

STRATEGIC HOTELS & RESORTS, INC

Form 10-K

February 23, 2012

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2011

or

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

For the transition period from to

Commission file number: 001-32223

STRATEGIC HOTELS & RESORTS, INC.

(Exact name of registrant as specified in its charter)

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Maryland
(State or other jurisdiction of

33-1082757
(I.R.S. Employer Identification No.)

incorporation or organization)
200 West Madison Street, Suite 1700, Chicago, Illinois
(Address of principal executive offices)

60606-3415
(Zip Code)

Registrant's telephone number, including area code: (312) 658-5000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of exchange on which registered
Common Stock (\$0.01 par value)	New York Stock Exchange
8.50% Series A Cumulative Preferred Stock (\$0.01 par value)	New York Stock Exchange
8.25% Series B Cumulative Preferred Stock (\$0.01 par value)	New York Stock Exchange
8.25% Series C Cumulative Preferred Stock (\$0.01 par value)	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer
 Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company
 Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

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The aggregate market value of the common stock of the registrant held by non-affiliates of the registrant was approximately \$1.14 billion as of June 30, 2011 (based on the closing sale price of the common stock on the New York Stock Exchange on such date).

The number of shares of common stock (\$0.01 par value per share) of the registrant outstanding as of February 22, 2012 was 185,627,199.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this annual report on Form 10-K incorporates information by reference from the registrant's definitive proxy statement to be filed with the Securities and Exchange Commission within 120 days after the close of the registrant's fiscal year.

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This report contains registered trademarks that are the exclusive property of their respective owners, which are companies other than us, including Fairmont®, Four Seasons®, Hilton®, Hyatt®, InterContinental®, Loews®, Marriott®, Renaissance®, Ritz-Carlton®, and Westin®. None of the owners of these trademarks, their affiliates or any of their respective officers, directors, agents or employees has or will have any liability or responsibility for any financial statements, projections, other financial information or other information contained in this report.

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DISCLOSURE REGARDING FORWARD LOOKING STATEMENTS

On one or more occasions, we may make statements regarding our assumptions, projections, expectations, targets, intentions or beliefs about future events. All statements other than statements of historical facts included or incorporated by reference in this annual report on Form 10-K are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act).

Words or phrases such as anticipates, believes, estimates, expects, intends, may, plans, potential, predicts, projects, should, continue, will likely result or other comparable expressions or the negative of these terms identify forward-looking statements. Forward-looking statements reflect our current views about future events and are subject to risks, uncertainties, assumptions and changes in circumstances that may cause actual results or outcomes to differ materially from those expressed in any forward-looking statement. We caution that while we make such statements in good faith and we believe such statements are based on reasonable assumptions, including without limitation, management's examination of historical operating trends, data contained in records and other data available from third parties, we cannot assure you that our projections will be achieved.

Our actual results may differ significantly from any results expressed or implied by these forward-looking statements. Some, but not all, of the factors that might cause such a difference include, but are not limited to:

the factors discussed in this report set forth in Item 1A under the section titled Risk Factors ;

the effects of the recent global economic recession upon business and leisure travel and the hotel markets in which we invest;

our liquidity and refinancing demands;

our ability to obtain or refinance maturing debt;

our ability to maintain compliance with covenants contained in our debt facilities;

our ability to meet the requirements of the Maryland General Corporation Law, or MGCL, with respect to the payment of preferred dividends on the June 29, 2012 payment date as further described below;

stagnation or further deterioration in economic and market conditions, particularly impacting business and leisure travel spending in the markets where our hotels operate and in which we invest, including luxury and upper upscale product;

general volatility of the capital markets and the market price of our shares of common stock;

availability of capital;

our ability to dispose of properties in a manner consistent with our investment strategy and liquidity needs;

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hostilities and security concerns, including future terrorist attacks, or the apprehension of hostilities, in each case that affect travel within or to the United States, Mexico, Germany, England or other countries where we invest;

difficulties in identifying properties to acquire and completing acquisitions;

our failure to maintain effective internal control over financial reporting and disclosure controls and procedures;

risks related to natural disasters;

increases in interest rates and operating costs, including insurance premiums and real property taxes;

contagious disease outbreaks, such as the H1N1 virus outbreak;

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delays and cost-overruns in construction and development;

marketing challenges associated with entering new lines of business or pursuing new business strategies;

our failure to maintain our status as a REIT;

changes in the competitive environment in our industry and the markets where we invest;

changes in real estate and zoning laws or regulations;

legislative or regulatory changes, including changes to laws governing the taxation of REITs;

changes in generally accepted accounting principles, policies and guidelines; and

litigation, judgments or settlements.

Any forward-looking statement speaks only as of the date on which such statement is made. New factors emerge from time to time and it is not possible for management to predict all such factors. We do not intend, and disclaim any duty or obligation, to update or revise any industry information or forward-looking statements set forth in this annual report on Form 10-K to reflect new information, future events or otherwise, except as required by law. Readers are urged to carefully review and consider the various disclosures made in this annual report on Form 10-K and in our other documents filed with the Securities and Exchange Commission (SEC) that attempt to advise interested parties of the risks and other factors that may affect our business, prospects and results of operations and financial condition.

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PART I

ITEM 1. BUSINESS.

Overview

Strategic Hotels & Resorts, Inc. (SHR) was incorporated in Maryland in January 2004 to acquire and asset-manage upper upscale and luxury hotels that are subject to long-term management contracts. The terms upper upscale and luxury are classifications of hotels by brand that are defined by Smith Travel Research, an independent provider of lodging industry statistical data. We completed our initial public offering in June 2004. Our accounting predecessor, Strategic Hotel Capital, L.L.C. (SHC LLC), was founded in 1997 by Laurence Geller, our president and chief executive officer, Goldman, Sachs & Co.'s Whitehall Fund and others. We own our properties through our investment in Strategic Hotel Funding, L.L.C., our operating partnership, which we refer to herein as SH Funding, and its subsidiaries.

We operate as a self-administered and self-managed real estate investment trust (REIT) managed by our board of directors and executive officers and conduct our operations through our direct and indirect subsidiaries including SH Funding. We are the managing member of SH Funding and hold approximately 99% of its membership units as of February 22, 2012.

As of February 22, 2012, we:

wholly own or lease 14 hotels, have a 53.5% interest in an affiliate that owns a hotel where we asset manage such hotel, and have 50.0% and 34.3% interests in, and act as asset manager for, two unconsolidated affiliates that each own one hotel;

own land held for development including:

20.5 acres of oceanfront land adjacent to our Four Seasons Punta Mita Resort, Nayarit, Mexico and 60.0 acres of oceanfront land near the Four Seasons Punta Mita Resort;

a 20,000 square-foot parcel of land on the ocean in Santa Monica, California adjacent to our Loews Santa Monica Beach Hotel entitled for development and residential units;

a 50% interest in an unconsolidated affiliate that owns 10.0 acres of land adjacent to the Fairmont Scottsdale Princess hotel; and

a 31% interest in an unconsolidated affiliate with two unaffiliated parties that is developing the fractional ownership program known as the Four Seasons Residence Club Punta Mita.

We do not operate any of our hotels directly; instead we employ internationally known hotel management companies to operate them for us under management contracts or operating leases. Our existing hotels are operated under the widely-recognized upper upscale and luxury brands of Fairmont®, Four Seasons®, Hyatt®, InterContinental®, Loews®, Marriott®, Ritz-Carlton® and Westin®. The Hotel del Coronado is operated by a specialty management company, KSL Resorts.

We seek to maximize asset values and operating results through asset management. Although we have no imperative to grow, we will opportunistically seek to acquire additional properties that meet our disciplined investment criteria.

As used in this report, references to we, our, us, and the Company are references to SHR together, except as the context otherwise requires, with its consolidated subsidiaries, including SH Funding.

Business Strategy

We are a preeminent owner of upper upscale and luxury branded hotels located primarily in North America with select international hotels. Our strategy involves the acquisition of hotels with strong underlying real estate

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values, adding value through the application of our management's superior asset management skills, identifying redevelopment opportunities to enhance cash flow and value, and opportunistic dispositions of hotels upon completion of our value enhancement and cash flow generating strategies.

Acquisition Strategy

One of our core competencies is a diligent approach to acquisitions that includes continuous research-based selection of target markets and individual properties. We target upper upscale and luxury hotels in select urban and resort markets, including major business centers and leisure destinations, with strong growth characteristics and high barriers to entry. We believe that the upper upscale and luxury hotel sector is an extremely attractive sector for long-term investment, especially considering the supply constraints characteristic of that sector.

Asset Management Strategy

We believe that we can enhance our cash flow and earnings growth through expert asset management, which we expect will ultimately generate increased operating margins and higher investment returns. Our value-added asset management strategy has the following general components:

Working in partnership with the hotel management companies that operate our hotels, we build an asset management approach to enhance the cash flow and value of our properties. We have multi-property relationships with a select group of hotel management companies that in our opinion have strong brand recognition, superior marketing capabilities, management depth and an ability to work with our team to create efficient operations. We improve hotel operating performance through the application of value-added programs involving consumer and market research, competitive benchmarking, technology upgrades and systems development and upgrades.

We provide rigorous oversight of our properties and the hotel management companies that operate them to ensure the alignment of the hotel management companies' and our interests and to monitor the hotel management companies' and our compliance with the management contracts relating to our properties. Typically, this oversight allows us to maximize operating margins and enhance property values.

Redevelopment Strategy

A major component of our value creation strategy is to create incremental sources of income from our properties through thoughtfully executed and consumer market research based redevelopment.

Our current portfolio now includes capital investments, which give us a competitive portfolio in excellent physical condition that management believes can provide relative outperformance during the current recovery cycle. We have planned a variety of property investment programs with the goal of enhancing the cash flow growth of our portfolio through the careful execution of these plans.

Disposition Strategy

We recycle capital for future investments through opportunistic dispositions. We would consider the disposition of all or part of our investment in a property in circumstances where we believe our asset management strategy has maximized the property's value, the proceeds of the disposition are unusually attractive, the market in which the property is located is declining or static, or competition in the market requires substantial capital investment that will not generate returns that meet our criteria.

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Proceeds from dispositions would generally be intended to be reinvested in redevelopment activities in our existing portfolio, the acquisition of additional hotel properties where the application of our life cycle-based investment strategy can begin again, or enhancement of our balance sheet.

We continually undertake a comprehensive review of our assets against sources of capital in the marketplace with the objective of seeking strategies to sell assets in order to supplement our liquidity position.

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Competition

The hotel industry is highly competitive and the hotels in which we invest are subject to competition from other hotels for guests. Competition is based on a number of factors, most notably convenience of location, brand affiliation, price, range of services, guest amenities or accommodations offered and quality of customer service. Competition is often specific to the individual markets in which our properties are located and includes competition from existing and new hotels operated under brands in the upper upscale and luxury segments. Increased competition could have a material adverse effect on the occupancy rate, average daily room rate and room revenue per available room of our hotels or may require us to make capital improvements that we otherwise would not have to make, which may result in decreases in our profitability.

Because our hotels operate in the upper upscale and luxury segment of the market, we face increased competition from providers of less expensive accommodations, such as limited service hotels or independent owner-managed hotels, during periods of economic downturn when leisure and business travelers become more sensitive to room rates. As a result, there is pressure to lower average daily rates during such periods to compete for these guests.

We face competition from institutional pension funds, private equity investors, other REITs and numerous local, regional and national owners in each of our markets. Some of these entities may have substantially greater financial resources and may be able to accept more risk than we can prudently manage. Competition may generally reduce the number of suitable investment opportunities offered to us and increase the bargaining power of property owners seeking to sell their properties to us.

Seasonality

For information relating to the seasonality of our business, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Seasonality on page 63 of this Form 10-K.

Employees

As of February 22, 2012, we had 37 full-time and five part-time corporate employees. We believe that our relations with our employees are good. None of our corporate employees are unionized.

Environmental

Environmental consultants retained by us or our lenders have conducted environmental site assessments on many of our properties. These environmental assessments often relied on older environmental assessments prepared in connection with a prior financing or acquisition. The lenders did not conduct environmental assessments on our European properties, although older environmental assessments or building engineering surveys exist for these properties. The environmental assessments are designed to evaluate the potential for environmental contamination on properties, but these assessments will not necessarily reveal the existence or extent of all environmental conditions, liabilities or compliance concerns at the properties.

Although the environmental assessments that have been conducted with respect to certain of our properties disclose certain conditions on our properties and the use of hazardous substances in operation and maintenance activities that could pose a risk of environmental contamination or liability, we are not aware of any environmental liability that we believe would have a material adverse effect on our business, financial position, results of operations or cash flows. See Item 1A. Risk Factors Environmental and other governmental laws and regulations could increase our compliance costs and liabilities and adversely affect our financial condition and results of operations and Item 1A. Risk Factors The presence of any environmental conditions at our properties could result in remediation and other costs and liabilities and adversely affect our financial condition and results of operations.

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Insurance

Our management believes that our properties are adequately covered by insurance, subject to the risks described under Item 1A. Risk Factors, including, among others, the factors described under Uninsured and underinsured losses could adversely affect our financial condition and results of operations, which may affect our ability to make distributions to our stockholders. We are responsible for arranging the insurance for most of our hotels, although in certain cases, the hotel management companies that operate our hotels assume responsibility for arranging insurance under the relevant management agreement. Our properties are covered by blanket insurance policies, which cover multiple properties. In the event that these blanket policies are drawn on to cover certain losses on certain properties, the amount of insurance coverage available under such policies could thereby be reduced and could be insufficient to cover the remaining properties' insurable risks.

