.

(h) This Lease and the provisions thereof shall be governed by and construed and enforced in accordance with the laws of the State of Florida.

(i) If the TENANT or TENANTS are signing in a capacity other than as individuals, then the LANDLORD may require personal guarantees from individuals as the LANDLORD deems necessary.

(j) LANDLORD may delegate its decision-making authority regarding any provision of this Lease to an Advisory Board.

IN WITNESS WHEREOF, the parties hereto have caused the foregoing Lease to be executed on the day and year first above written.



*Cheryl Smith*  
Cheryl Smith, City Clerk

Date: 6-2-09

LANDLORD: CITY OF KEY WEST

*Morgan Matherson*  
Morgan Matherson, Mayor

Date: 6-2-09

*[Signature]*  
WITNESS

Date: 5-14-09

*Himelby Rosen*  
WITNESS

Date: 5-14-09

TENANT: SMB RESTAURANT LLC

*[Signature]*  
Stuart M. Kaufman, Manager Member

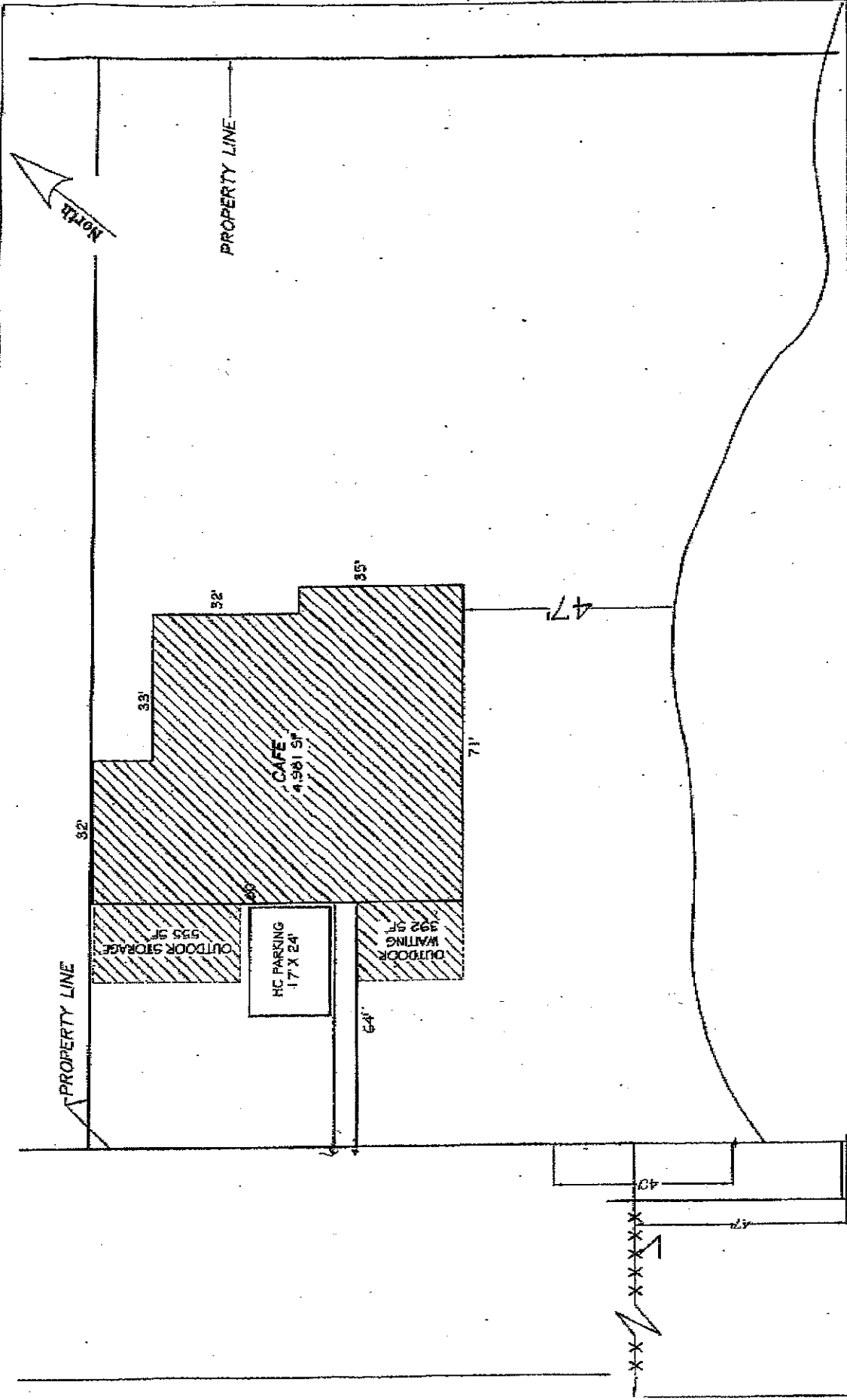
Date: 5-14-09

*[Signature]*  
Dale G. Rands, Manager Member

Date: 5-14-09



**EXHIBIT "A" Demised Premises, Site Plan**



**Southernmost Beach Cafe**  
 1405 Duval Street

**City of Key West**  
 601 Stockton Street  
 Key West, Florida 33540  
 (305) 235-3100

NMO	NTS
EXHIBIT 'A'	
1 OF 1	

**EXHIBIT "B" Rent Schedule**

*2-2*

**EXHIBIT "B"**

Tenant: SMB Restaurant LLC

Location: 1405 Duval

Contact: Matthew Babich

Building Square Feet 4981

Term 10 years effective 5/1/09

YEAR #	Period Beginning	Base Rent per sq. ft.	5% Increase	Base Rent		Sales Tax	Total Rent with Tax	TOTAL RENT	Percentage Rent Base Amount
				Annual	Monthly				
1	May 1, 2009	\$30.11	\$30.11	\$180,000.00	\$12,600.00	\$937.50	\$13,437.50	\$161,250.00	\$2,307,692.31
2	May 1, 2010	\$31.62	\$31.62	\$167,500.00	\$13,725.00	\$894.38	\$14,109.38	\$169,312.50	\$2,423,076.82
3	May 1, 2011	\$33.20	\$33.20	\$155,975.00	\$13,751.25	\$1,033.69	\$14,814.94	\$177,778.13	\$2,644,230.77
4	May 1, 2012	\$34.86	\$34.86	\$173,643.75	\$14,470.31	\$1,089.27	\$15,559.58	\$186,567.03	\$2,671,442.37
5	May 1, 2013	\$36.60	\$36.60	\$182,325.94	\$15,183.83	\$1,139.54	\$16,333.37	\$196,000.38	\$2,806,014.42
6	May 1, 2014	\$38.43	\$38.43	\$191,442.23	\$15,923.52	\$1,195.51	\$17,150.03	\$205,800.40	\$2,945,265.74
7	May 1, 2015	\$40.36	\$40.36	\$201,014.35	\$16,751.20	\$1,256.34	\$18,007.54	\$216,090.42	\$3,092,526.40
8	May 1, 2016	\$42.37	\$42.37	\$211,065.08	\$17,588.76	\$1,319.16	\$18,907.91	\$226,994.94	\$3,247,154.82
9	May 1, 2017	\$44.49	\$44.49	\$221,678.32	\$18,468.19	\$1,385.11	\$19,853.31	\$238,239.69	\$3,409,512.65
10	May 1, 2018	\$46.72	\$46.72	\$232,699.23	\$19,381.80	\$1,464.37	\$20,846.17	\$250,161.67	\$3,579,988.19

**EXHIBIT "C" Rules and Regulations**

1. Except as permitted hereunder, TENANT shall not use any area outside of the Demised Premises as shown on Exhibit A or any portion of any public area or any parking areas for or any other purpose whatsoever including but not limited to the storage of goods, inventory, equipment, materials, whether or not said area is inside a building or outdoors.

**EXHIBIT "D"**

TENANT'S written notice of acceptance of the Demised Premises and setting forth the commencement and expiration dates of the lease.