REIT Structure

Subject to certain limitations, REITs may own, directly or indirectly, up to 100% of the stock of a taxable REIT subsidiary (TRS) that can engage in businesses prohibited to a REIT. Thus, hotel REITs may own TRSs that lease hotels from the REIT, rather than requiring the lessee to be a separate, unaffiliated party. However, hotels leased to a TRS must be managed by an unaffiliated third party. The TRS provisions are complex and impose several conditions on the use of TRSs. No more than 25% of a REIT's assets may consist of securities of TRSs, and no more than 25% of a REIT's assets may consist of non-qualifying assets, including securities of TRSs and other taxable subsidiaries. In addition, REITs may generally not own more than 10% of the voting power or value of a corporation that is not treated as a TRS.

Ownership of Hotels

Where we have an ownership interest in a hotel, the entity through which we hold such ownership interest (a Strategic Ownership Entity) will generally lease the hotel to one of our TRSs and the TRS will enter into a management agreement with an independent third party for such party to operate the hotel. A lease between a Strategic Ownership Entity and one of our TRSs (an Affiliate Lease) provides for the TRS to pay to the Strategic Ownership Entity a base rent plus a percentage rent (as more fully described below). An Affiliate Lease must contain economic terms that are similar to a lease between unrelated parties or, pursuant to the RMA, the Strategic Ownership Entity may have to pay a 100% penalty tax on some of the payments it receives from our TRS under such Affiliate Lease.

Each Affiliate Lease has a non-cancelable term of three to five years, subject to earlier termination upon the occurrence of certain contingencies such as damage or destruction that renders the hotel unsuitable for our TRS' use and occupancy, condemnation or our sale or disposition of the hotel.

During the term of each Affiliate Lease, our TRS is obligated to pay a fixed annual base rent and a percentage rent to the applicable Strategic Ownership Entity. Percentage rent is calculated by multiplying fixed percentages by gross room revenues and other revenues, subject to certain adjustments. Percentage rent is paid quarterly. Base rent accrues and is paid monthly. Base rents and percentage rents are adjusted annually for changes in the consumer price index or similar indices.

Fixed charges, including real estate and personal property taxes, capital expenditures and a reserve for capital expenditures are obligations of the lessor under our Affiliate Lease. Our TRSs are required to pay rent, all costs and expenses and all utility and other charges incurred in the operation of the hotels we own. The party responsible for maintaining insurance on a property is dependent on the specific lease.

Third Party Lease Agreements

We are the tenant under a lease with a third-party landlord for the Marriott Hamburg. We are also the tenant under ground leases with third-party landlords where we lease the land for the Marriott Lincolnshire Resort and

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the Marriott London Grosvenor Square. Additionally, an unconsolidated affiliate is a tenant under a ground lease for a parcel of land that is part of the Fairmont Scottsdale Princess hotel property. The remaining life on the initial terms of these third party leases range from nine to 73 years. These third party lease agreements require us to make annual rental payments comprised of a minimum rental amount (subject to indexation) and may also include additional rent comprised of a percentage of hotel operating profit, less minimum rent, or the greater of a minimum rental amount and a percentage of certain revenues.

Hotel Management Agreements

Most of our hotels are managed and operated by third parties pursuant to management agreements entered into between our TRSs and hotel management companies. These management agreements generally provide for the payment of base management fees within a range of 1.0% to 4.0% of revenues, as defined in the applicable agreements. In addition, an incentive fee may be paid if certain criteria are met. Certain of the management agreements also provide for the payment by us of advisory fees or license fees. The remaining terms (not including renewal options) of these management agreements range from three to 25 years. A management agreement with one of our operators typically has the terms described below.

Operational services. The manager has exclusive authority to supervise, direct and control the day-to-day operation and management of the hotel, including establishing all room rates, processing reservations, procuring inventories, supplies and services, and preparing public relations, publicity and marketing plans for the hotel.

Compensation of manager. The manager receives compensation in the form of a base management fee and an incentive management fee, typically calculated as percentages of gross revenues and operating profits, respectively. In some cases, the incentive management fee is paid only after we have received a certain level of income.

Executive supervision and management services. The manager supervises all managerial and other employees for the hotel, reviews the operation and maintenance of the hotel, prepares reports, budgets and projections and provides other administrative and accounting support services to the hotel. In some cases, we maintain authority to approve the appointment of the hotel's general manager.

Chain services. Our management agreements require the managers to furnish chain services that are generally made available to other hotels managed by such operators. Such services include: (1) the development and operation of computer systems and reservation services, (2) management and administrative services, (3) marketing and sales services, (4) human resources training services and (5) such additional services as may from time to time be more efficiently performed on a national, regional or group level.

Working capital. Our management agreements typically require us to maintain working capital for a hotel and to fund the cost of fixed asset supplies such as linens and other similar items. We are also responsible for providing funds to meet the cash needs for the hotel operations if at any time the funds available from hotel operations are insufficient to meet the financial requirements of the hotel.

Furniture, fixtures and equipment replacements. Our management agreements generally provide that once each year the manager will prepare a list of furniture, fixtures and equipment to be acquired and certain routine repairs to be performed in the next year and an estimate of the funds that are necessary, subject to our review and approval. In addition, we are required to provide to the manager all necessary furniture, fixtures and equipment for the operation of a hotel (including funding any required furniture, fixtures and equipment replacements). For purposes of funding the furniture, fixtures and equipment replacements, a specified percentage of the gross revenues of the hotel is deposited by the manager in a separate account (typically 4.0% to 5.0%).

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Building alterations, improvements and renewals. Our management agreements generally require the manager to prepare an annual estimate of the expenditures necessary for major repairs, alterations, improvements, renewals and replacements to the structural, mechanical, electrical, heating, ventilating,

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air conditioning, plumbing and vertical transportation elements of a hotel. In addition to the foregoing, the management agreements generally provide that the manager may propose such changes, alterations and improvements to the hotel as are required by reason of laws or regulations or, in the manager's reasonable judgment, to keep the hotel in a safe, competitive and efficient operating condition.

Sale of the hotel. Most of our management agreements limit our ability to sell, lease, or otherwise transfer a hotel unless the transferee is not a competitor of the manager, and unless the transferee assumes the related management agreement and meets specified other conditions.

Service marks. During the term of our management agreements, the service mark, symbols and logos currently used by the manager may be used in the operation of the hotel. Any right to use the service marks, logo and symbols and related trademarks at a hotel will terminate with respect to that hotel upon termination of the management agreement with respect to such hotel.

We lease one of our hotels, the Marriott Hamburg, pursuant to a lease agreement whereby rent is paid by the hotel management company that operates the hotel, as lessee, to us for an amount equal to a fixed base rent plus a specified percentage of profits in excess of the base rent. Otherwise, the terms of the lease are similar to the terms of our management contracts described above.

Code of Business Conduct and Ethics and Corporate Governance Documents

We have adopted a code of business conduct and ethics that applies to all of our employees, directors and officers, including our principal executive officer, principal financial officer and principal accounting officer. This code of business conduct and ethics is designed to comply with SEC regulations and New York Stock Exchange (NYSE) corporate governance rules related to codes of conduct and ethics and is posted on our corporate website at www.strategichotels.com. We intend to disclose future amendments to certain provisions of our code of business conduct and ethics, or waivers of such provisions granted to directors and specified officers, on our website within four business days following the date of such amendment or waiver. In addition, our corporate governance guidelines and charters for our audit, compensation and corporate governance and nominating committees are also posted on our corporate website. Copies of our code of business conduct and ethics, our corporate governance guidelines and our committee charters are also available free of charge upon request directed to Corporate Secretary, Strategic Hotels & Resorts, Inc., 200 West Madison Street, Suite 1700, Chicago, Illinois 60606.

Geographic and Business Segment Information

For information with respect to revenues from and our long-lived assets located in different geographic areas, refer to Item 8. Financial Statements and Supplementary Data 18. Geographic and Business Segment Information.

Where to Find More Information

We maintain a website at www.strategichotels.com. Through our website, we make available, free of charge, our annual proxy statement, our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. The SEC maintains a website that contains these reports at www.sec.gov.

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ITEM 1A. RISK FACTORS.

In addition to the information and factors discussed elsewhere in this annual report on Form 10-K, including our consolidated financial statements and the related notes, the factors disclosed below could cause our actual results to differ materially from those projected in any future-looking statements and could affect our future financial performance.

Risks related to our business

The U.S. and other financial markets have recently been in turmoil and the U.S. and other economies in which we operate are in the midst of a slow but fragile economic recovery and highly volatile stock market climate, which continue to negatively impact our operations and our liquidity.

The U.S. and other financial markets have recently experienced extreme dislocations and a severe contraction in available liquidity globally as important segments of the credit markets were impaired. Global financial markets were disrupted by, among other things, volatility in securities prices, ratings downgrades and declining valuations, and this disruption has been acute in real estate related markets. This disruption has led to a decline in business and consumer confidence and increased unemployment and has precipitated an economic recession around the globe. As a consequence, owners and operators of commercial real estate, including hotels and resorts, may experience a stagnation or further declines of business and real estate values in the United States or elsewhere and continuing liquidity constraints as lenders may be unwilling or unable to originate new credit on commercially reasonable terms, or at all, and the capital markets may be otherwise unavailable. We are unable to predict the likely duration of the slow, but fragile economic recovery and highly volatile stock market climate and the effects they may have on our business, financial condition and results of operations.

We incurred losses in fiscal years 2011, 2010, 2009 and 2008 due to the negative economic environment, and we may continue to incur losses in the future.

We incurred net losses of \$4.9 million, \$230.8 million, \$246.4 million and \$317.5 million for our 2011, 2010, 2009 and 2008 fiscal years, respectively. The recent economic downturn has negatively impacted business and leisure travel leading to a reduction in revenues at our hotel properties. The slow rate of the fragile economic recovery or a further decline in economic conditions will likely produce continued losses. There can be no assurance that we will resume profitable operations and generate net income for our stockholders in the near term or at all.

Our financial covenants may adversely affect our financial position, results of operations and liquidity.

The agreement governing our bank credit facility and certain other agreements include financial and other covenants that must be met for us to remain in compliance with those agreements. Those agreements also contain customary restrictions, requirements and other limitations, including restrictions on our ability to incur additional indebtedness. Importantly, the bank credit facility contains financial covenants that must be met, including the maintenance of stipulated minimum levels of tangible net worth and fixed charge coverage, and maximum levels of leverage and borrowing base availability. Availability under the bank credit facility is based on, among other factors, the lesser of the calculation of 1.2 times debt service coverage based on the greater of the in-place interest rate or 7.0% debt constant for the borrowing base assets or a 60% advance rate against the appraised value of the borrowing base assets. The actual interest rate on the bank credit facility is LIBOR plus 3.00%, which equates to 3.30% as of December 31, 2011. Our ability to borrow under our bank credit facility is subject to compliance with these financial and other covenants, and our ability to comply with these covenants will be impacted by, among other things, any deterioration in our operations brought on by the recent economic downturn, potential further declines in our property values, additional borrowings to maintain our liquidity and fund our capital and financing obligations, and security concerns impacting travel to Mexico.

Our available capacity under the bank credit facility and compliance with financial covenants in future periods will depend substantially on the financial results of our hotels, and in particular, the results of the

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borrowing base assets, which include the Four Seasons Punta Mita Resort, Marriott Lincolnshire Resort, Ritz-Carlton Half Moon Bay and Ritz-Carlton Laguna Niguel hotels. The recent operating results of the Four Seasons Punta Mita Resort in Mexico has been negatively impacted by security concerns impacting travel to Mexico, as well as the recent economic downturn. If these negative conditions persist, the financial results of our hotels deteriorate, or if our property values decline, the maximum availability under the bank credit facility may decline to a level below our short-term borrowing needs. If that were to occur, outstanding borrowings exceeding the maximum availability under the bank credit facility would need to be repaid to avoid a default under the bank credit facility, absent an amendment or waiver. If we are unable to borrow under our bank credit facility or to refinance existing indebtedness, we may be prevented from funding our working capital needs or proposed debt restructurings.

In the event that the slow, but fragile economic recovery stalls and negative economic conditions worsen and our business significantly deteriorates, we may be required to take further steps to acquire the funds necessary to satisfy our short-term cash needs, including possibly liquidating some of our assets on terms that would be less attractive than would be obtainable after conditions in the economy, the credit markets and the hotel markets improve. If negative conditions worsen, our business deteriorates further and we do not achieve a successful disposition of assets or increase our liquidity through alternative channels or modify or obtain a waiver to certain terms of our bank credit facility, we may breach one or more of our financial covenants or the maximum availability under the bank credit facility may fall below our short-term borrowing needs. A default under the bank credit facility would allow the lenders to declare all amounts outstanding under the facility to become due and payable. Additionally, such an acceleration event would allow for acceleration of the interest rate swaps (with a termination cost of \$70.7 million as of December 31, 2011).

In addition, our lenders, including the lenders participating in our bank credit facility, may have suffered losses related to their lending and other financial relationships, especially because of the general weakening of the economy and increased financial instability of many borrowers (and may suffer additional losses if negative conditions worsen and the economy deteriorates further). As a result, lenders may become less able or unwilling to allow us to draw down on our bank credit facility and/or we may be unable to obtain other financing on favorable terms or at all. Our financial condition and results of operations would be adversely affected if we were unable to draw funds under our bank credit facility because of a lender default or if we were unable to obtain other financing.

We have substantial debt, a portion of which is variable-rate debt, and upon maturity, we plan to refinance with new debt, which may not be available when required on optimal terms or at all.

We have a substantial amount of outstanding indebtedness, a portion of which bears interest at a variable-rate, and to the extent available, we may borrow additional variable-rate debt under our bank credit facility. When we seek to refinance our outstanding indebtedness, our interest expense may increase. Increases in interest rates on our existing variable-rate indebtedness, or on new indebtedness we incur when refinancing our existing indebtedness, would increase our interest expense, which could harm our cash flow and our ability to pay distributions. As of December 31, 2011, we had total debt of \$1.05 billion, and, including the effect of interest rate swaps, approximately 93.1% of our total debt had fixed interest rates.

Our significant debt may negatively affect our business and financial results, including:

requiring us to use a substantial portion of our funds from operations to make required payments on principal and interest, which reduces the amounts available for distributions to our stockholders and funds available for operations, capital expenditures, future business opportunities and other purposes;

making us more vulnerable to economic and industry downturns and reducing our flexibility in responding to changing business and economic conditions;

limiting our ability to borrow more money for operations, capital or to finance acquisitions in the future; and

requiring us to dispose of properties to make required payments of interest and principal.

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Since we anticipate that our internally generated cash will be adequate to repay only a portion of our indebtedness prior to maturity, we expect that we will be required to repay debt through refinancings and/or equity offerings. The amount of our existing indebtedness may adversely affect our ability to repay debt through refinancings. See the discussion under the subheading "Debt Maturity:" in Note 9 of the Notes to our Consolidated Financial Statements included in Item 8 of Part II of this annual report on Form 10-K for quantified information regarding our debt maturities as of December 31, 2011. While the credit markets have begun to recover from the severe contraction experienced during the recent economic downturn, there can be no assurance that we will be able to refinance our debt with new borrowings or raise capital through the sale of equity. If we are unable to refinance or restructure our indebtedness on acceptable terms, or at all, we might be forced to dispose of one or more of our properties on disadvantageous terms, or forfeit the property securing such indebtedness, which might result in losses to us and which might adversely affect cash available for distributions to our stockholders. Alternatively, any debt we may arrange may carry a higher rate of interest or the shares we issue in any equity offering may require a higher rate of dividends or other dilutive terms. As a result, certain growth initiatives could prove more costly or not economically feasible. A failure to retain or refinance our bank credit facility or to add new or replacement debt facilities could have a material adverse effect on our business, financial condition and results of operations.

The \$97.5 million mortgage debt related to the Hyatt Regency La Jolla hotel matures September 1, 2012. We own a 53.5% controlling interest in an affiliate that owns this hotel. There can be no assurance that we and our partner will be able to refinance or restructure this indebtedness or cure or receive a waiver for an event of default if one were to occur. If this occurs, we may be forced to forfeit the property or seek legal protection from creditors, both of which could result in losses to us and which would adversely impact cash available for distributions.

We also could incur additional debt in connection with future acquisitions of real estate. We may, in some instances, to the extent available, borrow under our bank credit facility or borrow new funds to acquire properties. The curtailment of lending by many traditional commercial real estate lenders impedes our ability to grow our portfolio of hotels through future acquisitions and otherwise may prevent us from executing our business plans, including limiting the likelihood of successful asset dispositions. In addition, we may incur mortgage debt by obtaining loans secured by a portfolio of some or all of the real estate properties we acquire. If necessary or advisable, we may also borrow funds to satisfy the requirement that we distribute to stockholders at least 90% of our annual REIT taxable income or to ensure otherwise that we maintain our qualification as a REIT for U.S. federal income tax purposes.

Our working capital and liquidity reserves may not be adequate to cover all of our cash needs and we may have to obtain financing from either affiliated or unaffiliated sources. The recent financial market turmoil and economic recession have severely contracted available liquidity and therefore sufficient financing may not be available or, if available, may not be available on reasonable terms. Additional borrowings for working capital purposes will increase our interest expense, and therefore may harm our financial condition and results of operations.

Our organizational documents do not limit the amount of indebtedness that we may incur. To the extent we become more leveraged, the resulting increase in our debt service obligations would reduce cash available for distributions to our stockholders and could adversely affect our ability to make payments on our outstanding indebtedness and harm our financial condition.

The uncertain environment in the lodging industry and the economy generally will continue to impact our financial results and growth.

While the global economic climate appears to be improving, it is unclear whether the lodging industry, which prior to 2008 had experienced a period of sustained growth, will stagnate or decline further. Negative publicity regarding luxury hotels and decreases in airline capacity could also reduce demand for our hotel rooms. Accordingly, our financial results and growth could be harmed if the global economic climate does not continue to improve or becomes worse.

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We own primarily upper upscale and luxury hotels, and the upper upscale and luxury segments of the lodging market are highly competitive and generally subject to greater volatility than other segments of the market, which could negatively affect our profitability.

The upper upscale and luxury segments of the hotel business are highly competitive. Our hotels compete on the basis of location, room rates and quality, service levels, reputation and reservations systems, among many other factors. There are many competitors in our hotel chain scale segments, and many of these competitors have substantially greater marketing and financial resources than we have. This competition could reduce occupancy levels and room revenue at our hotels, which would harm our operations. Over-building in the hotel industry may increase the number of rooms available and may decrease occupancy and room rates. We also face competition from nationally recognized hotel brands with which we are not associated. In addition, in periods of weak demand, profitability is negatively affected by the relatively high fixed costs of operating upper upscale and luxury hotels when compared to other classes of hotels.

The illiquidity of real estate investments and the lack of alternative uses of hotel properties could significantly limit our ability to respond to adverse changes in the performance of our properties and harm our financial condition.

Because real estate investments are relatively illiquid, our ability to promptly sell one or more of our properties in response to changing economic, financial and investment conditions is limited. We cannot predict whether we will be able to sell any property for the price or on the terms set by us, or whether any price or other terms offered by a prospective purchaser would be acceptable to us. We also cannot predict the length of time needed to find a willing purchaser and to close the sale of a property. The difficulty in selling an asset is exacerbated by the dislocation in the debt and equity markets currently being experienced.

In addition, hotel properties may not readily be converted to alternative uses if they were to become unprofitable due to competition, age of improvements, decreased demand or other factors. The conversion of a hotel to alternative uses would also generally require substantial capital expenditures.

We may be required to expend funds to correct defects or to make improvements before a property can be sold. We may not have funds available to correct those defects or to make those improvements and as a result our ability to sell the property would be limited. These factors and any others that would impede our ability to respond to adverse changes in the performance of our properties could significantly harm our financial condition and results of operations.

Certain of our long-lived assets, intangible assets, investments in unconsolidated affiliates and goodwill have in the past become impaired and may become impaired in the future.

We periodically review each of our hotels and any related goodwill for possible impairment. Based on the results of these analyses, in fiscal year 2010 we wrote off \$141.9 million to impairment losses to reduce the carrying values of long-lived assets and investments in unconsolidated affiliates on our balance sheet to their estimated fair values. Our other hotels and related goodwill may become impaired, or our hotels which have previously become impaired may become further impaired, in the future, which may adversely affect our financial condition and results of operations.

We rely to a significant extent on our president and chief executive officer, Mr. Laurence Geller, the loss of whom could have a material adverse effect on our business.

Our continued success will depend to a significant extent on the efforts and abilities of our president and chief executive officer, Mr. Laurence Geller. Mr. Geller is an experienced hotel industry senior executive, operator and consultant with over 40 years of experience working with many major multinational hotel companies and executives. Mr. Geller is actively engaged in our management and determines our strategic direction, especially with regard to our operational, financing, acquisition and disposition activities. Mr. Geller's departure could have a material adverse effect on our operations, financial condition and operating results. Mr. Geller's employment agreement was amended and restated on August 27, 2009. Pursuant to that agreement,

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Mr. Geller will serve as our president and chief executive officer through December 31, 2012, subject to earlier termination under certain circumstances described in the agreement. We can make no assurance that Mr. Geller's employment agreement will be extended beyond its current expiration date.

The geographic concentration of our hotels in California makes us more susceptible to an economic downturn or natural disaster in that state.

As of February 22, 2012, seven of the hotels we own were located in California, the greatest concentration of our portfolio of properties in any state. California has been historically at greater risk to certain acts of nature, such as fire, floods and earthquakes, than other states, and has also been subject to a more pronounced economic downturn than other states. It is also possible that a change in California laws applicable to hotels and the lodging industry may have a greater impact on us than a change in comparable laws in another jurisdiction where we have hotels. Accordingly, our business, financial condition and results of operations may be particularly susceptible to a natural disaster, downturn or changes in the California economy.

We have suspended the payment of dividends on our common stock and have suspended the payment of dividends on our preferred stock in the past.

On November 4, 2008, we suspended payment of our dividend on our shares of common stock. In addition, in February 2009, our board of directors elected to suspend the quarterly dividend beginning with the first quarter of 2009 to holders of shares of our 8.50% Series A Cumulative Redeemable Preferred Stock, 8.25% Series B Cumulative Redeemable Preferred Stock and 8.25% Series C Cumulative Redeemable Preferred Stock, which we collectively refer to herein as our Preferred Stock. We suspended these dividend payments in an effort to preserve liquidity. Pursuant to the Articles Supplementary governing our Preferred Stock, if we do not pay quarterly dividends on our Preferred Stock for six quarters, whether or not consecutive, the size of our board of directors will be increased by two and the holders of our Preferred Stock will have the right to elect two additional directors to our board. As of December 31, 2011, we did not pay quarterly dividends for twelve quarters. There have been no new directors added to the board pursuant to this right. In the fourth quarter of 2011, our board of directors authorized, and we declared, the payment of accrued and unpaid dividends through September 30, 2011, and dividends for the quarter ended December 31, 2011, which we collectively refer to herein as the Unpaid Dividends, and a sum sufficient for the payment of the Unpaid Dividends has been set apart for payment on our books through the recording of a liability in accordance with the terms of our charter; however, the Unpaid Dividends are not payable until June 29, 2012, are payable to holders of record as of the close of business on June 15, 2012 and are contingent upon our ability to meet, on the June 29, 2012 Unpaid Dividends payment date, the requirements of the MGCL with respect to the payment of dividends, or the Maryland Dividend Requirement. In addition, in February 2012, our board of directors authorized, and we declared, the payment of dividends on our Preferred Stock for the quarter ending March 31, 2012, which we refer to herein as the First Quarter 2012 Dividends, payable on June 29, 2012, to holders of record as of the close of business on June 15, 2012, contingent upon our ability to meet the Maryland Dividend Requirement on such payment date. A sum sufficient for the payment of the First Quarter 2012 Dividends has been set apart for payment on our books through the recording of a liability in accordance with the terms of our charter. While we cannot make any guarantees, we currently expect to be able to meet the Maryland Dividend Requirement on the June 29, 2012 Unpaid Dividends and First Quarter 2012 Dividends payment date. We can provide no assurance that we will not suspend the payment of quarterly dividends on our Preferred Stock in the future. In addition, we can provide no assurance as to when we will resume paying dividends on our common stock, if ever.

If we fail to maintain effective internal control over financial reporting and disclosure controls and procedures in the future, we may not be able to accurately report our financial results, which could have an adverse effect on our business.

If our internal control over financial reporting and disclosure controls and procedures are not effective, we may not be able to provide reliable financial information. If we discover deficiencies in our internal controls, we will make efforts to remediate these deficiencies; however, there is no assurance that we will be successful either

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in identifying deficiencies or in their remediation. Any failure to maintain effective controls in the future could adversely affect our business or cause us to fail to meet our reporting obligations. Such non-compliance could also result in an adverse reaction in the financial marketplace due to a loss of investor confidence in the reliability of our financial statements. In addition, perceptions of our business among customers, suppliers, rating agencies, lenders, investors, securities analysts and others could be adversely affected.

Rising operating expenses and costs of capital improvements could reduce our cash flow, earnings before interest expense, taxes, depreciation and amortization (EBITDA) and funds available for future distributions.

Our properties are subject to operating risks common to the lodging industry in general. If a property's occupancy or room rates drop to the point where its revenues are insufficient to cover its operating expenses, then we could be required to spend additional funds for that property's operating expenses. Our properties are continually subject to increases in real estate and other tax rates, wages and benefits, utility costs, operating expenses, insurance costs, repairs and maintenance and administrative expenses, which may reduce our cash flow, EBITDA and funds available for future distributions to our stockholders.

Our hotel properties have an ongoing need for renovations and other capital improvements, including replacements, from time to time, of furniture, fixtures and equipment. Some of these capital improvements are mandated by health, safety or other regulations. These capital improvements may give rise to (i) a possible shortage of available cash to fund capital improvements, (ii) the possibility that financing for these capital improvements may not be available to us on affordable terms and (iii) uncertainties as to market demand or a loss of market demand after capital improvements have begun. The costs of these capital improvements could adversely affect our financial condition and amounts available for distributions to our stockholders.

Our business and operating results depend in large part upon the performance of third-party hotel management companies that manage our hotels.

Our hotels are managed by third-party hotel management companies pursuant to management agreements or, with respect to the Marriott Hamburg, the lease applicable to that property. Therefore, our business and operating results depend in large part upon the performance of these hotel management companies under these management agreements.