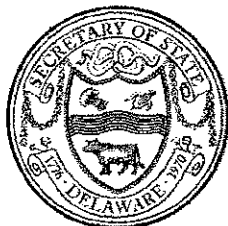
PK

# Delaware

PAGE 1

*The First State*


I, JEFFREY W. BULLOCK, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF FORMATION OF "SUNSET CITY, LLC", FILED IN THIS OFFICE ON THE TWELFTH DAY OF AUGUST, A.D. 2013, AT 10:56 O'CLOCK A.M.



5381666 8100

130977514

You may verify this certificate online  
at [corp.delaware.gov/authver.shtml](http://corp.delaware.gov/authver.shtml)

  
Jeffrey W. Bullock, Secretary of State  
AUTHENTICATION: 0656880

DATE: 08-12-13

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X-A.F. Q  
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**CERTIFICATE OF FORMATION**

**OF**

**Sunset City, LLC**

1. The name of the limited liability company is Sunset City, LLC

2. The address of its registered office in the State of Delaware is 2711 Centerville Road, Suite 400, City of Wilmington 19808, County of New Castle; and the name of the registered agent of the corporation in the State of Delaware at such address is Corporation Service Company.

IN WITNESS WHEREOF, the undersigned have executed this Certificate of Formation of Sunset City, LLC this 12<sup>th</sup> day of August, 2013.

By: /s/ Elizabeth Machaj  
Name: Elizabeth Machaj  
Title: Organizer



**LIMITED LIABILITY COMPANY  
OPERATING AGREEMENT  
OF  
SUNSET CITY, LLC**

THIS LIMITED LIABILITY COMPANY OPERATING AGREEMENT is made and entered into as of the 12th day of August, 2013, by LaSalle Hotel Operating Partnership, L.P., a Delaware Limited Partnership, together with those Persons set forth on Exhibit A hereto and any other Persons who, after the date of this Agreement, become members in the Company (collectively, the "Members").

WHEREAS, Sunset City, LLC (the "Company") was formed as a limited liability company by the filing of its Articles of Organization with the Secretary of the State of the State of Delaware on the 12th day of August, 2013; and

WHEREAS, the Members desire to set forth their respective rights and obligations in this Limited Liability Company Operating Agreement for the Company.

NOW THEREFORE, the parties agree as follows:

**ARTICLE 1**

**DEFINITIONS**

The following terms used in this Agreement shall have the following meanings:

- 1.1 "Act" shall mean the Delaware Limited Liability Company Act, as amended from time to time.
- 1.2 "Affiliate" shall mean, with respect to any Person, (i) any Person directly or indirectly controlling, controlled by or under common control with such Person, (ii) any Person owning or controlling 10% or more of the outstanding voting interests of such Person, (iii) any officer, director, or general partner of such Person, or (iv) any Person who is an officer, director, general partner, trustee, or holder of 10% or more of the voting interests of any Person described in clauses (i) through (iii) of this sentence.
- 1.3 "Agreement" shall mean this Limited Liability Company Operating Agreement as originally executed and as amended from time to time.
- 1.4 "Articles of Organization" shall mean the Articles of Organization of Sunset City, LLC, as filed with the Secretary of State of the State of Delaware on the 12th day of August, 2013, and as amended from time to time.

- 1.5 "Capital Account" shall mean, with respect to any Member, the aggregate amount of Capital Contributions made by such Member to the Company, (i) reduced by (A) any Losses allocated to such Member under Article 6, and (B) any distributions to such Member under Article 5; and (ii) increased by any Profits allocated to such Member under Article 6; and (iii) further adjusted as appropriate for other items, including items of tax-exempt income and nondeductible expenditures of the Company. The Capital Accounts of the Members shall be established and maintained in accordance with Treas. Reg. § 1.704-1(b)(2)(iv), or any similar successor provision. The Capital Account of any Member shall reflect all prior adjustments to the Capital Account of any prior holder of such Member's Interest in the Company, or portion thereof.
- 1.6 "Capital Contribution" shall mean any contribution to the capital of the Company in cash or property by a Member whenever made. "Initial Capital Contribution" shall mean the initial contribution to the capital of the Company pursuant to Section 4.1 of this Agreement.
- 1.7 "Code" shall mean the Internal Revenue Code of 1986, as amended, or corresponding provisions of subsequent superseding federal revenue laws.
- 1.8 "Company" shall mean Sunset City, LLC, a Delaware limited liability company.
- 1.9 "Distributable Cash" shall mean, with respect to any period, all cash revenues and funds received by the Company in such period, other than funds received as Capital Contributions, less the sum of the following (to the extent not made from funds received as Capital Contributions): (i) all sums paid to lenders in such period, including any Member or any Affiliate of a Member in its capacity as a lender; (ii) all cash expenditures, including capital expenditures, made in such period incident to the normal operation of the Company's business, including any fees, reimbursements and other amounts payable to any Member or its Affiliates as provided herein; and (iii) such reserves, whether for possible future capital expenditures, working capital, contingent liabilities or obligations of the Company, or otherwise, as the Managing Member believe are necessary or desirable for the operation of the Company's business.
- 1.10 "Economic Interest" shall mean a Member's share of the Company's Distributable Cash and Profits or Losses, but shall not include any right to participate in the management or affairs of the Company, or any right to vote on, consent to or otherwise participate in any decision of the Managing Member.
- 1.11 "Entity" shall mean any general partnership, limited partnership, limited liability company, corporation, joint venture, trust, business trust, cooperative association, foreign trust or foreign business organization.
- 1.12 "Majority Approval" shall mean the approval of Members holding at least fifty-one percent (51%) of the Percentage Interest in the Company.

- 1.13 "Managing Member" shall mean LaSalle Hotel Operating Partnership, L.P. and its successors and assigns.
- 1.14 "Members" shall mean each of the parties who execute a counterpart of this Agreement and each of the parties who may hereafter become Members pursuant to this Agreement.
- 1.15 "Membership Interest" shall mean a Member's entire interest in the Company including such Member's Economic Interest and the right to participate in the management of the business and affairs of the Company, including the right to vote on, consent to or otherwise participate in any decision or action of the Members granted pursuant to this Agreement or the Act.
- 1.16 "Percentage Interest" shall mean with respect to any Member the percentage which the number of such Member's Units bears to the number of all outstanding Units. Each Member's Percentage Interest is set forth on Exhibit A hereto, as the same may be amended from time to time.
- 1.17 "Persons" shall mean any individual or Entity, and the heirs, executors, administrators, legal representatives, successors, and assigns of such Person where the context so indicates.
- 1.18 "Profits" or "Losses" shall mean the profits or losses of the Company as determined for Federal income tax purposes, including each item of Company income, loss, gain or deduction (including nonrecourse deductions, as that term is used in Treas. Reg. § 1.704-2(b)(1)).
- 1.19 "Property" shall mean all property owned by the Company.
- 1.20 "Units" shall mean ownership units in the Company.

## ARTICLE 2

### FORMATION, NAME, PURPOSE, OFFICE AND TERM

- 2.1 Formation. The Company has been organized as a Delaware Limited Liability Company by executing and delivering Articles of Organization to the Delaware Secretary of State in accordance with and pursuant to the Act, and the Members hereby acknowledge and ratify the formation of the Company. Except as otherwise provided herein, the rights and liabilities of the Members shall be as provided in the Act.
- 2.2 Name. The name of the Company is "Sunset City, LLC".
- 2.3 Purpose. The purpose of the Company is to carry on any business permitted by the Act.
- 2.4 Principal Office and Registered Office. The principal office of the Company in the State of Delaware shall be located at the offices of its registered agent, Corporation Service Company, 2711 Centerville Road, Suite 400, City of Wilmington 19808, County of New Castle. The principal business office of the Company shall be 3 Bethesda Metro Center, Bethesda, MD

20814. The Company may have such other offices as the Managing Member may designate or as the business of the Company may from time to time require. The registered office and the registered agent may be changed from time to time by filing the prescribed form with the Delaware Secretary of State by the Managing Member.

- 2.5 Term. The term of the Company has commenced upon the filing of the Articles of Organization with the Secretary of State, and shall continue until December 31, 2113, unless the Company is earlier dissolved in accordance with either the provisions of this Agreement or the Act.