Under the terms of these management agreements, the third-party hotel managers control the daily operations of our hotels. We do not have the authority to require any hotel to be operated in a particular manner or to govern any particular aspect of the daily operations of any hotel (for instance, setting room rates). Thus, even if we believe our hotels are being operated inefficiently or in a manner that does not result in satisfactory occupancy rates, net revenue per available room or average daily rate, we may not be able to force the hotel management companies in question to change their methods of operation of our hotels. Additionally, in the event that we need to replace any hotel management company, we may be required by the terms of the applicable management agreement to pay a substantial termination fee and may experience disruptions at any affected hotel. The effectiveness of the hotel management companies in managing our hotels will, therefore, significantly affect the revenues, expenses and value of our hotels. Occasionally, we have discovered accounting errors at some of our properties relating to the improper recording of income statement expenses, misstated inventories and other items apparently caused by poor accounting practices and oversight. In the event our third-party hotel management companies are not able to implement and maintain appropriate accounting controls with respect to our properties, our business, results of operations and financial condition could be adversely affected.

Additionally, the hotel management companies that operate our hotels and their affiliates own, operate, or franchise properties other than our properties, including properties that directly compete with our properties. Therefore, a hotel management company may have different interests than our own with respect to short-term or long-term goals and objectives, including interests relating to the brand under which such hotel management company operates. Such differences may be significant depending upon many factors, including the remaining term of the applicable management agreement, trade area restrictions with respect to competitive practices by the hotel management company or its affiliates or differing policies, procedures or practices. Any of these factors

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may adversely impact the operation and profitability of a hotel, which could harm our financial condition and results of operations.

All revenues generated at our hotels, including credit card receivables, are deposited by the payors into accounts maintained and controlled by the relevant hotel management company, which pays operating and other expenses for the relevant hotel (including real and personal property taxes), pays itself management fees in accordance with the terms of the applicable management agreement and makes deposits into any reserve funds required by the applicable management agreement. In the event of a bankruptcy or insolvency involving a hotel management company, there is a risk that the payment of operating and other expenses for the relevant hotel and payment of revenues to us may be delayed or otherwise impaired. The bankruptcy or insolvency of a hotel management company may significantly impair its ability to provide services required under the management agreement.

Certain of the employees at our hotels are covered by collective bargaining agreements and labor disputes may disrupt operations or increase costs at our hotels.

Our hotel management companies act as employer of the hotel level employees. At certain of our hotels, these employees are covered by collective bargaining agreements. At the current time, the collective bargaining agreements at our Loews Santa Monica hotel and Fairmont Chicago hotel have expired. At this time, we cannot predict when or whether new agreements will be reached in these markets and what the impact of prolonged negotiations could be. If agreements are reached, the agreements may cause us to incur additional expenses related to our employees, thereby reducing our profits and impacting our financial results negatively. Additionally, if agreements are not reached and there are labor disputes, including strikes, operations at our hotels could suffer due to the diversion of business to other hotels or increased costs of operating the hotel during such a labor dispute, thereby impacting our financial results negatively.

The outbreak of a pandemic disease, such as the H1N1 virus, has had and may in the future have an adverse impact on our financial results.

An outbreak of a pandemic disease, such as the H1N1 virus, has had and may in the future have a significant adverse impact on travel and the lodging industry. As a consequence, our financial results of operations may be adversely effected.

Our renovation and development activities are subject to timing, budgeting and other risks.

We are in the process of renovating several of our properties and expect to continue similar activities in the future, as well as develop and redevelop certain properties. These renovation, development, and redevelopment activities and the pursuit of acquisition and other corporate opportunities expose us to certain risks, including those relating to:

construction delays or cost overruns that may increase project costs and, as a result, make the project uneconomical;

defects in design or construction that may result in additional costs to remedy or require all or a portion of a property to be closed during the period required to rectify any such situation;

the failure to complete construction of a property on schedule;

insufficient occupancy rates at a completed project impeding our ability to pay operating expenses or achieve targeted rates of return on investment;

the incurrence of acquisition and/or predevelopment costs in connection with projects that are delayed or not pursued to completion;

natural disasters such as earthquakes, hurricanes, floods or fires that could adversely impact a project;

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receipt of zoning, occupancy, building, land-use or other required governmental permits and authorizations; and

governmental restrictions on the nature or size of a project or timing of completion.

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In the case of an unsuccessful project, we may be required to write off capitalized costs associated with the project and such write-offs may be significant and adversely affect our financial condition and results of operations.

We face competition for the acquisition of real estate properties.

We compete with institutional pension funds, private equity investors, other REITs, owner-operators of hotels and others who are engaged in real estate investment activities that focus on the acquisition of hotels. These competitors may drive up the price we must pay for real estate property, other assets or other companies we seek to acquire or may succeed in acquiring those real estate properties, other assets or other companies themselves. In addition, our potential acquisition targets may find our competitors to be more attractive suitors because they may have greater resources, may be willing to pay more or may have a more compatible operating philosophy. In addition, the number of entities competing for suitable investment properties may increase in the future. This would result in increased demand for these real estate properties, other assets or other companies and therefore increase the prices required to be paid for them. If we pay higher prices for real estate properties, other assets or other companies, our profitability may be reduced. Also, future acquisitions of real property, other assets or other companies may not yield the returns we expect and, if financed using our equity, may result in stockholder dilution. We also may not be successful in identifying or consummating acquisitions and investments in unconsolidated affiliates on satisfactory terms. In addition, our profitability may suffer because of acquisition-related costs or amortization costs for intangible assets. We also may incur significant expenses in connection with acquisition or other corporate opportunities we pursue but do not consummate.

Investing through partnerships or unconsolidated affiliates decreases our ability to manage risk.

In addition to acquiring or developing hotels and resorts directly, we have from time to time invested, and expect to continue to invest in hotels and ancillary businesses, as a partner. Partners in unconsolidated affiliates often have shared control over the operation of the assets. Therefore, investments in unconsolidated affiliates may involve risks such as the possibility that the partner in an investment might become bankrupt or not have the financial resources to meet its obligations, or have economic or business interests or goals that are inconsistent with our business interests or goals, or be in a position to take action contrary to our instructions or requests or contrary to our policies or objectives. Consequently, actions by a partner might subject hotels, resorts and businesses owned by the unconsolidated affiliate to additional risk. We may be unable to take action without the approval of our partners in the unconsolidated affiliate, and alternatively, our partners in the unconsolidated affiliate could take actions binding on the unconsolidated affiliate without our consent. Additionally, should a partner in the unconsolidated affiliate become bankrupt, we could become liable for our partner's share of the unconsolidated affiliate's liabilities.

Our business and operations would suffer in the event of system failures.

Despite system redundancy, the implementation of security measures and the existence of a disaster recovery plan for our internal information technology systems, our systems are vulnerable to damages from any number of sources, including computer viruses, unauthorized access, energy blackouts, natural disasters, terrorism, war and telecommunication failures. Any system failure or accident that causes interruptions in our operations could result in a material disruption to our business. We may also incur additional costs to remedy damages caused by such disruptions.

Risks related to the lodging and real estate industries

A number of factors, many of which are common to the lodging industry and beyond our control, could affect our business, including those described elsewhere herein as well as the following:

increased competition from new supply or existing hotel properties in our markets, which would likely adversely affect occupancy and revenues at our hotels;

dependence on business, commercial and leisure travelers and tourism;

dependence on group and meeting/conference business;

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increases in energy costs, airline bankruptcies, airline strikes or other factors that may affect travel patterns and reduce the number of business and commercial travelers and tourists;

risks generally associated with the ownership of hotel properties and real estate, as we discuss in more detail below;

general economic and business conditions affecting the lodging and travel industry, both nationally and locally, including a prolonged U.S. recession;

increases in operating costs due to inflation, labor costs (including the impact of unionization), workers' compensation and health-care related costs, utility costs, insurance and unanticipated costs such as acts of nature and their consequences and other factors that may not be offset by increased room rates;

changes in governmental laws and regulations, fiscal policies and zoning ordinances and the related costs of compliance with laws and regulations, fiscal policies and ordinances; and

adverse effects of international market conditions, which may diminish the desire for leisure travel or the need for business travel, as well as national, regional and local economic and market conditions in which our hotels operate and where our customers live.

These factors could have an adverse effect on our financial condition and results of operations, which may affect our ability to make distributions to our stockholders.

Uninsured and underinsured losses could adversely affect our financial condition and results of operations, which may affect our ability to make distributions to our stockholders.

Various types of catastrophic losses, such as losses due to wars, terrorist acts, earthquakes, floods, hurricanes or pollution or other environmental matters generally are either uninsurable or not economically insurable, or may be subject to insurance coverage limitations, such as large deductibles or co-payments. Although our earthquake insurance coverage is limited, as of February 22, 2012, seven of our hotels were located in California, which has been historically at a greater risk for certain acts of nature (such as fire, floods and earthquakes) than other states. Our InterContinental Miami and Four Seasons Punta Mita Resort are located in areas that are prone to hurricanes and/or floods.

In the event of a catastrophic loss, our insurance coverage may not be sufficient to cover the full current market value or replacement cost of our lost investment. Should an uninsured loss or a loss in excess of insured limits occur, we could lose all or a portion of the capital we have invested in a property, as well as the anticipated future revenue from the property. In that event, we might nevertheless remain obligated for any mortgage debt or other financial obligations related to the property. In the event of a significant loss that is covered by insurance, our deductible may be high and, as a consequence, it could materially adversely affect our financial condition. Inflation, changes in building codes and ordinances, environmental considerations and other factors might also keep us from using insurance proceeds to replace or renovate a hotel after it has been damaged or destroyed. Under those circumstances, the insurance proceeds we receive might be inadequate to restore our economic position in the damaged or destroyed property.

Certain events, such as Hurricanes Katrina and Rita in 2005, have historically made it more difficult and expensive to obtain property and casualty insurance, including coverage for windstorm, flood and earthquake damage, and such events could occur again. We may encounter difficulty in obtaining or renewing property insurance, including coverage for windstorm, flood and earthquake damage, or casualty insurance on our properties at the same levels of coverage, under similar terms and in a timely manner due to a lack of capacity in the insurance markets or a lack of availability of such insurance at commercially reasonable rates. Insurance we would be able to obtain may be more limited and for some catastrophic risks (e.g., earthquake, flood, windstorm and terrorism) may not be generally available to fully cover potential losses. Even if we would be able to obtain new policies with desired levels and with limitations, we cannot be sure that we would be able to obtain such

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insurance at premium rates that are commercially reasonable or that there would not be gaps in our coverage. If we did not obtain adequate insurance on our properties for certain risks or in a timely manner, it would expose us to uninsured losses and could cause us to be in default under specific covenants on certain of our indebtedness or other contractual commitments which require us to maintain adequate insurance on our properties to protect against the risk of loss. If this were to occur, or if we were unable to obtain adequate insurance and our properties experienced damage which would otherwise have been covered by insurance, it could materially adversely affect our financial condition and the operations of our properties.

We obtain terrorism insurance to cover any property damage caused by any terrorism act under a separate stand-alone policy of insurance, and also have terrorism insurance under our general liability program and in our program for directors and officers coverage. We may not be able to recover fully under our existing terrorism insurance for losses caused by some types of terrorist acts, and federal terrorism legislation does not ensure that we will be able to obtain terrorism insurance in adequate amounts or at acceptable premium levels in the future. Insurers only have to provide terrorism coverage to the extent mandated by the Terrorism Risk Insurance Program Reauthorization Act (TRIPRA) effective December 26, 2007. While TRIPRA will reimburse insurers for losses resulting from nuclear, radiological, biological and chemical perils, TRIPRA does not require insurers to offer coverage for these perils and, to date, insurers are not willing to provide this coverage, even with government reinsurance. Any damage related to war and to nuclear, biological and chemical incidents, therefore, is excluded under our policies. TRIPRA is due to expire on December 31, 2014. There is no guaranty that terrorism insurance will be readily available or affordable before or after expiration of the TRIPRA in December 2014 or that TRIPRA will not be modified or repealed. As a result of the above, there remains uncertainty regarding the extent and adequacy of terrorism coverage that will be available to protect our interests in the event of future terrorist attacks that impact our properties.

We derive revenues from outside the United States, which subjects us to different legal, monetary and political risks, as well as currency exchange risks, and may cause unpredictability in our cash flows.

A portion of our investments are in hotel properties located outside the United States. International investments and operations generally are subject to various political and other risks that are different from and in addition to those for U.S. investments and operations, including:

enactment of laws prohibiting or restricting the foreign ownership of property;

laws restricting us from removing profits earned from activities within the country to the United States (i.e., nationalization of assets located within a country);

changes in laws, regulations and policies, including land use, zoning and environmental laws, and in real estate and other tax rates;

exchange rate fluctuations;

change in the availability, cost and terms of mortgage funds resulting from varying national economic policies or changes in interest rates;

high administrative costs; and

terrorism, war or civil unrest.

Unfavorable legal, regulatory, economic or political changes such as those described above could adversely affect our financial condition and results of operations.

The threat of terrorism has historically adversely affected the lodging industry generally and these adverse effects may worsen if there are further terrorist events.

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The threat of terrorism has historically caused a significant decrease in hotel occupancy and average daily rates due to disruptions in business and leisure travel patterns and concerns about travel safety. Future terrorist acts, terrorism alerts or outbreaks of hostilities could have a negative effect on travel and on our business.

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Seasonal variations in revenue at our hotels can be expected to cause quarterly fluctuations in our revenues.

Revenues for hotels in tourist areas generally are substantially greater during tourist season than other times of the year. To the extent that cash flows from operations are insufficient during any quarter, due to seasonal fluctuations in revenues, we may have to enter into short-term borrowings to fund operations, pay interest expense or make distributions to our stockholders.