### ARTICLE 3

#### CLASS OF MEMBERS AND UNITS

- 3.1 Classes of Members. The Company shall have one class of Members. The addresses and Percentage Interests of the Members are listed on Exhibit A attached hereto, which may be amended from time to time by the Company as Members are added or deleted.
- 3.2 Classes and Ownership of Units. The Company shall have one class of ownership Units. The Members by Majority Approval may from time to time create additional classes of Units.
- 3.3 Obligations of Members. Except as expressly stated in this Agreement, no Member will be personally liable for any debts or losses of the Company beyond its respective Initial Capital Contribution.

### ARTICLE 4

#### CAPITAL CONTRIBUTIONS

- 4.1 Initial Capital Contributions. LaSalle Hotel Operating Partnership, L.P. shall make an initial capital contribution to the Company in the amount of \$1000.00 and shall receive 100 Units in exchange therefore.
- 4.2 Additional Capital Contributions. Members may make additional contributions to the capital of the Company with the unanimous consent of all of the members, but no Member shall be required to make any contribution to the capital of the Company other than the amounts required by Section 4.1 and shown on Exhibit A as its Initial Capital Contribution.
- 4.3 Loans. No Member shall have any obligation whatsoever to make loans to the Company. Loans may be made by a Member to the Company only upon the Majority Approval of the Members. Loans by Members to the Company shall not constitute a contribution to the capital of the Company or be credited to the Capital Account of the lending Member or entitle the lending Member to any increase in such Member's share of Company gains, profits or distributions or subject such Member to any greater proportion of the losses which the Company may sustain. Any loans made by any Member to the Company shall be on terms at

least as favorable to the Company as terms which would be demanded by an unrelated lender.

- 4.4 No Right to Interest, Etcetera. Except as expressly provided herein, no Member shall have any right to demand or receive the return of its Capital Contribution to the Company or a redemption of its Units. No Member shall be entitled to interest with respect to any Capital Contribution or on such Member's Capital Account, notwithstanding any disproportion in such Capital Accounts among the Members. Except as otherwise provided herein, each Member shall look solely to the assets of the Company for all distributions with respect to the Company and such Member's Capital Contribution thereto and share of Profits or Losses thereof, and shall have no recourse therefor (upon dissolution or otherwise) against any other Member. No Member shall have any right to demand or receive property other than cash at any time, including upon dissolution and termination of the Company.

## ARTICLE 5

### DISTRIBUTIONS

- 5.1 Distributions of Distributable Cash. Except as provided in Section 5.2, the Distributable Cash of the Company shall be distributed to the Members in proportion to their Percentage Interests, at the times and in the amounts determined by the Managing Member in its sole discretion.
- 5.2 Distributions Upon Liquidation of the Company. Notwithstanding anything to the contrary in this Agreement, in the year of liquidation of the Company, the final liquidating distributions of the Company shall be made in accordance with the positive Capital Account balances of the Members, after all other adjustments, including final allocations of Profits or Losses pursuant to Section 6.3 hereof and all distributions are reflected in such Capital Accounts.

## ARTICLE 6

### TAX MATTERS

- 6.1 Taxation as a Partnership. It is the intention of the Members that the Company shall be classified as a partnership for Federal income tax purposes, and if for any reason at any time it appears that the Company may be classified as an association taxable as a corporation (or otherwise be subjected to an entity-level Federal income tax), then this Agreement shall be amended to carry out the intent of the Members that the Company be taxed as a partnership.
- 6.2 Allocation of Profits or Losses for Taxable Years Other than the Taxable Year of Liquidation. Except as provided in Sections 6.3 through 6.5 hereof, the Profits or Losses for each taxable year of the Company shall be allocated to the Members in proportion to their Percentage Interests.

- 6.3 Allocations of Profits or Losses in the Taxable Year of Liquidation. The Profits or Losses of the Company for the taxable year of liquidation of the Company shall be allocated immediately prior to the final liquidating distributions of the Company and shall be allocated so that the Capital Accounts of the Members will, to the extent possible, be in proportion to the Percentage Interests of the Members.
- 6.4 Qualified Income Offset. Any Member who unexpectedly receives an adjustment, allocation, or distribution described in Treas. Reg. § 1.704-1(b)(2)(ii)(d)(4), (5), or (6) shall be allocated items of income and gain (consisting of a pro rata portion of each item of Company income, including gross income and gain for such year) in an amount and manner sufficient to eliminate such deficit balance as quickly as possible; provided, however, that this qualified income offset provision is intended to comply with the foregoing Treasury Regulation and shall be interpreted consistently therewith.
- 6.5 Allocation of Nonrecourse Deductions and Minimum Gain Chargeback. Notwithstanding the other provisions of this Article 6, Member nonrecourse deductions, as defined in Treas. Reg. § 1.704-2(b)(1), shall be allocated to the Members in proportion to their percentage Interests, consistent with the allocation of Losses under Section 6.2. If there is a net decrease in partnership minimum gain (as defined in Treas. Reg. § 1.704-2(b)(2)) of the Company during any fiscal year, each Member shall be allocated items of income and gain for such year (and if necessary, subsequent years) equal to the Member's share of the net decrease in partnership minimum gain during such year as provided by Treas. Reg. § 1.704-2(f)(1) and -2(g)(2). This Section 6.6 is intended to comply with the minimum gain chargeback requirement in such Treasury Regulations and shall be interpreted consistently therewith
- 6.6 Tax Matters Member. The Managing Member shall be the "tax matters partner" pursuant to Section 6231 of the Code. In the event of an audit of the Company's federal income tax return, the tax matters partner shall promptly advise the other Members of the audit and provide them with a copy of any final administrative adjustment resulting from such audit.
- 6.7 Tax Elections. The Managing Member may make any and all elections for federal, state and local tax purposes, including, without limitation, any election if permitted by applicable law to adjust the basis of property of the Company pursuant to Sections 754, 734(b) and 743(b) of the Code, or comparable provisions of state or local law in connection with transfers of Membership Interests and distributions of assets of the Company.

## ARTICLE 7

### MANAGEMENT

- 7.1 Managing Member. The Company shall be managed by the Managing Member. The Managing Member shall be responsible for the operations of the Company and shall have the right to make all decisions on behalf of the Company. No third party dealing with the Company in any matter shall be obligated to inquire into the propriety of the exercise of any power or authority by the Managing Member or any Person to whom the Managing Member has delegated any of its power or authority (including any officer of the Managing Member),

and such third party shall be fully protected in accepting any written instrument executed by the Managing Member or Person stating that he or she has such power or authority. Except as otherwise set forth herein, no Member who is not a Managing Member shall have any right or power to take part in the management or control of the Company or its business and affairs or to act for or bind the Company in any way.

- 7.2 Rights and Powers of the Managing Member; By-laws and Officers. The exclusive right to manage the business of the Company shall be vested in the Managing Member, who shall have all of the rights and powers which may be possessed by managers under the Act. The Managing Member may adopt By-Laws for the management of the Company, provided that no provision of such By-Laws may conflict with this Agreement. The Managing Member may provide for the appointment of officers (including without limitation a president, treasurer, secretary, vice presidents and other officers) of the Company, with such powers as may be delegated to such officers, and for such compensation and upon such other terms (including indemnification) as determined by the Managing Member in its sole discretion.
- 7.3 Duties of Managing Member; Other Activities. The Managing Member shall devote to the Company such time as may be necessary for the proper performance of all duties hereunder, but the Managing Member shall not be required to manage the Company as its sole and exclusive function, and the Managing Member may have other business interests and may engage in other activities in addition to those relating to the Company. Neither the Company nor any Member shall have any right, by virtue of this Agreement, to share or participate in other investments or activities of the Managing Member or to the income or proceeds derived therefrom.
- 7.4 Transactions with Affiliates. Subject to the other provisions of this Article 7, any of the Members or their Affiliates may be employed by the Managing Member on behalf of the Company and may receive from the Company fair and reasonable compensation therefor, and neither the Company nor any of the Members shall have, as a consequence of this Agreement, any rights in or to any such income earned by such Members or Affiliates.
- 7.5 Indemnification of Members by the Company. The Company shall indemnify any Person who was or is a party defendant or is threatened to be made a party defendant to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative, or investigative (other than an action by or in the right of the Company) by reason of the fact that he or she is or was a Member of the Company, or is or was serving at the request of the Company, against expenses (including attorney's fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if the Members determine by Majority Approval (without taking into account the vote of any Members seeking indemnification under this Section 7.6) that he or she acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Company, and with respect to any criminal action or proceeding, has no reasonable cause to believe its conduct was unlawful. The termination of any action, suit, or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not in itself create a presumption that the Person is not entitled to indemnification under the foregoing standard.

- 7.6 Exculpation. No Member shall be liable to the Company or the other Members (a) for mistakes of judgment, or for other acts or omissions not amounting to willful misconduct or gross negligence, or for losses or liabilities due to such mistakes or other acts or omissions, so long as he or she acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Company, or (b) due to the negligence, dishonesty or bad faith of any agent, employee or independent contractor retained or engaged to provide services, provided that reasonable care was exercised in selecting, employing or appointing such Person.

## ARTICLE 8

### ACTIONS OF THE MEMBERS

- 8.1 Informal Action of Members. Unless otherwise provided by the Act, any action required to be taken by the Members may be taken without a meeting if a consent thereto in writing, setting forth the action so taken, shall be signed by the number of Members necessary to take such action; and provided further that, any such consent may be signed in counterparts.
- 8.2 Meetings. The Managing Member may provide reasonable written rules for the conduct of meetings. The Managing Member may call meetings from time to time when necessary or desirable to conduct the business of the Company.

## ARTICLE 9

### TRANSFER OF MEMBERSHIP INTERESTS

- 9.1 Restrictions on Transferability. Except as otherwise provided in this Article 9, no Member may, directly or indirectly, sell, exchange, assign, pledge, grant a security interest, lien or other encumbrance in or against, or otherwise transfer or dispose of all or any portion of its Membership Interest without the prior written consent of the Managing Member, and any attempted or purported transfer without such consent shall be void ab initio and of no effect and shall not terminate the continued membership of such Member or confer any right on the proposed transferee or assignee.
- 9.2 Termination of Membership. Upon the death of a Member or the happening of any other event that terminates the continued membership of a Member for any reason, if the Company is not dissolved and continues pursuant to the Act and this Agreement, the Members shall be deemed to have consented to the transfer to the heirs, beneficiaries, personal representatives or other Person succeeding to the ownership of such Member's Membership Interest; however, in the event that the Membership Interest is transferred as described in this Section 9.2, the transferee shall succeed only to the departing Member's Economic Interest, and in no event will the transferee become a Member except as provided in Section 9.3.
- 9.3 Transferee as a Member. No transferee of a Membership Interest or any portion thereof shall become a Member of the Company unless (a) such transfer is approved by the unanimous



consent of the Members or occurs in a transaction described in Section 9.2, and (b) in either case, until the transferee of the Membership Interest satisfies such additional requirements as the Members shall determine, including (i) the acceptance of, and Agreement to be bound by, all of the terms and provisions of this Agreement, in form and substance satisfactory to the Members, (ii) the payment of such amount as the Members determine to cover all expenses incurred by the Company in connection with such substitution as a Member, and (iii) such other conditions as the Members may require. From and after the date such transferee or assignee becomes a substituted Member (with either an Economic Interest or both an Economic Interest and a Membership Interest), he or she shall have all of the rights and powers, and be subject to all of the restrictions and liabilities, of his transferor or assignor to the extent of the Membership Interest so transferred, but such substitution shall not release such transferor or assignor from liability to the Company for any contributions he agreed to make.

- 9.4 Legends on Certificates of Units. In the event that certificates representing the Units are issued (which the Managing Member may direct in its discretion), each such certificate shall be endorsed with a legend in substantially the following form:

"The Units represented by this certificate have been acquired for investment and have not been registered under the Securities Act of 1993 or under any state securities acts. The Units may not be sold or transferred in the absence of such registration or exemption therefrom under said acts and the existence of any such exemption must be established to the satisfaction of counsel for the Company."

"The Units represented by this certificate are subject to, and are transferable only upon compliance with, the provisions of the Limited Liability Company Operating Agreement of Sunset City, LLC, dated as of the 12th of August, 2013."

## ARTICLE 10

### BOOKS AND RECORDS; ACCOUNTING MATTERS

- 10.1 Books of Account. The Managing Member shall maintain or cause to be maintained full and accurate books and records of the Company at the Company's principal place of business, showing all receipts and expenditures, assets and liabilities, profits and losses, and all other matters required by the Act. The books and records of the Company shall be open to the reasonable inspection and examination of each Member in person or by its duly authorized representative at any time during regular business hours for any purpose reasonably related to such Member's interest as a member.
- 10.2 Financial Records. All financial records shall be maintained and reported based on generally acceptable accounting practices and the accrual or cash basis method of accounting, as the Managing Member shall determine. Within a reasonable period after the close of each fiscal year, the Managing Member, at the Company's expense, will give a written report to each

Member indicating such Member's share of the Company's income which requirement may be satisfied by giving each Member a copy of any tax form which includes such information.

- 10.3 Fiscal Year. The fiscal year of the Company shall be the calendar year.
- 10.4 Bank Accounts. All funds of the Company shall be deposited from time to time to the credit of the Company in such banks, trust companies or other depositories as the Managing Member may select.
- 10.5 Accountants and Attorneys. The Managing Member may select and dismiss accountants, attorneys or other professionals to perform services for the Company.

## ARTICLE 11

### DISSOLUTION AND TERMINATION

- 11.1 Dissolution. The Company shall be dissolved and its affairs shall be wound up upon the happening of the first to occur of the following events:
- (a) The expiration of the term of the Company;
  - (b) The Majority Approval of the Members;
  - (c) The sale or other disposition of all, or substantially all, of the assets of the Company and the collection of all amounts derived from such sale or other disposition (including all amounts payable to the Company under any promissory notes or other evidence of indebtedness taken by the Company in connection with such sale or other disposition, unless the Managing Member elects to distribute such evidence of indebtedness in kind);
  - (d) The death, retirement, resignation, expulsion, bankruptcy, court declaration of incompetence with respect to, or dissolution of, a Member or the occurrence of any other event that terminates the continued membership of a Member in the Company, unless the business of the Company is continued by the Majority Approval of the remaining Members within ninety days after the event; or
  - (e) Any other event that, under the Act, would cause the dissolution of the Company or make it unlawful for the business of the Company to be continued.
- 11.2 Distribution of Assets Upon Dissolution. Upon the dissolution and winding up of the Company, the assets of the Company shall be liquidated in an orderly manner, with due regard for the effects of then current market conditions on the sale of the Property of the Company, and thereafter distributed as follows: (a) to creditors of the Company (including Members who are creditors, to the extent otherwise permitted by law), in satisfaction of liabilities of the Company; and (b) to the Members in accordance with Article 5 of this Agreement.

- 11.3 Articles of Dissolution. When all debts, liabilities and obligations of the Company have been paid and discharged or adequate provision has been made therefor and all of the remaining property and assets of the Company have been distributed to the Members, the Managing Member shall execute and file articles of dissolution pursuant to the Act.
- 11.4 Winding Up. Except as provided by law, upon dissolution, each Member shall look solely to the assets of the Company for the return of its Capital Contribution. If the assets remaining after the payment or discharge of the debts and liabilities of the Company are insufficient to return the Capital Contribution of each Member, such Member shall have no recourse against any other Member.