We consider acquisition opportunities in the ordinary course of our business; we face competition in the acquisition of properties and properties that we acquire may not perform as anticipated.

In the ordinary course of our business and when our liquidity position permits, we consider strategic acquisitions. The acquisition of properties involves risks, including the risk that the acquired property will not perform as anticipated and the risk that any actual costs for rehabilitating, repositioning, renovating and improving identified in the pre-acquisition process will exceed estimates. There is, and it is expected that there will continue to be, significant competition for acquisitions that meet our investment criteria as well as risks associated with obtaining financing for acquisition activities.

Environmental and other governmental laws and regulations could increase our compliance costs and liabilities and adversely affect our financial condition and results of operations.

Our hotel properties are subject to various U.S. federal, state and local environmental laws. Under these laws, courts and government agencies have the authority to require us, as owner of a contaminated property, to clean up the property, even if the contamination pre-dated our ownership of the property or we did not know of or were not responsible for the contamination. These laws may also force a party who owned a property at the time of its contamination, but no longer owns the property, to be responsible for the cleanup. In addition to the costs of clean-up, environmental contamination can affect the value of a property and, therefore, an owner's ability to borrow funds using the property as collateral or to sell the property. These laws can also impose liability on parties that arrange for the disposal of wastes at an offsite property that becomes contaminated.

In addition, some of these environmental laws can restrict the use of a property and place conditions on various activities. An example would be laws that require a business using hazardous substances on a property (such as swimming pool and lawn care chemicals) to manage them carefully and to notify local officials that the chemicals are being used. Failure to comply with these laws could result in fines and penalties or expose us to third-party liability.

From time to time, the United States Environmental Protection Agency (EPA) designates certain sites affected by hazardous substances as Superfund sites. Superfund sites can cover large areas, affecting many different parcels of land. The EPA may choose to pursue parties regardless of their actual contribution to the contamination. The Hilton Burbank Airport and Convention Center, which we sold in September 2006, is located within a Federal Superfund site. The area was designated as a Superfund site because groundwater underneath the area is contaminated. We have not been named, and do not expect to be named, as a party responsible for the clean-up of the groundwater contamination; however, there can be no assurance regarding potential future developments concerning this site.

The presence of any environmental conditions at our properties could result in remediation and other costs and liabilities and adversely affect our financial condition and results of operations.

We have reviewed environmental reports prepared by our consultants and consultants retained by our lenders at various times, which disclose certain conditions on our properties and the use of hazardous substances in operation and maintenance activities that could pose a risk of environmental contamination or impose liability on us. At some facilities these include on-site dry cleaning operations, petroleum storage in underground storage tanks, past tank removals and the known or suspected presence of asbestos, mold or thorium.

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The costs to clean up a contaminated property or defend against a related claim or to comply with environmental laws could be material and could adversely affect the funds available for distributions to our stockholders. Future laws or regulations may impose material environmental liabilities on us, the current environmental condition of our hotel properties may be affected by the condition of the properties in the vicinity of our hotel properties (such as the presence of leaking underground storage tanks) or by third parties unrelated to us and currently unknown environmental liabilities related to our hotel properties may be identified.

If we are not in compliance with the Americans with Disabilities Act of 1990, we may face significant costs to modify our properties and/or be subject to fines.

Under the Americans with Disabilities Act of 1990 (ADA), all public accommodations must meet various federal requirements related to access and use by disabled persons. Compliance with the ADA's requirements could require removal of access barriers, and non-compliance could result in the U.S. government imposing fines or in private litigants winning damages. If we are required to make substantial modifications to our hotels, whether to comply with the ADA or other changes in governmental rules and regulations, our financial condition, results of operations and ability to make distributions to our stockholders could be adversely affected. One of our subsidiaries is currently defending two lawsuits related to the access and use by disabled persons at the Ritz-Carlton Half Moon Bay. We can make no assurance about the outcome of these lawsuits.

Risks related to our organization and structure

Provisions of our organizational documents may limit the ability of a third party to acquire control of our company and may depress our stock price.

In order for us to maintain our status as a REIT, no more than 50% of the value of outstanding shares of our stock may be owned, actually or constructively, by five or fewer individuals at any time during the last half of each taxable year. To make sure that we will not fail to qualify as a REIT under this test, subject to some exceptions, our charter prohibits any individual from owning beneficially or constructively more than 9.8% of the value of outstanding shares of our stock or more than 9.8% of the value or number of shares, whichever is more restrictive, of the outstanding shares of our common stock. Any attempt to own or transfer shares of our capital stock in excess of the ownership limit without the consent of our board of directors will be void, and could result in the shares being automatically transferred to a charitable trust. This ownership limitation may prevent an acquisition of control of our company by a third party without our board of directors' grant of an exemption from the ownership limitation, even if our stockholders believe the change of control is in their interest.

Our charter authorizes our board of directors to cause us to issue up to 250,000,000 shares of common stock and up to 150,000,000 shares of preferred stock. Additionally, our charter authorizes our board of directors to amend our charter without stockholder approval to increase or decrease the aggregate number of shares of stock or the number of shares of any class or series of our stock that we have authority to issue, to classify or reclassify any unissued shares of common stock or preferred stock and to set the preferences, rights and other terms of the classified or reclassified shares. Issuances of additional shares of stock may have the effect of delaying or preventing a change in control of our company, including transactions at a premium over the market price of our stock, even if stockholders believe that a change of control is in their interest.

Our charter permits the removal of a director only upon the affirmative vote of two-thirds of the votes entitled to be cast, generally in the election of directors, and provides that vacancies may only be filled by a majority of the remaining directors. Our bylaws require advance notice of a stockholder's intention to nominate directors or present business for consideration by stockholders at an annual meeting of our stockholders. These provisions may delay, defer or prevent a transaction or change in control that involves a premium price for our common stock or that for other reasons may be desired by our stockholders.

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Provisions of Maryland law and our shareholder rights plan may limit the ability of a third party to acquire control of our company.

Certain provisions of the MGCL may have the effect of inhibiting a third party from making a proposal to acquire us or of impeding a change of control under circumstances that otherwise could provide the holders of shares of our common stock with the opportunity to realize a premium over the then prevailing market price of such shares, including:

business combination provisions that, subject to limitations, prohibit certain business combinations between us and an interested stockholder (defined generally as any person who beneficially owns 10% or more of the voting power of our shares or an affiliate thereof) for five years after the most recent date on which the stockholder becomes an interested stockholder, and thereafter imposes special super majority stockholder voting requirements on these combinations;

control share provisions that provide that control shares of our company (defined as shares which, when aggregated with other shares controlled by the stockholder, entitle the stockholder to exercise one of three increasing ranges of voting power in electing directors) acquired in a control share acquisition (defined as the direct or indirect acquisition of ownership or control of control shares) have no voting rights except to the extent approved by our stockholders by the affirmative vote of at least two-thirds of all the votes entitled to be cast on the matter, excluding all interested shares; and

unsolicited takeover provisions of Maryland law permit our board of directors, without stockholder approval, to implement a classified board as well as impose other restrictions on the ability of a third party to acquire control.

We have opted out of the control share provisions of the MGCL pursuant to a provision in our bylaws. However, we may, by amendment to our bylaws, become subject to the control share provisions of the MGCL in the future.

On November 24, 2009, we also extended a shareholder rights plan, commonly known as a poison pill anti-takeover device, through November 30, 2012 to deter hostile or coercive attempts to acquire us. Under the plan, if any person or group acquires more than 20% of our common stock without approval of the board of directors under specified circumstances, our other stockholders have the right to purchase shares of our common stock, or shares of the acquiring company, at a substantial discount to the public market price. This plan makes an acquisition not approved by our board of directors much more costly to a potential acquirer, which may deter a potential acquisition.

You have limited control as a stockholder regarding any changes we make to our policies.

Our board of directors approves our major policies, including our investment objectives, financing, growth and distributions. Our board of directors may amend or revise these and other policies without a vote of our stockholders. This means that our stockholders will have limited control over changes in our policies.

Tax risks

If we fail to maintain our status as a REIT, our distributions will not be deductible by us, and our income will be subject to U.S. federal taxation, reducing our earnings available for distribution.

We currently qualify as a REIT under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended, which we refer to herein as the Tax Code. The requirements for this qualification, however, are complex and require annual distributions to our stockholders tied to our taxable income (irrespective of available cash from operations), quarterly asset tests and diversity of stock ownership rules. If we fail to meet these requirements in the future, our distributions to our stockholders will not be deductible by us and we will have to pay a corporate U.S. federal level tax on our income. This would substantially reduce our cash available to pay distributions to our stockholders. In addition, such a tax liability might cause us to borrow funds, liquidate some

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of our investments or take other steps, which could negatively affect our results of operations. Moreover, if our REIT status is terminated because of our failure to meet a technical REIT requirement or if we voluntarily revoke our election, we would be disqualified from electing treatment as a REIT for the four taxable years following the year in which REIT status is lost.

Even if we maintain our status as a REIT, we may become subject to U.S. federal, state, local or foreign taxes on our income or property reducing our earnings available for distribution.

Even if we maintain our status as a REIT, we may become subject to U.S. federal income and other taxes and state and local taxes. For example, if we have net income from a prohibited transaction, that income will be subject to a 100% tax. A prohibited transaction is, in general, the sale or other disposition of inventory or property, other than foreclosure property, held primarily for sale to customers in the ordinary course of business. We may not be able to make sufficient distributions to avoid excise taxes applicable to REITs. We may also decide to retain income we earn from the sale or other disposition of our property and pay U.S. federal income tax directly on that income. In that event, our stockholders would be treated as if they earned that income and paid the tax on it directly. However, stockholders that are tax-exempt, such as charities or qualified pension plans, would have no benefit from their deemed payment of that tax liability. In addition, the REIT rules impose various taxes and penalties on transactions with taxable REIT subsidiaries that are determined not to be priced at an arm's length, and on a REIT that has to avail itself of certain cure provisions in the Tax Code for the failure to meet all of the REIT qualification requirements. We cannot assure you that we will be able to continue to satisfy the REIT requirements, or that it will be in our best interests to continue to do so.

We may also be subject to state and local taxes on our income or property, either directly or at the level of our operating partnerships or at the level of the other companies through which we indirectly own our assets.

Foreign countries impose taxes on our hotels and our operations within their jurisdictions. We may not fully benefit from a foreign tax credit against our U.S. federal income tax liability for the foreign taxes we pay. As a result, our foreign taxes may reduce our income and available cash flow from our foreign hotels, which, in turn, could reduce our ability to make distributions to our stockholders.

Certain of our entities, including our foreign entities, are subject to corporate income taxes. Consequently, these entities are subject to potential audit. There can be no assurance that certain tax positions the entities have taken will not be challenged by taxing authorities and if the challenge is successful, could result in increased tax expense, which could be material.

If the leases of our hotels to our taxable REIT subsidiaries, or Affiliate Leases, are not respected as true leases for federal income tax purposes, we would fail to maintain our status as a REIT.

To continue to qualify as a REIT, we must satisfy two gross income tests under which specified percentages of our gross income must be certain types of passive income, such as rent. The rent paid pursuant to our Affiliate Leases will only qualify for purposes of the gross income tests if such Affiliate Leases are respected as true leases for U.S. federal income tax purposes and are not treated as service contracts, transfers between unconsolidated affiliates or some other type of arrangement. If our Affiliate Leases are not respected as true leases for U.S. federal income tax purposes, we would fail to qualify as a REIT.

Our taxable REIT subsidiaries, or TRSs, are subject to special rules that may result in increased taxes.

The REIT has to pay a 100% penalty tax on certain payments that it receives if the economic arrangements between the REIT and the TRS are not comparable to similar arrangements between unrelated parties. The Internal Revenue Service may successfully assert that the economic arrangements of any of our inter-company transactions, including our Affiliate Leases, are not comparable to similar arrangements between unrelated parties.

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We may be required to pay a penalty tax upon the sale of a hotel.

The U.S. federal income tax provisions applicable to REITs provide that any gain realized by a REIT on the sale of property held as inventory or other property held primarily for sale to customers in the ordinary course of business is treated as income from a prohibited transaction that is subject to a 100% penalty tax. Under current laws, unless a sale of real property qualifies for a safe harbor, the question of whether the sale of a hotel (or other property) constitutes the sale of property held primarily for sale to customers is generally a question of the facts and circumstances regarding a particular transaction. We may make sales that do not satisfy the requirements of the safe harbors or the Internal Revenue Service may successfully assert that one or more of our sales are prohibited transactions; consequently, we may be required to pay a penalty tax if we have gains on any such transactions.

Dividends payable by REITs do not qualify for the reduced tax rates applicable to certain dividends.

The maximum federal tax rate for certain dividends payable to domestic stockholders that are individuals, trusts and estates is 15% (through 2012 under current law). Dividends payable by REITs, however, are generally not eligible for this reduced rate. Although this legislation does not adversely affect the taxation of REITs or dividends paid by REITs, the more favorable rates applicable to regular qualified corporate dividends could cause investors who are individuals, trusts and estates to perceive investments in REITs to be relatively less competitive than investments in stock of non-REIT corporations that pay dividends, which could adversely affect the comparative value of the stock of REITs, including our common stock.

We may pay required dividends in the form of common stock.