## ARTICLE 12

### MISCELLANEOUS PROVISIONS

- 12.1 Amendment. Any amendment of this Agreement shall require the Majority Approval of the Members; provided, however, that this Agreement may be amended only with the consent of the affected Member if the amendment would adversely change such Member's required Capital Contributions or Economic Interest in the Company.
- 12.2 Notices. Any notice, distribution, demand or other communication required or permitted to be given under this Agreement shall be deemed to have been given for all purposes on the earlier of (a) the date when received (whether received by mail, courier, facsimile or other means) or (b) the second business day following the date of mailing if sent by registered or certified mail, postage prepaid, addressed if to the Company at its principal office, and, if to a Member, at its address as it appears in the Company's records.
- 12.3 Waiver of Partition. Each Member irrevocably waives any right that he or she may have to maintain any action for partition with respect to the Property or any other asset of the Company.
- 12.4 Construction. As used in this Agreement, the singular shall include the plural, and the masculine shall include the feminine and neuter and vice versa, as the context requires.
- 12.5 Headings. The headings in this Agreement are inserted for convenience only and shall not in any way define or affect the meaning, construction or scope of any provision of this Agreement.
- 12.6 Binding Effect. Subject to the provisions of this Agreement restricting transfers of interests in the Company, this Agreement shall be binding upon, and shall inure to the benefit of, the parties and their respective heirs, personal representatives, successors and assigns.
- 12.7 No Waivers; Remedies Cumulative. Neither the waiver by any Member of a breach of or a default under any provision of this Agreement, nor the failure of any Member on one or more occasions to enforce any of the provisions of this Agreement or to exercise any right, remedy

or privilege hereunder, shall be construed as a waiver of any subsequent breach or default of a similar nature or as a waiver of any such provision, right, remedy or privilege. No failure or delay on the part of either Member or the Company in exercising any right, power or privilege under this Agreement and no course of dealing between the Members or between any Member and the Company shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided in this Agreement are cumulative and not exclusive of any other rights or remedies which a Member or the Company would otherwise have at law or in equity.

- 12.8 No Third Party Beneficiary. This Agreement is for the benefit of the Members and the Company, and no other Person shall have any rights, interest or claims under this Agreement or be entitled to any benefits under or on account of this Agreement as a third party beneficiary or otherwise.
- 12.9 Attorneys' Fees and Expenses of Litigation. If any Member shall bring suit to enforce or interpret this Agreement, the substantially prevailing party shall be entitled to a reasonable sum as attorneys' fees and all other reasonable costs and expenses in connection with such suit, which sum shall be included in the judgment or decree entered in such suit.
- 12.10 Governing Law and Partial Invalidity. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware. If any part of this Agreement shall be held invalid for any reason, the remainder of this Agreement shall continue in full force and effect.
- 12.11 Counterparts. This Agreement may be executed in several counterparts, each of which shall be deemed an original but all of which shall constitute one and the same instrument. In addition, this Agreement may contain more than one counterpart of the signature page, and this Agreement may be executed by the affixing of the signature of each of the Members to any of such counterpart signature pages; all of such counterpart signature pages shall be read as those one, and they shall have the same force and effect as though all of the signers had executed a single signature page.

#### CERTIFICATION

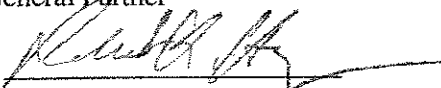
THE UNDERSIGNED, being the Members of Sunset City, LLC, a Delaware limited liability company, hereby evidences its adoption and ratification of the foregoing Limited Liability Company Operating Agreement of the Company.

EXECUTED by the Members as of the date of this Limited Liability Company Operating Agreement.

Managing Member:

LaSalle Hotel Operating Partnership, L.P.

By: LaSalle Hotel Properties,  
its General Partner

By: 

Name: Robert K. Hagan  
Title: Vice President and  
Assistant Secretary

**EXHIBIT A**

**Members, Capital Contributions, and Percentage Interests**

<u>Name and Address</u>	<u>Initial Capital Contribution</u>	<u>Units</u>	<u>Percentage Interest</u>
LaSalle Hotel Operating Partnership, L.P. 3 Bethesda Metro Center Bethesda, MD 20814	\$1000	100	100%
<hr/>			
TOTALS	\$1,000	100.00	100.00%

# Delaware

PAGE 1

*The First State*

I, JEFFREY W. BULLOCK, SECRETARY OF STATE OF THE STATE OF DELAWARE, DO HEREBY CERTIFY THE ATTACHED IS A TRUE AND CORRECT COPY OF THE CERTIFICATE OF FORMATION OF "SUNSET CITY LESSEE, LLC", FILED IN THIS OFFICE ON THE TWELFTH DAY OF AUGUST, A.D. 2013, AT 10:58 O'CLOCK A.M.



5381669 8100

130977524

You may verify this certificate online at [corp.delaware.gov/authver.shtml](http://corp.delaware.gov/authver.shtml)

  
Jeffrey W. Bullock, Secretary of State  
AUTHENTICATION: 0656889

DATE: 08-12-13

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X-A, E, R  
G-7

CERTIFICATE OF FORMATION

OF

**Sunset City Lessee, LLC**

1. The name of the limited liability company is Sunset City Lessee, LLC
2. The address of its registered office in the State of Delaware is 2711 Centerville Road, Suite 400, City of Wilmington 19808, County of New Castle; and the name of the registered agent of the corporation in the State of Delaware at such address is Corporation Service Company.

IN WITNESS WHEREOF, the undersigned have executed this Certificate of Formation of Sunset City Lessee, LLC this 12<sup>th</sup> day of August, 2013.

By: /s/ Elizabeth Machaj  
Name: Elizabeth Machaj  
Title: Organizer



**LIMITED LIABILITY COMPANY  
OPERATING AGREEMENT  
OF  
SUNSET CITY LESSEE, LLC**

THIS LIMITED LIABILITY COMPANY OPERATING AGREEMENT is made and entered into as of the 12th day of August, 2013, by LaSalle Hotel Lessee, Inc., an Illinois corporation, together with any other Persons who, after the date of this Agreement, become members in the Company (collectively, the "Members").

WHEREAS, Sunset City Lessee, LLC (the "Company") was formed as a limited liability company by the filing of its Articles of Organization with the Secretary of the State of the State of Delaware on the 12th day of August, 2013; and

WHEREAS, the Members desire to set forth their respective rights and obligations in this Limited Liability Company Operating Agreement for the Company.

NOW THEREFORE, the parties agree as follows:

**ARTICLE 1**

**DEFINITIONS**

The following terms used in this Agreement shall have the following meanings:

- 1.1 "Act" shall mean the Delaware Limited Liability Company Act, as amended from time to time.
- 1.2 "Affiliate" shall mean, with respect to any Person, (i) any Person directly or indirectly controlling, controlled by or under common control with such Person, (ii) any Person owning or controlling 10% or more of the outstanding voting interests of such Person, (iii) any officer, director, or general partner of such Person, or (iv) any Person who is an officer, director, general partner, trustee, or holder of 10% or more of the voting interests of any Person described in clauses (i) through (iii) of this sentence.
- 1.3 "Agreement" shall mean this Limited Liability Company Operating Agreement as originally executed and as amended from time to time.
- 1.4 "Articles of Organization" shall mean the Articles of Organization of Sunset City Lessee, LLC, as filed with the Secretary of State of the State of Delaware on the 12th day of August, 2013, and as amended from time to time.