We are required to distribute 90% of our annual REIT taxable income in order to maintain our REIT status. Under guidelines published by the Internal Revenue Service, REITs are allowed to declare dividends in 2012 (that otherwise comply with the REIT distribution timing requirements) payable in the form of additional shares of common stock to satisfy up to 90% of the required REIT dividends amount applicable with respect to the 2011 taxable year. The amount of the dividend would be taxable to shareholders (to the extent the dividend is from earnings and profits), including the value of our stock received, not just the portion of the dividend paid in cash. We expect that, as we continue to undertake efforts to conserve cash and enhance our liquidity, future required dividends on our common stock, if any, may be paid in common stock to the fullest extent permitted under law. There can be no assurance as to when we will resume the payment of dividends on common stock or to pay any such dividends completely or substantially in cash.

Complying with REIT requirements may cause us to forego otherwise attractive opportunities.

To remain qualified as a REIT for federal income tax purposes, we must continually satisfy requirements and tests under the tax law concerning, among other things, the sources of our income, the nature and diversification of our assets, the amounts we distribute to our stockholders and the ownership of our stock. In order to meet these tests, we may be required to forego or limit attractive business or investment opportunities. For example, we may not lease to our TRS any hotel where gaming or wagering activities are conducted. Therefore, compliance with the REIT requirements may hinder our ability to operate solely to maximize profits.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

Offices. We lease our headquarters located at 200 West Madison Street, Suite 1700, Chicago, Illinois 60606.

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Property Overview and Performance. The following table presents certain information related to our hotel properties. All of the hotel properties in the following table relate to our one reportable business segment, hotel ownership.

Hotel	Location	Date Acquired	Year Ended December 31, 2011(1)				% Change 2011		2010(2)
			Number of Rooms	Average Occupancy	Average Daily Rate	RevPAR	Total RevPAR	RevPAR	Total RevPAR
Fee Simple Property Interest									
Westin St. Francis(*)	San Francisco, CA	6/2006	1,195	82.6%	\$ 213.32	\$ 176.28	\$ 295.52	20.2%	19.4%
InterContinental Chicago(*)	Chicago, IL	4/2005	792	76.5%	\$ 186.26	\$ 142.47	\$ 233.63	9.0%	7.6%
Hotel del Coronado(3)	Coronado, CA	1/2006	757	67.1%	\$ 358.33	\$ 240.60	\$ 494.84	7.9%	6.9%
Fairmont Chicago(*)	Chicago, IL	9/2005	687	66.4%	\$ 212.06	\$ 140.87	\$ 236.37	14.4%	12.0%
Fairmont Scottsdale Princess(4)	Scottsdale, AZ	9/2006	649	65.3%	\$ 215.39	\$ 140.57	\$ 309.20	10.0%	5.1%
InterContinental Miami(*)	Miami, FL	4/2005	641	70.5%	\$ 162.79	\$ 114.72	\$ 202.72	5.6%	3.7%
Hyatt Regency La Jolla(5)(*)	La Jolla, CA	7/1999	419	72.9%	\$ 158.68	\$ 115.62	\$ 215.76	12.4%	11.4%
Ritz-Carlton Laguna Niguel(6)	Dana Point, CA	7/2006	396	60.8%	\$ 339.83	\$ 206.73	\$ 447.34	18.0%	19.2%
Loews Santa Monica Beach Hotel(*)	Santa Monica, CA	3/1998	342	86.6%	\$ 298.57	\$ 258.50	\$ 385.64	9.4%	7.8%
Ritz-Carlton Half Moon Bay(6)	Half Moon Bay, CA	8/2004	261	67.7%	\$ 358.94	\$ 243.06	\$ 584.33	11.4%	7.6%
Four Seasons Washington, D.C.(*)	Washington, D.C.	3/2006	222	71.5%	\$ 530.23	\$ 378.97	\$ 761.89	3.9%	5.7%
Four Seasons Silicon Valley	East Palo Alto, CA	3/2011	200	69.5%	\$ 297.94	\$ 207.07	\$ 395.58	13.3%	13.9%
Four Seasons Punta Mita Resort(6)	Punta Mita, Mexico	2/2001	173	44.8%	\$ 645.00	\$ 289.13	\$ 535.15	(11.7)%	(13.2)%
Four Seasons Jackson Hole	Teton Village, WY	3/2011	124	52.6%	\$ 523.32	\$ 275.11	\$ 631.91	8.8%	4.9%
Ground Lease Property Interest									
Marriott Lincolnshire Resort(6)	Lincolnshire, IL	9/1997	389	52.1%	\$ 124.11	\$ 64.61	\$ 230.02	16.5%	8.0%
Marriott London Grosvenor Square(*)	London, England	8/2006	237	81.1%	\$ 377.05	\$ 305.88	\$ 422.10	6.6%	5.9%
Leasehold Property Interest									
Marriott Hamburg(7)	Hamburg, Germany	6/2000	278	82.3%	\$ 199.17	\$ 163.84	\$ 230.88	11.7%	11.9%
Total			7,762	71.1%	\$ 253.39	\$ 180.25	\$ 337.75	10.3%	8.7%

- (1) The table includes statistical information only for our period of ownership.
- (2) The year-over-year comparisons are calculated using full year results which may include prior ownership periods.
- (3) We indirectly have a 34.3% interest in the unconsolidated affiliate that owns this property, which is subject to a mortgage. See Item 8. Financial Statements and Supplementary Data 6. Investment in Unconsolidated Affiliates for further detail.
- (4) We indirectly have a 50.0% interest in the unconsolidated affiliate that owns this property, which is subject to a mortgage. The unconsolidated affiliate has a ground lease interest in one land parcel at this property. See Item 8. Financial Statements and Supplementary Data 6. Investment in Unconsolidated Affiliates for further detail.
- (5) We own a 53.5% controlling interest in an affiliate that owns this property. See Item 8. Financial Statements and Supplementary Data 10. Equity and Distribution Activity for further detail.
- (6) These properties are borrowing base assets under our bank credit facility, which are subject to mortgages.

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- (7) This property was originally acquired on the date indicated in the table but was subsequently sold to a third party and leased back to us in a transaction that is more fully described under Item 8. Financial Statements and Supplementary Data 8. Operating Lease Agreements.

- (*) These properties are subject to mortgages as more fully described under Item 8. Financial Statements and Supplementary Data 9. Indebtedness.

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Principal Terms of Management Agreements. Of our hotel properties, 16 are subject to management agreements with third party hotel managers and one is subject to a lease agreement with a third party hotel manager. For the management agreements, the principal terms are described below:

Base Management Fees. Our agreements generally provide for the payment of base management fees between 1.0% and 4.0% of the applicable hotel's revenues, as determined in the agreements.

Incentive Management Fees. Our agreements generally provide the opportunity for the hotel manager to earn incentive management fees, which are typically a percentage of a hotel's profit for the year. In certain instances, a level of return to us or performance of the hotel is required before a hotel manager is entitled to an incentive fee. Additionally, notwithstanding the specific formulas for the incentive fee calculations in the agreements, in certain instances, the incentive management fee to be earned by the hotel manager is capped.

Terms. As of December 31, 2011, the remaining terms of the management agreements, not including renewal options, range from three to 25 years and average 13 years. Generally, we do not have the right to exercise renewal options for the agreements. Instead, the term of an agreement either renews automatically, unless the hotel manager provides notice of termination, or is otherwise renewable within the discretion of the hotel manager.

Services. The agreements require the hotel managers to furnish the hotels with certain services, which include on-site management and may include central training, advertising and promotion, national reservations systems, payroll and accounting services and such additional services as needed. We are responsible for payment of the operating expenses related to the hotel.

Annual Budget. The agreements require the hotel manager to prepare and implement annual budgets, subject to our review and approval.

Ability to Terminate. The agreements generally are not subject to early termination by us unless certain conditions exist, including the failure of the hotel manager to satisfy yearly performance-related criteria in 13 of our agreements.

Working Capital. Our agreements typically require us to maintain working capital for the related hotel. We are also responsible for providing funds to meet the cash needs for the hotel operations if at any time the funds available from the hotel operations are insufficient to meet the financial requirements of the hotel.

Furniture, Fixtures and Equipment Reserves. We are required to provide to the hotel manager all of the necessary furniture, fixtures and equipment for the operations of the hotel. Our agreements generally provide that between 4.0% and 5.0% of revenues of the hotel be reserved by the manager or deposited into a separate account held by us each year.

Sale of Hotel. Generally, our agreements limit our ability to sell, lease or otherwise transfer each hotel unless the transferee is not a competitor of the manager, assumes the management agreement, and meets other specified conditions.

Mortgage Debt Pertaining to Our Properties. For information relating to the mortgage debt pertaining to our properties, refer to Item 8. Financial Statements and Supplementary Data 9. Indebtedness - Mortgages and Other Debt Payable.

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ITEM 3. LEGAL PROCEEDINGS.

We are not involved in any material litigation, and, to our knowledge, there is no material litigation threatened against us, other than routine litigation arising in the ordinary course of business or which is expected to be covered by insurance.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

Table of Contents**PART II****ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.**

Our common stock is listed and traded on the New York Stock Exchange (NYSE) under the symbol BEE. As of February 22, 2012, the number of registered holders of record of our common stock was 76.

The following table sets forth the high and low sale prices for our common stock as reported on the NYSE composite transaction tape and the per share cash dividends declared on our common stock for the period January 1, 2010 through December 31, 2011.

	2011 Per Share of Common Stock			2010 Per Share of Common Stock		
	Market Price		Dividend	Market Price		Dividend
	High	Low	Paid	High	Low	Paid
First Quarter	\$ 6.92	\$ 5.23	\$ 0.00	\$ 4.82	\$ 1.84	\$ 0.00
Second Quarter	7.14	5.93	0.00	6.97	3.82	0.00
Third Quarter	7.62	4.05	0.00	4.78	3.33	0.00
Fourth Quarter	5.84	3.76	0.00	5.33	4.16	0.00
Year	\$ 7.62	\$ 3.76	\$ 0.00	\$ 6.97	\$ 1.84	\$ 0.00

We generally intend to distribute each year substantially all of our taxable income (which does not necessarily equal net income as calculated in accordance with generally accepted accounting principles) to our shareholders to comply with REIT provisions of the Tax Code. If necessary for REIT qualification purposes, we may need to distribute any taxable income in cash or by a special dividend. Our dividend policy is subject to revision at the discretion of our board of directors. All distributions will be made at the discretion of our board of directors and will depend on our taxable income, our financial condition, our maintenance of REIT status and other factors as our board of directors deems relevant.

On November 4, 2008, our board of directors elected to suspend the quarterly dividend to holders of shares of common stock, and, in February 2009, our board of directors elected to suspend the quarterly dividend to holders of shares of our Preferred Stock. In the fourth quarter of 2011, our board of directors authorized, and we declared, the payment of the Unpaid Dividends, and a sum sufficient for the payment of the Unpaid Dividends has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. However, the Unpaid Dividends are not payable until June 29, 2012, are payable to holders of record as of the close of business on June 15, 2012 and are contingent upon our ability to meet, on the June 29, 2012 Unpaid Dividends payment date, the Maryland Dividend Requirement. In addition, in February 2012, our board of directors authorized, and we declared, preferred dividends for the quarter ending March 31, 2012, payable on June 29, 2012, to holders of record as of the close of business on June 15, 2012, contingent upon our ability to meet the Maryland Dividend Requirement on such payment date. A sum sufficient for the payment of the preferred dividends for the quarter ending March 31, 2012 has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. Our board of directors has continued the suspension of the quarterly dividend to holders of shares of our common stock as a measure to preserve liquidity due to the uncertainty in the economic environment and no projected taxable distribution requirement. Based on our current forecasts, we would not be required to make any distributions during 2012 in order to maintain our REIT status. Our board of directors will continue to evaluate the dividend policy in light of the REIT provisions of the Tax Code, restrictions under the bank credit facility, and the overall economic climate.

For a description of restrictions on the payment of dividends, see Item 8. Financial Statements and Supplementary Data 9. Indebtedness Bank Credit Facility.

Table of Contents**Equity Compensation Plan Information**

There are 9,700,000 shares of common stock authorized for issuance under our Second Amended and Restated 2004 Incentive Plan (the Amended and Restated Plan). As of December 31, 2011, there have been 1,409,531 securities issued into common stock. The following table sets forth certain information with respect to securities authorized and available for issuance under the Amended and Restated Plan as of December 31, 2011.

	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under the Amended and Restated Plan (excluding securities reflected in column a) (c)
Equity compensation plans approved by security holders:			5,784,631
Stock options	669,797	\$ 20.40	
Restricted stock units	1,836,041	N/A	
Equity compensation plans not approved by security holders:		N/A	
Total	2,505,838		5,784,631

Repurchases of Equity Securities

In December 2011, we settled tender offers to purchase up to an aggregate of 4,716,981 shares of our issued and outstanding (i) 8.25% Series C Cumulative Redeemable Preferred Stock, at a purchase price of \$26.50 per share, (ii) 8.25% Series B Cumulative Redeemable Preferred Stock, at a purchase price of \$26.50 per share, and (iii) 8.50% Series A Cumulative Redeemable Preferred Stock, at a purchase price of \$26.70 per share, in each case, net to the seller in cash, less any applicable withholding taxes and without interest or accrued and unpaid dividends. In the aggregate, we paid approximately \$86.1 million to acquire 1,922,273 shares of our 8.25% Series C Cumulative Redeemable Preferred Stock, 984,625 shares of our 8.25% Series B Cumulative Redeemable Preferred Stock and 340,609 shares of our 8.50% Series A Cumulative Redeemable Preferred Stock that were validly tendered and not withdrawn, for a total of 3,247,507 preferred shares validly tendered. The shares of Preferred Stock acquired by us were retired upon receipt. Accrued and unpaid dividends of \$10.9 million or \$5.67 per share of the acquired 8.25% Series C Cumulative Redeemable Preferred Stock were eliminated. Accrued and unpaid dividends of \$5.6 million or \$5.67 per share of the acquired 8.25% Series B Cumulative Redeemable Preferred Stock were eliminated. Accrued and unpaid dividends of \$2.0 million or \$5.84 per share of the acquired 8.50% Series A Cumulative Redeemable Preferred Stock were eliminated. As a result, total accrued and unpaid dividends of \$18.5 million across all three series were eliminated. After settlement of the tender offers, 3,827,727 shares of our 8.25% Series C Cumulative Redeemable Preferred Stock, 3,615,375 shares of our 8.25% Series B Cumulative Redeemable Preferred Stock and 4,148,141 shares of our 8.50% Series A Cumulative Redeemable Preferred Stock remain outstanding for trading on the NYSE.