- 1.5 "Capital Account" shall mean, with respect to any Member, the aggregate amount of Capital Contributions made by such Member to the Company, (i) reduced by (A) any Losses allocated to such Member under Article 6, and (B) any distributions to such Member under Article 5; and (ii) increased by any Profits allocated to such Member under Article 6; and (iii) further adjusted as appropriate for other items, including items of tax-exempt income and nondeductible expenditures of the Company. The Capital Accounts of the Members shall be established and maintained in accordance with Treas. Reg. § 1.704-1(b)(2)(iv), or any similar successor provision. The Capital Account of any Member shall reflect all prior adjustments to the Capital Account of any prior holder of such Member's Interest in the Company, or portion thereof.
- 1.6 "Capital Contribution" shall mean any contribution to the capital of the Company in cash or property by a Member whenever made. "Initial Capital Contribution" shall mean the initial contribution to the capital of the Company pursuant to Section 4.1 of this Agreement.
- 1.7 "Code" shall mean the Internal Revenue Code of 1986, as amended, or corresponding provisions of subsequent superseding federal revenue laws.
- 1.8 "Company" shall mean Sunset City Lessee, LLC, a Delaware limited liability company.
- 1.9 "Distributable Cash" shall mean, with respect to any period, all cash revenues and funds received by the Company in such period, other than funds received as Capital Contributions, less the sum of the following (to the extent not made from funds received as Capital Contributions): (i) all sums paid to lenders in such period, including any Member or any Affiliate of a Member in its capacity as a lender; (ii) all cash expenditures, including capital expenditures, made in such period incident to the normal operation of the Company's business, including any fees, reimbursements and other amounts payable to any Member or its Affiliates as provided herein; and (iii) such reserves, whether for possible future capital expenditures, working capital, contingent liabilities or obligations of the Company, or otherwise, as the Managing Member believe are necessary or desirable for the operation of the Company's business.
- 1.10 "Economic Interest" shall mean a Member's share of the Company's Distributable Cash and Profits or Losses, but shall not include any right to participate in the management or affairs of the Company, or any right to vote on, consent to or otherwise participate in any decision of the Managing Member.
- 1.11 "Entity" shall mean any general partnership, limited partnership, limited liability company, corporation, joint venture, trust, business trust, cooperative association, foreign trust or foreign business organization.
- 1.12 "Majority Approval" shall mean the approval of Members holding at least fifty-one percent (51%) of the Percentage Interest in the Company.
- 1.13 "Managing Member" shall mean LaSalle Hotel Lessee, Inc. and its successors and assigns.

- 1.14 "Members" shall mean each of the parties who execute a counterpart of this Agreement and each of the parties who may hereafter become Members pursuant to this Agreement.
- 1.15 "Membership Interest" shall mean a Member's entire interest in the Company including such Member's Economic Interest and the right to participate in the management of the business and affairs of the Company, including the right to vote on, consent to or otherwise participate in any decision or action of the Members granted pursuant to this Agreement or the Act.
- 1.16 "Percentage Interest" shall mean with respect to any Member the percentage which the number of such Member's Units bears to the number of all outstanding Units. Each Member's Percentage Interest is set forth on Exhibit A hereto, as the same may be amended from time to time.
- 1.17 "Persons" shall mean any individual or Entity, and the heirs, executors, administrators, legal representatives, successors, and assigns of such Person where the context so indicates.
- 1.18 "Profits" or "Losses" shall mean the profits or losses of the Company as determined for Federal income tax purposes, including each item of Company income, loss, gain or deduction (including nonrecourse deductions, as that term is used in Treas. Reg. § 1.704-2(b)(1)).
- 1.19 "Property" shall mean all property owned by the Company.
- 1.20 "Units" shall mean ownership units in the Company.

## ARTICLE 2

### FORMATION, NAME, PURPOSE, OFFICE AND TERM

- 2.1 Formation. The Company has been organized as a Delaware Limited Liability Company by executing and delivering Articles of Organization to the Delaware Secretary of State in accordance with and pursuant to the Act, and the Members hereby acknowledge and ratify the formation of the Company. Except as otherwise provided herein, the rights and liabilities of the Members shall be as provided in the Act.
- 2.2 Name. The name of the Company is "Sunset City Lessee, LLC".
- 2.3 Purpose. The purpose of the Company is to carry on any business permitted by the Act.
- 2.4 Principal Office and Registered Office. The principal office of the Company in the State of Delaware shall be located at the offices of its registered agent, Corporation Service Company, 2711 Centerville Road, Suite 400, City of Wilmington 19808, County of New Castle. The principal business office of the Company shall be 3 Bethesda Metro Center, Bethesda, MD 20814. The Company may have such other offices as the Managing Member may designate or as the business of the Company may from time to time require. The registered office and

the registered agent may be changed from time to time by filing the prescribed form with the Delaware Secretary of State by the Managing Member.

- 2.5 Term. The term of the Company has commenced upon the filing of the Articles of Organization with the Secretary of State, and shall continue until December 31, 2113, unless the Company is earlier dissolved in accordance with either the provisions of this Agreement or the Act.

### ARTICLE 3

#### CLASS OF MEMBERS AND UNITS

- 3.1 Classes of Members. The Company shall have one class of Members. The addresses and Percentage Interests of the Members are listed on Exhibit A attached hereto, which may be amended from time to time by the Company as Members are added or deleted.
- 3.2 Classes and Ownership of Units. The Company shall have one class of ownership Units. The Members by Majority Approval may from time to time create additional classes of Units.
- 3.3 Obligations of Members. Except as expressly stated in this Agreement, no Member will be personally liable for any debts or losses of the Company beyond its respective Initial Capital Contribution.

### ARTICLE 4

#### CAPITAL CONTRIBUTIONS

- 4.1 Initial Capital Contributions. LaSalle Hotel Lessee, Inc. shall make an initial capital contribution to the Company in the amount of \$1000.00 and shall receive 100 Units in exchange therefore.
- 4.2 Additional Capital Contributions. Members may make additional contributions to the capital of the Company with the unanimous consent of all of the members, but no Member shall be required to make any contribution to the capital of the Company other than the amounts required by Section 4.1 and shown on Exhibit A as its Initial Capital Contribution.
- 4.3 Loans. No Member shall have any obligation whatsoever to make loans to the Company. Loans may be made by a Member to the Company only upon the Majority Approval of the Members. Loans by Members to the Company shall not constitute a contribution to the capital of the Company or be credited to the Capital Account of the lending Member or entitle the lending Member to any increase in such Member's share of Company gains, profits or distributions or subject such Member to any greater proportion of the losses which the Company may sustain. Any loans made by any Member to the Company shall be on terms at least as favorable to the Company as terms which would be demanded by an unrelated lender.

- 4.4 No Right to Interest, Etcetera. Except as expressly provided herein, no Member shall have any right to demand or receive the return of its Capital Contribution to the Company or a redemption of its Units. No Member shall be entitled to interest with respect to any Capital Contribution or on such Member's Capital Account, notwithstanding any disproportion in such Capital Accounts among the Members. Except as otherwise provided herein, each Member shall look solely to the assets of the Company for all distributions with respect to the Company and such Member's Capital Contribution thereto and share of Profits or Losses thereof, and shall have no recourse therefor (upon dissolution or otherwise) against any other Member. No Member shall have any right to demand or receive property other than cash at any time, including upon dissolution and termination of the Company.

## ARTICLE 5

### DISTRIBUTIONS

- 5.1 Distributions of Distributable Cash. Except as provided in Section 5.2, the Distributable Cash of the Company shall be distributed to the Members in proportion to their Percentage Interests, at the times and in the amounts determined by the Managing Member in its sole discretion.
- 5.2 Distributions Upon Liquidation of the Company. Notwithstanding anything to the contrary in this Agreement, in the year of liquidation of the Company, the final liquidating distributions of the Company shall be made in accordance with the positive Capital Account balances of the Members, after all other adjustments, including final allocations of Profits or Losses pursuant to Section 6.3 hereof and all distributions are reflected in such Capital Accounts.

## ARTICLE 6

### TAX MATTERS

- 6.1 Taxation as a Partnership. It is the intention of the Members that the Company shall be classified as a partnership for Federal income tax purposes, and if for any reason at any time it appears that the Company may be classified as an association taxable as a corporation (or otherwise be subjected to an entity-level Federal income tax), then this Agreement shall be amended to carry out the intent of the Members that the Company be taxed as a partnership.
- 6.2 Allocation of Profits or Losses for Taxable Years Other than the Taxable Year of Liquidation. Except as provided in Sections 6.3 through 6.5 hereof, the Profits or Losses for each taxable year of the Company shall be allocated to the Members in proportion to their Percentage Interests.
- 6.3 Allocations of Profits or Losses in the Taxable Year of Liquidation. The Profits or Losses of the Company for the taxable year of liquidation of the Company shall be allocated immediately prior to the final liquidating distributions of the Company and shall be allocated

so that the Capital Accounts of the Members will, to the extent possible, be in proportion to the Percentage Interests of the Members.

- 6.4 Qualified Income Offset. Any Member who unexpectedly receives an adjustment, allocation, or distribution described in Treas. Reg. § 1.704-1(b)(2)(ii)(d)(4), (5), or (6) shall be allocated items of income and gain (consisting of a pro rata portion of each item of Company income, including gross income and gain for such year) in an amount and manner sufficient to eliminate such deficit balance as quickly as possible; provided, however, that this qualified income offset provision is intended to comply with the foregoing Treasury Regulation and shall be interpreted consistently therewith.
- 6.5 Allocation of Nonrecourse Deductions and Minimum Gain Chargeback. Notwithstanding the other provisions of this Article 6, Member nonrecourse deductions, as defined in Treas. Reg. § 1.704-2(b)(1), shall be allocated to the Members in proportion to their percentage Interests, consistent with the allocation of Losses under Section 6.2. If there is a net decrease in partnership minimum gain (as defined in Treas. Reg. § 1.704-2(b)(2)) of the Company during any fiscal year, each Member shall be allocated items of income and gain for such year (and if necessary, subsequent years) equal to the Member's share of the net decrease in partnership minimum gain during such year as provided by Treas. Reg. § 1.704-2(f)(1) and -2(g)(2). This Section 6.6 is intended to comply with the minimum gain chargeback requirement in such Treasury Regulations and shall be interpreted consistently therewith
- 6.6 Tax Matters Member. The Managing Member shall be the "tax matters partner" pursuant to Section 6231 of the Code. In the event of an audit of the Company's federal income tax return, the tax matters partner shall promptly advise the other Members of the audit and provide them with a copy of any final administrative adjustment resulting from such audit.
- 6.7 Tax Elections. The Managing Member may make any and all elections for federal, state and local tax purposes, including, without limitation, any election if permitted by applicable law to adjust the basis of property of the Company pursuant to Sections 754, 734(b) and 743(b) of the Code, or comparable provisions of state or local law in connection with transfers of Membership Interests and distributions of assets of the Company.

## ARTICLE 7

### MANAGEMENT

- 7.1 Managing Member. The Company shall be managed by the Managing Member. The Managing Member shall be responsible for the operations of the Company and shall have the right to make all decisions on behalf of the Company. No third party dealing with the Company in any matter shall be obligated to inquire into the propriety of the exercise of any power or authority by the Managing Member or any Person to whom the Managing Member has delegated any of its power or authority (including any officer of the Managing Member), and such third party shall be fully protected in accepting any written instrument executed by the Managing Member or Person stating that he or she has such power or authority. Except as otherwise set forth herein, no Member who is not a Managing Member shall have any

right or power to take part in the management or control of the Company or its business and affairs or to act for or bind the Company in any way.

- 7.2 Rights and Powers of the Managing Member; By-laws and Officers. The exclusive right to manage the business of the Company shall be vested in the Managing Member, who shall have all of the rights and powers which may be possessed by managers under the Act.- The Managing Member may adopt By-Laws for the management of the Company, provided that no provision of such By-Laws may conflict with this Agreement. The Managing Member may provide for the appointment of officers (including without limitation a president, treasurer, secretary, vice presidents and other officers) of the Company, with such powers as may be delegated to such officers, and for such compensation and upon such other terms (including indemnification) as determined by the Managing Member in its sole discretion.
- 7.3 Duties of Managing Member; Other Activities. The Managing Member shall devote to the Company such time as may be necessary for the proper performance of all duties hereunder, but the Managing Member shall not be required to manage the Company as its sole and exclusive function, and the Managing Member may have other business interests and may engage in other activities in addition to those relating to the Company. Neither the Company nor any Member shall have any right, by virtue of this Agreement, to share or participate in other investments or activities of the Managing Member or to the income or proceeds derived therefrom.
- 7.4 Transactions with Affiliates. Subject to the other provisions of this Article 7, any of the Members or their Affiliates may be employed by the Managing Member on behalf of the Company and may receive from the Company fair and reasonable compensation therefor, and neither the Company nor any of the Members shall have, as a consequence of this Agreement, any rights in or to any such income earned by such Members or Affiliates.
- 7.5 Indemnification of Members by the Company. The Company shall indemnify any Person who was or is a party defendant or is threatened to be made a party defendant to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative, or investigative (other than an action by or in the right of the Company) by reason of the fact that he or she is or was a Member of the Company, or is or was serving at the request of the Company, against expenses (including attorney's fees), judgments, fines and amounts paid in settlement actually and reasonably incurred by him in connection with such action, suit or proceeding if the Members determine by Majority Approval (without taking into account the vote of any Members seeking indemnification under this Section 7.6) that he or she acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the Company, and with respect to any criminal action or proceeding, has no reasonable cause to believe its conduct was unlawful. The termination of any action, suit, or proceeding by judgment, order, settlement, conviction, or upon a plea of nolo contendere or its equivalent, shall not in itself create a presumption that the Person is not entitled to indemnification under the foregoing standard.
- 7.6 Exculpation. No Member shall be liable to the Company or the other Members (a) for mistakes of judgment, or for other acts or omissions not amounting to willful misconduct or

gross negligence, or for losses or liabilities due to such mistakes or other acts or omissions, so long as he or she acted in good faith and in a manner he reasonably believed to be in, or not opposed to, the best interests of the Company, or (b) due to the negligence, dishonesty or bad faith of any agent, employee or independent contractor retained or engaged to provide services, provided that reasonable care was exercised in selecting, employing or appointing such Person.

## ARTICLE 8

### ACTIONS OF THE MEMBERS

- 8.1 Informal Action of Members. Unless otherwise provided by the Act, any action required to be taken by the Members may be taken without a meeting if a consent thereto in writing, setting forth the action so taken, shall be signed by the number of Members necessary to take such action; and provided further that, any such consent may be signed in counterparts.
- 8.2 Meetings. The Managing Member may provide reasonable written rules for the conduct of meetings. The Managing Member may call meetings from time to time when necessary or desirable to conduct the business of the Company.

## ARTICLE 9

### TRANSFER OF MEMBERSHIP INTERESTS

- 9.1 Restrictions on Transferability. Except as otherwise provided in this Article 9, no Member may, directly or indirectly, sell, exchange, assign, pledge, grant a security interest, lien or other encumbrance in or against, or otherwise transfer or dispose of all or any portion of its Membership Interest without the prior written consent of the Managing Member, and any attempted or purported transfer without such consent shall be void ab initio and of no effect and shall not terminate the continued membership of such Member or confer any right on the proposed transferee or assignee.
- 9.2 Termination of Membership. Upon the death of a Member or the happening of any other event that terminates the continued membership of a Member for any reason, if the Company is not dissolved and continues pursuant to the Act and this Agreement, the Members shall be deemed to have consented to the transfer to the heirs, beneficiaries, personal representatives or other Person succeeding to the ownership of such Member's Membership Interest; however, in the event that the Membership Interest is transferred as described in this Section 9.2, the transferee shall succeed only to the departing Member's Economic Interest, and in no event will the transferee become a Member except as provided in Section 9.3.
- 9.3 Transferee as a Member. No transferee of a Membership Interest or any portion thereof shall become a Member of the Company unless (a) such transfer is approved by the unanimous consent of the Members or occurs in a transaction described in Section 9.2, and (b) in either case, until the transferee of the Membership Interest satisfies such additional requirements as the Members shall determine, including (i) the acceptance of, and Agreement to be bound by,



all of the terms and provisions of this Agreement, in form and substance satisfactory to the Members, (ii) the payment of such amount as the Members determine to cover all expenses incurred by the Company in connection with such substitution as a Member, and (iii) such other conditions as the Members may require. From and after the date such transferee or assignee becomes a substituted Member (with either an Economic Interest or both an Economic Interest and a Membership Interest), he or she shall have all of the rights and powers, and be subject to all of the restrictions and liabilities, of his transferor or assignor to the extent of the Membership Interest so transferred, but such substitution shall not release such transferor or assignor from liability to the Company for any contributions he agreed to make.