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The table below provides information concerning our repurchase of shares of our equity securities during the quarter ended December 31, 2011.

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs (1)	Maximum number (or approximate dollar value) of shares that may yet be purchased under the plans or programs
October 1 – October 31, 2011				
November 1 – November 30, 2011				
December 1 – December 31, 2011				
8.25% Series C Cumulative Redeemable Preferred Stock	1,922,273	\$ 26.50	1,922,273	
8.25% Series B Cumulative Redeemable Preferred Stock	984,625	\$ 26.50	984,625	
8.50% Series A Cumulative Redeemable Preferred Stock	340,609	\$ 26.70	340,609	
Total	3,247,507	\$ 26.52	3,247,507	

- (1) On November 7, 2011, we announced the commencement of offers to purchase up to an aggregate of 4,716,981 shares of our issued and outstanding (i) 8.25% Series C Cumulative Redeemable Preferred Stock, at a purchase price of \$26.50 per share, (ii) 8.25% Series B Cumulative Redeemable Preferred Stock, at a purchase price of \$26.50 per share, and (iii) 8.50% Series A Cumulative Redeemable Preferred Stock, at a purchase price of \$26.70 per share, in each case, net to the seller in cash, less any applicable withholding taxes and without interest or accrued and unpaid dividends. The offers expired at 5:00 p.m., New York City time, on December 19, 2011.

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The following sets forth our selected consolidated financial and operating information on a historical basis. The following information should be read together with Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and notes thereto, which are included in Item 8. Financial Statements and Supplementary Data.

	Years Ended December 31,				
	2011(1)	2010(1)	2009(1)	2008(1)(2)	2007(1)(2)
	(In thousands, except per share data)				
Operating Data:					
Revenue:					
Rooms	\$ 410,315	\$ 362,559	\$ 343,891	\$ 445,244	\$ 462,701
Food and beverage	267,194	238,762	216,982	293,344	306,805
Other hotel operating revenue	80,907	79,981	89,525	97,316	99,255
Lease revenue	5,422	4,991	4,858	5,387	5,118
Total revenues	763,838	686,293	655,256	841,291	873,879
Operating costs and expenses:					
Rooms	114,087	105,142	100,642	114,445	116,416
Food and beverage	192,028	171,279	160,252	202,641	207,961
Other departmental expenses	207,664	199,336	193,699	218,606	218,831
Management fees	24,719	22,911	23,386	32,336	34,219
Other hotel expenses	53,808	48,781	52,385	57,154	60,474
Lease expense	4,865	4,566	4,752	4,953	4,555
Depreciation and amortization	112,062	130,601	130,955	109,532	91,894
Impairment losses and other charges		141,858	99,740	277,917	7,372
Corporate expenses	39,856	34,692	23,910	24,800	28,307
Total operating costs and expenses	749,089	859,166	789,721	1,042,384	770,029
Operating income (loss)	14,749	(172,873)	(134,465)	(201,093)	103,850
Interest expense	(86,447)	(86,285)	(93,929)	(79,993)	(81,006)
Equity in (losses) earnings of unconsolidated affiliates	(9,215)	13,025	1,718	2,810	8,344
(Loss) income from continuing operations	(106,424)	(265,311)	(231,296)	(288,376)	104,055
Income (loss) from discontinued operations, net of tax	101,572	34,511	(15,137)	(29,110)	(35,284)
Net (loss) income	(4,852)	(230,800)	(246,433)	(317,486)	68,771
Net loss (income) attributable to the noncontrolling interests in SHR's operating partnership	29	1,687	3,129	4,065	(969)
Net income attributable to the noncontrolling interests in consolidated affiliates	(383)	(1,938)	(641)	(3,870)	(1,363)
Preferred shareholder dividends	(18,482)	(30,886)	(30,886)	(30,886)	(30,107)
Net (loss) income attributable to SHR common shareholders	(23,688)	(261,937)	(274,831)	(348,177)	36,332
(Loss) income from continuing operations attributable to SHR common shareholders per share - basic	(0.70)	(2.41)	(3.45)	(4.25)	0.94
Cash dividends declared per common share				0.72	0.96

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	2011(1)	As of the Years Ended December 31,			2007(1)(2)
		2010(1)	2009(1)	2008(1)(2)	
		(In thousands, except statistical data)			
Balance Sheet Data:					
Total assets	\$ 2,086,689	\$ 2,162,316	\$ 2,598,143	\$ 2,909,167	\$ 3,365,909
Long-term debt obligations	1,050,385	1,146,281	1,648,197	1,672,690	1,633,869
Total liabilities	1,419,686	1,511,922	2,003,258	2,093,095	2,069,071
Noncontrolling interests in SHR s operating partnership	4,583	5,050	2,717	5,330	16,326
Noncontrolling interests in consolidated affiliates	8,222	25,082	23,188	27,203	30,653
SHR s shareholders equity	654,198	620,262	568,980	783,539	1,249,859
Statistical Data:					
Number of hotels at the end of the year excluding unconsolidated affiliates	15	15	16	18	19
Number of rooms at the end of the year excluding unconsolidated affiliates	6,356	6,873	7,245	7,590	8,287
Average occupancy rate	72.2%	69.5%	66.8%	72.3%	76.0%

- (1) We sold one hotel property in 2011, one hotel property in 2010, two hotel properties in 2009, one hotel property in 2008, and one hotel property in 2007. The operations of these hotels are included as discontinued operations in the operating data above for all years presented.
- (2) The table presents certain selected historical financial data which has been updated to reflect the impact of the retrospective application of new accounting guidance related to noncontrolling interests and convertible debt instruments.

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ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The following discussion and analysis is based primarily on the consolidated financial statements of Strategic Hotels & Resorts, Inc. (SHR) and its subsidiaries for the years presented and should be read together with the notes thereto contained in this annual report on Form 10-K. Terms employed herein as defined terms, but without definition, have meanings set forth in the notes to the financial statements (see Item 8. Financial Statements and Supplementary Data).

Overview

We were incorporated in Maryland in January 2004 to acquire and asset-manage upper upscale and luxury hotels (as defined by Smith Travel Research). Our accounting predecessor, Strategic Hotel Capital, L.L.C. (SHC LLC) was founded in 1997 by Laurence Geller, our president and chief executive officer, Goldman, Sachs & Co.'s Whitehall Fund and others. We made an election to be taxed as a real estate investment trust (REIT) under the Sections 856 through 860 of the Internal Revenue Code of 1986, as amended (the Tax Code). On June 29, 2004, we completed our initial public offering (IPO) of our common stock. Prior to the IPO, 21 hotel interests were owned by SHC LLC. Concurrent with and as part of the transactions relating to the IPO, a reverse spin-off distribution to shareholders separated SHC LLC into two companies, a new, privately-held SHC LLC, with interests, at that time, in seven hotels and SHR, a public entity with interests, at that time, in 14 hotels. See Item 8. Financial Statements and Supplementary Data 1. General for the hotel interests owned or leased by us as of December 31, 2011.

We operate as a self-administered and self-managed REIT, which means that we are managed by our board of directors and executive officers. A REIT is a legal entity that holds real estate interests and, through payments of dividends to stockholders, is permitted to reduce or avoid federal income taxes at the corporate level. To continue to qualify as a REIT, we cannot operate hotels; instead we employ internationally known hotel management companies to operate our hotels under management contracts. We conduct our operations through our direct and indirect subsidiaries including our operating partnership, Strategic Hotel Funding, L.L.C. (SH Funding), which currently holds substantially all of our assets. We are the managing member of SH Funding and hold approximately 99% of its membership units as of December 31, 2011. We manage all business aspects of SH Funding, including the sale and purchase of hotels, the investment in these hotels and the financing of SH Funding and its assets.

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations section, references to we, our, us, and the Company are references to SHR together, except as the context otherwise requires, with its consolidated subsidiaries, including SH Funding.

When presenting the U.S. dollar equivalent amount for any amounts expressed in a foreign currency, the U.S. dollar equivalent amount has been computed based on the exchange rate on the date of the transaction or the exchange rate prevailing on December 31, 2011, as applicable, unless otherwise noted.

Key Indicators of Operating Performance

We evaluate the operating performance of our business using a variety of operating and other information that includes financial information prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) such as total revenues, operating income (loss), net income (loss), and earnings per share, as well as non-GAAP financial information. In addition, we use other information that may not be financial in nature, including statistical information and comparative data. We use this information to measure the performance of individual hotels, groups of hotels, and/or our business as a whole. Key indicators that we evaluate include average daily occupancy, average daily rate (ADR), revenue per available room (RevPAR), and Total RevPAR, which are more fully discussed under Factors Affecting Our Results of

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Operations Revenues. We also evaluate Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA), Comparable EBITDA, Funds from Operations (FFO), FFO-Fully Diluted, and Comparable FFO as supplemental non-GAAP measures to GAAP performance measures. We provide a more detailed discussion of the non-GAAP financial measures under Non-GAAP Financial Measures.

Outlook

RevPAR and occupancy gains accelerated throughout 2011, driven by improved demand from both group and transient business. The lodging industry began its recovery near the end of the first quarter of 2010, after one of the worst downturns in its history. Luxury demand, in which our portfolio has the highest concentration of assets, has experienced positive RevPAR growth beginning with the week of February 20, 2010, following 96 consecutive weeks of negative RevPAR growth.

The fourth quarter of 2011 represented the eighth consecutive quarter of demand growth and seventh consecutive quarter of RevPAR growth and profit margin expansion for our North American portfolio. Same Store Assets (see *Total Portfolio and Same Store Asset Definitions* below) located in North America, which excludes hotels acquired in 2011 and hotels owned through unconsolidated affiliates, gained 2.1 percentage points in occupancy, driven by an 8.8% increase in group room nights compared to the quarter ended December 31, 2010. ADR at our hotels increased a strong 6.4% in the quarter, as a result of a 7.6% increase in group rate and a 6.0% increase in transient rate. For the quarter, RevPAR increased 9.8% and Total RevPAR increased 9.0%.

For the full year of 2011, our Same Store North American portfolio RevPAR grew by 11.0%, driven by a 5.8% increase in ADR and a 3.4 percentage point increase in occupancy. Improvements in both group and transient demand were the drivers of growth in the year as lower rated transient business continued to be replaced with higher rated transient and group room nights. Group room nights increased 5.4% in 2011 at rates that were 5.9% higher than in 2010. Transient room nights grew by 4.6% in 2011 with rates 5.7% higher.

RevPAR for our Same Store Assets located in the United States increased 12.7%, driven by a 7.0% increase in ADR and a 3.6 percentage point increase in occupancy, compared to the full year 2010.

The performance of our asset in Mexico, the Four Seasons Punta Mita Resort, has lagged the recovery of the rest of our portfolio as the hotel continues to be impacted by broad based security concerns in Mexico. For 2011, occupancy at the Four Seasons Punta Mita Resort declined by 5.1 percentage points leading to an 11.7% decline in RevPAR.

As we assess lodging supply and demand dynamics looking forward, we are optimistic about the long-term prospects for a robust and sustained recovery, particularly in the product niche and markets in which we own assets. However, in the near-term we remain cautious given the current backdrop of global macroeconomic uncertainty. Group bookings pace remains our best forward indicator of demand. For our North American portfolio of hotels, definite group room nights for 2012 are up 1.0% compared to the same time last year and are booked at 3.2% higher rates. New supply in the luxury and upper upscale segments remains very well contained in our markets and the current significant gap between hotel trading values and replacement costs bodes favorably for very limited supply growth into the future.

During the lodging downturn we implemented hotel specific contingency plans designed to reduce costs and maximize efficiency at each hotel. These include, but are not limited to, adjusting variable labor, eliminating certain fixed labor, and reducing the hours of room service operations and other food and beverage outlets. We believe the cost structures of our hotels have been fundamentally redesigned to sustain many of the cost reductions, even during periods of rising lodging demand. Therefore, we are optimistic that improving lodging demand will lead to increases in ADR and drive significant profit margin expansion throughout our portfolio.

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Balance Sheet Restructuring

Since the beginning of 2010, we have been in the process of restructuring our balance sheet to decrease our leverage, improve both our short-term and long-term liquidity, and address our near-term debt maturities. This restructuring has been multifaceted and has included asset sales, equity issuances, and recapitalization and refinancing transactions on many of our assets as summarized below:

We issued an aggregate of 109.9 million shares of common stock in a private offering, a public offering and in connection with the purchase of assets, raising \$544.0 million of new equity.

We tendered for and retired our 3.50% Exchangeable Senior Notes (Exchangeable Notes) totaling \$180.0 million.

We tendered for and purchased approximately 3.2 million shares of Preferred Stock totaling \$86.1 million.