- 9.4 Legends on Certificates of Units. In the event that certificates representing the Units are issued (which the Managing Member may direct in its discretion), each such certificate shall be endorsed with a legend in substantially the following form:

"The Units represented by this certificate have been acquired for investment and have not been registered under the Securities Act of 1993 or under any state securities acts. The Units may not be sold or transferred in the absence of such registration or exemption therefrom under said acts and the existence of any such exemption must be established to the satisfaction of counsel for the Company."

"The Units represented by this certificate are subject to, and are transferable only upon compliance with, the provisions of the Limited Liability Company Operating Agreement of Sunset City Lessee, LLC dated as of the 12th of August, 2013."

## ARTICLE 10

### BOOKS AND RECORDS; ACCOUNTING MATTERS

- 10.1 Books of Account. The Managing Member shall maintain or cause to be maintained full and accurate books and records of the Company at the Company's principal place of business, showing all receipts and expenditures, assets and liabilities, profits and losses, and all other matters required by the Act. The books and records of the Company shall be open to the reasonable inspection and examination of each Member in person or by its duly authorized representative at any time during regular business hours for any purpose reasonably related to such Member's interest as a member.
- 10.2 Financial Records. All financial records shall be maintained and reported based on generally acceptable accounting practices and the accrual or cash basis method of accounting, as the Managing Member shall determine. Within a reasonable period after the close of each fiscal year, the Managing Member, at the Company's expense, will give a written report to each Member indicating such Member's share of the Company's income which requirement may be satisfied by giving each Member a copy of any tax form which includes such information.

- 10.3 Fiscal Year. The fiscal year of the Company shall be the calendar year.
- 10.4 Bank Accounts. All funds of the Company shall be deposited from time to time to the credit of the Company in such banks, trust companies or other depositories as the Managing Member may select.
- 10.5 Accountants and Attorneys. The Managing Member may select and dismiss accountants, attorneys or other professionals to perform services for the Company.

## ARTICLE 11

### DISSOLUTION AND TERMINATION

- 11.1 Dissolution. The Company shall be dissolved and its affairs shall be wound up upon the happening of the first to occur of the following events:
- (a) The expiration of the term of the Company;
  - (b) The Majority Approval of the Members;
  - (c) The sale or other disposition of all, or substantially all, of the assets of the Company and the collection of all amounts derived from such sale or other disposition (including all amounts payable to the Company under any promissory notes or other evidence of indebtedness taken by the Company in connection with such sale or other disposition, unless the Managing Member elects to distribute such evidence of indebtedness in kind);
  - (d) The death, retirement, resignation, expulsion, bankruptcy, court declaration of incompetence with respect to, or dissolution of, a Member or the occurrence of any other event that terminates the continued membership of a Member in the Company, unless the business of the Company is continued by the Majority Approval of the remaining Members within ninety days after the event; or
  - (e) Any other event that, under the Act, would cause the dissolution of the Company or make it unlawful for the business of the Company to be continued.
- 11.2 Distribution of Assets Upon Dissolution. Upon the dissolution and winding up of the Company, the assets of the Company shall be liquidated in an orderly manner, with due regard for the effects of then current market conditions on the sale of the Property of the Company, and thereafter distributed as follows: (a) to creditors of the Company (including Members who are creditors, to the extent otherwise permitted by law), in satisfaction of liabilities of the Company; and (b) to the Members in accordance with Article 5 of this Agreement.
- 11.3 Articles of Dissolution. When all debts, liabilities and obligations of the Company have been paid and discharged or adequate provision has been made therefor and all of the remaining

property and assets of the Company have been distributed to the Members, the Managing Member shall execute and file articles of dissolution pursuant to the Act.

- 11.4 Winding Up. Except as provided by law, upon dissolution, each Member shall look solely to the assets of the Company for the return of its Capital Contribution. If the assets remaining after the payment or discharge of the debts and liabilities of the Company are insufficient to return the Capital Contribution of each Member, such Member shall have no recourse against any other Member.

## ARTICLE 12

### MISCELLANEOUS PROVISIONS

- 12.1 Amendment. Any amendment of this Agreement shall require the Majority Approval of the Members; provided, however, that this Agreement may be amended only with the consent of the affected Member if the amendment would adversely change such Member's required Capital Contributions or Economic Interest in the Company.
- 12.2 Notices. Any notice, distribution, demand or other communication required or permitted to be given under this Agreement shall be deemed to have been given for all purposes on the earlier of (a) the date when received (whether received by mail, courier, facsimile or other means) or (b) the second business day following the date of mailing if sent by registered or certified mail, postage prepaid, addressed if to the Company at its principal office, and, if to a Member, at its address as it appears in the Company's records.
- 12.3 Waiver of Partition. Each Member irrevocably waives any right that he or she may have to maintain any action for partition with respect to the Property or any other asset of the Company.
- 12.4 Construction. As used in this Agreement, the singular shall include the plural, and the masculine shall include the feminine and neuter and vice versa, as the context requires.
- 12.5 Headings. The headings in this Agreement are inserted for convenience only and shall not in any way define or affect the meaning, construction or scope of any provision of this Agreement.
- 12.6 Binding Effect. Subject to the provisions of this Agreement restricting transfers of interests in the Company, this Agreement shall be binding upon, and shall inure to the benefit of, the parties and their respective heirs, personal representatives, successors and assigns.
- 12.7 No Waivers; Remedies Cumulative. Neither the waiver by any Member of a breach of or a default under any provision of this Agreement, nor the failure of any Member on one or more occasions to enforce any of the provisions of this Agreement or to exercise any right, remedy or privilege hereunder, shall be construed as a waiver of any subsequent breach or default of a similar nature or as a waiver of any such provision, right, remedy or privilege. No failure or delay on the part of either Member or the Company in exercising any right, power or

privilege under this Agreement and no course of dealing between the Members or between any Member and the Company shall operate as a waiver thereof; nor shall any single or partial exercise of any right, power or privilege preclude any other or further exercise thereof or the exercise of any other right, power or privilege. The rights and remedies provided in this Agreement are cumulative and not exclusive of any other rights or remedies which a Member or the Company would otherwise have at law or in equity.

- 12.8 No Third Party Beneficiary. This Agreement is for the benefit of the Members and the Company, and no other Person shall have any rights, interest or claims under this Agreement or be entitled to any benefits under or on account of this Agreement as a third party beneficiary or otherwise.
- 12.9 Attorneys' Fees and Expenses of Litigation. If any Member shall bring suit to enforce or interpret this Agreement, the substantially prevailing party shall be entitled to a reasonable sum as attorneys' fees and all other reasonable costs and expenses in connection with such suit, which sum shall be included in the judgment or decree entered in such suit.
- 12.10 Governing Law and Partial Invalidity. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware. If any part of this Agreement shall be held invalid for any reason, the remainder of this Agreement shall continue in full force and effect.
- 12.11 Counterparts. This Agreement may be executed in several counterparts, each of which shall be deemed an original but all of which shall constitute one and the same instrument. In addition, this Agreement may contain more than one counterpart of the signature page, and this Agreement may be executed by the affixing of the signature of each of the Members to any of such counterpart signature pages; all of such counterpart signature pages shall be read as those one, and they shall have the same force and effect as though all of the signers had executed a single signature page.

#### CERTIFICATION

THE UNDERSIGNED, being the Members of Sunset City Lessee, LLC, a Delaware limited liability company, hereby evidences its adoption and ratification of the foregoing Limited Liability Company Operating Agreement of the Company.

EXECUTED by the Members as of the date of this Limited Liability Company Operating Agreement.

Managing Member:

LaSalle Hotel Lessee, Inc.

By: 

Name: Robert K. Hagan

Title: Assistant Secretary

**EXHIBIT A**

**Members, Capital Contributions, and Percentage Interests**

<u>Name and Address</u>	<u>Initial Capital Contribution</u>	<u>Units</u>	<u>Percentage Interest</u>
LaSalle Hotel Lessee, Inc. 3 Bethesda Metro Center Bethesda, MD 20814	\$1,000	100.00	100%
<hr/>			
<b>TOTALS</b>	<b>\$1,000</b>	<b>100.00</b>	<b>100.00%</b>