We sold our interests in the InterContinental Prague, the Paris Marriott Champs Elysees (Paris Marriott), and BuyEfficient generating net proceeds of \$70.6 million.

We recapitalized our investments in the Hotel del Coronado and the Fairmont Scottsdale Princess hotels and restructured the debt on those properties, reducing our pro-rata share of the debt on these assets from \$463.5 million to \$212.3 million.

We first extended and then replaced our bank credit facility with a new \$300.0 million credit facility with an initial maturity date of June 30, 2014, with an option to extend for an additional year, subject to certain conditions.

We refinanced \$749.5 million of property level mortgage debt scheduled to mature in 2011 and 2012 with new mortgage debt of \$787.8 million, with initial maturity dates ranging from 2014 to 2021 (and 2016 to 2021 assuming extension options are exercised). As a result of these transactions, our total consolidated debt decreased from \$1.6 billion at December 31, 2009 to \$1.1 billion as of December 31, 2011. As of December 31, 2011, we had approximately \$16.6 million of available corporate level cash, not including restricted cash and cash currently held by the hotels, and we had \$51.9 million outstanding borrowings on our \$300.0 million bank credit facility, including \$1.9 million in letters of credit outstanding. Additionally, we had a distribution payable of \$72.5 million for unpaid cumulative preferred dividends as of December 31, 2011.

European Strategy

We previously announced our intention to exit our assets in Europe in an orderly process designed to maximize proceeds. Since that time, we sold the Renaissance Paris Hotel LeParc Trocadero (Renaissance Paris), the InterContinental Prague and our leasehold interest in the Paris Marriott. Our remaining European assets are the Marriott London Grosvenor Square and our leasehold interest in the Marriott Hamburg. While we continue to opportunistically explore options to exit these investments and still intend to be North American-centric with respect to any new acquisitions, our two remaining European assets continue to perform well and we are not currently actively marketing either of these assets for sale.

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The table below summarizes the changes to our consolidated hotel properties and rooms as of December 31, 2011, 2010 and 2009:

	2011	2010	2009
Hotels			
Number of hotels, beginning of year	15	16	18
Acquisitions(a)	2		
Dispositions(b)	(1)	(1)	(2)
Recapitalization of property(c)	(1)		
Number of hotels, end of year	15	15	16
Rooms			
Number of rooms, beginning of year	6,873	7,245	7,590
Acquisitions(a)	324		
Room expansions			11
Dispositions(b)	(192)	(372)	(356)
Recapitalization of property(c)	(649)		
Number of rooms, end of year	6,356	6,873	7,245

- (a) On March 11, 2011, we acquired the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels in exchange for an aggregate of 15.2 million shares of our common stock at a price of \$6.08 per share based on our March 11, 2011 common share closing price, or approximately \$92.4 million.
- (b) See table below for sale of interests in consolidated properties.
- (c) On June 9, 2011, we completed a recapitalization transaction that changed our ownership interest in the Fairmont Scottsdale Princess hotel. See *Off-Balance Sheet Arrangements Fairmont Scottsdale Princess Venture* for further description of this transaction. Additionally, on June 24, 2011, we acquired the remaining 49.0% interest in the InterContinental Chicago hotel, previously owned by our partner in the consolidated affiliate, giving us 100% ownership of the InterContinental Chicago hotel. As part of the transaction, we also acquired an additional 2.5% ownership interest in the Hyatt Regency La Jolla hotel, increasing our controlling interest in the hotel to 53.5%. Total consideration was approximately \$90.2 million, which included the issuance of approximately 10.8 million shares of our common stock at a price of \$6.51 per share based on the June 24, 2011 common share closing price, approximately \$19.4 million of cash, which includes working capital, and post-closing adjustments of \$0.5 million.

Sale of Interests in Consolidated Properties. During the years ended December 31, 2011, 2010, and 2009, we sold our interests in the following consolidated properties and received net sales proceeds, after proration adjustments related to assets and liabilities of the hotels and closing costs, as shown below:

Hotel	Date Sold	Net Sales Proceeds (in millions)
Paris Marriott	April 6, 2011	\$ 58.0
InterContinental Prague(a)	December 15, 2010	\$ 3.6
Renaissance Paris	December 21, 2009	\$ 50.3
Four Seasons Mexico City	October 29, 2009	\$ 52.2

- (a) Approximate consideration received of 106.1 million (\$141.4 million) included the assignment of the hotel's third party debt and the interest rate swap liability related to the third party indebtedness.

Unconsolidated Affiliates. On June 9, 2011, we completed a recapitalization transaction that changed our ownership interest in the Fairmont Scottsdale Princess hotel. See *Off-Balance Sheet Arrangements Fairmont Scottsdale Princess Venture* for further description of this transaction.

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On February 4, 2011, we completed a recapitalization transaction that changed our ownership interest in the Hotel del Coronado. See Off-Balance Sheet Arrangements *Hotel and North Beach Ventures* and *Hotel del Coronado Venture* for further description of this transaction.

On January 21, 2011, we sold our 50.0% interest in BuyEfficient for \$9.0 million and recognized a gain of \$2.6 million.

Total Portfolio and Same Store Asset Definitions. We define our Total Portfolio as properties that we wholly or partially own or lease and whose operations are included in our consolidated operating results. The Total Portfolio excludes all sold properties and assets held for sale included in discontinued operations.

We present certain information about our hotel operating results on a comparable hotel basis, which we refer to as our Same Store analysis. We define our Same Store Assets as those hotels (a) that are owned or leased by us, and whose operations are included in our consolidated operating results and (b) for which we reported operating results throughout the entire reporting periods presented.

Our Same Store Assets for purposes of the comparison of the years ended December 31, 2011 and 2010 exclude the Four Seasons Silicon Valley hotel, the Four Seasons Jackson Hole hotel, unconsolidated affiliates, and all sold properties and assets held for sale included in discontinued operations. Our Same Store Assets equal our Total Portfolio for purposes of the comparison of the years ended December 31, 2010 and 2009.

We present these results of Same Store Assets because we believe that doing so provides useful information for evaluating the period-to-period performance of our hotels and facilitates comparisons with other hotel REITs and hotel owners. In particular, these measures assist in distinguishing whether increases or decreases in revenues and/or expenses are due to operations of the Same Store Assets or from acquisition or disposition activity.

Revenues. Substantially all of our revenue is derived from the operation of our hotels. Specifically, our revenue for the years ended December 31, 2011, 2010 and 2009 consisted of:

	Total Portfolio % of Total Revenues			Same Store Assets % of Total Revenues	
	2011	2010	2009	2011	2010
Revenues:					
Rooms	53.7%	52.8%	52.5%	54.5%	53.9%
Food and beverage	35.0%	34.8%	33.1%	34.9%	34.0%
Other hotel operating revenue	10.6%	11.7%	13.7%	9.8%	11.3%
Lease revenue	0.7%	0.7%	0.7%	0.8%	0.8%
Total revenues	100.0%	100.0%	100.0%	100.0%	100.0%

Rooms revenue. Occupancy and ADR are the major drivers of rooms revenue.

Food and beverage revenue. Occupancy, local catering and banquet events are the major drivers of food and beverage revenue.

Other hotel operating revenue. Other hotel operating revenue consists primarily of cancellation fees, spa, telephone, parking, golf course, Internet access, space rentals, retail and other guest services and is also driven by occupancy.

Lease revenue. We sublease our interest in the Marriott Hamburg to a third party and earn annual base rent plus additional rent contingent on the hotel meeting performance thresholds.

Changes in our revenues are most easily explained by performance indicators that are used in the hotel real estate industry:

average daily occupancy;

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ADR, which stands for average daily rate, is equal to rooms revenue divided by the number of occupied rooms;

RevPAR, which stands for revenue per available room, is equal to rooms revenue divided by the number of rooms available; and

Total RevPAR, which stands for total revenue per available room, is equal to the sum of rooms revenue, food and beverage revenue and other hotel operating revenue, divided by the number of rooms available.

We generate a significant portion of our revenue from two broad categories of customers, transient and group.

Our transient customers include individual or group business and leisure travelers that occupy fewer than 10 rooms per night. Transient customers accounted for approximately 57.5%, 57.2% and 60.1% of the rooms sold during the years ended December 31, 2011, 2010 and 2009, respectively. We divide our transient customers into the following subcategories:

Transient Leisure This category generates the highest room rates and includes travelers that receive published rates offered to the general public that do not have access to negotiated or discounted rates.

Transient Negotiated This category includes travelers, who are typically associated with companies and organizations that generate high volumes of business, that receive negotiated rates that are lower than the published rates offered to the general public.

Our group customers include groups of 10 or more individuals that occupy 10 or more rooms per night. Group customers accounted for approximately 42.5%, 42.8% and 39.9% of the rooms sold during the years ended December 31, 2011, 2010 and 2009, respectively. We divide our group customers into the following subcategories:

Group Association This category includes group bookings related to national and regional association meetings and conventions.

Group Corporate This category includes group bookings related to corporate business.

Group Other This category generally includes group bookings related to social, military, education, religious, fraternal and youth and amateur sports teams.

Fluctuations in revenues, which, for our domestic hotels, historically have been correlated with changes in the United States gross domestic product (U.S. GDP), are driven largely by general economic and local market conditions, which in turn affect levels of business and leisure travel. Guest demographics also affect our revenues. During 2011, demand at our hotels increased significantly, despite tepid U.S. GDP growth, which we believe reflects the relative strength of our primary customer demographics, particularly U.S. based corporations and affluent transient travelers. While hotel demand has improved and luxury hotel demand for the industry is currently at an all-time high, occupancy and ADR metrics for our hotels remain well below prior peak periods given the industry is still in the early stages of recovery.

In addition to economic conditions, supply is another important factor that can affect revenues. Room rates and occupancy tend to fall when supply increases unless the supply growth is offset by an equal or greater increase in demand. One reason we target upper upscale and luxury hotels in select urban and resort markets, including major business centers and leisure destinations, is because they tend to be in locations that have greater supply constraints such as lack of available land, high development costs, long development and entitlement lead times, and brand trade area restrictions that prevent the addition of a certain brand or brands in close proximity. Nevertheless, our hotels are not insulated from competitive pressures and our hotel operators will lower room rates to compete more aggressively for guests in periods when occupancy declines.

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For purposes of calculating our Total Portfolio RevPAR for the years ended December 31, 2011, 2010 and 2009, we exclude unconsolidated affiliates, discontinued operations, and the Marriott Hamburg because we sublease the operations of the hotel and only record lease revenue. Same Store Assets RevPAR is calculated in the same manner as Total Portfolio RevPAR but also excludes the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels for the year ended December 31, 2011. These methods for calculating RevPAR each period are consistently applied through the remainder of this Management's Discussion and Analysis of Financial Condition and Results of Operations and should be taken into consideration wherever RevPAR results are disclosed.

Hotel Operating Expenses. Our hotel operating expenses for the years ended December 31, 2011, 2010 and 2009 consisted of the costs and expenses to provide hotel services, including:

	Total Portfolio % of Total Hotel Operating Expenses			Same Store Assets % of Total Hotel Operating Expenses	
	2011	2010	2009	2011	2010
Hotel Operating Expenses:					
Rooms	19.3%	19.2%	19.0%	19.8%	19.8%
Food and beverage	32.4%	31.3%	30.2%	32.9%	31.6%
Other departmental expenses	35.0%	36.4%	36.5%	34.4%	35.9%
Management fees	4.2%	4.2%	4.4%	4.1%	4.0%
Other hotel expenses	9.1%	8.9%	9.9%	8.8%	8.7%
Total hotel operating expenses	100.0%	100.0%	100.0%	100.0%	100.0%

Rooms expense. Occupancy is a major driver of rooms expense, which has a significant correlation with rooms revenue.

Food and beverage expense. Occupancy, local catering and banquet events are the major drivers of food and beverage expense, which has a significant correlation with food and beverage revenue.

Other departmental expenses. Other departmental expenses consist of general and administrative, marketing, repairs and maintenance, utilities and expenses related to earning other operating revenue.

Management fees. We pay base and incentive management fees to our hotel operators. Base management fees are computed as a percentage of revenue. Incentive management fees are incurred when operating profits exceed levels prescribed in our management agreements.

Other hotel expenses. Other hotel expenses consist primarily of insurance costs and property taxes.

Salaries, wages and related benefits are included within the categories of hotel operating expenses described above and represented approximately 48.4%, 48.1% and 47.7% of the Total Portfolio total hotel operating expenses for the years ended December 31, 2011, 2010 and 2009, respectively.

Most categories of variable operating expenses, such as utilities and certain labor such as housekeeping, fluctuate with changes in occupancy. Increases in RevPAR attributable to increases in occupancy are accompanied by increases in most categories of variable operating costs and expenses while increases in RevPAR attributable to increases in ADR typically only result in increases in limited categories of operating costs and expenses, such as management fees charged by our operators, which are based on hotel revenues. Thus, changes in ADR have a more significant impact on operating margins.

Lease Expense. As a result of the sale-leaseback transaction of the Marriott Hamburg hotel, we record lease expense in our statements of operations. In conjunction with the sale-leaseback transaction, we also recorded a deferred gain, which is amortized as an offset to lease expense.

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Corporate Expenses. Corporate expenses include payroll and related costs, professional fees, travel expenses and office rent.

Recent Events. In addition to the changes to the consolidated hotel properties and unconsolidated affiliates noted above, we expect that the following events will cause our future results of operations to differ from our historical performance:

Preferred Stock Tender Offers. In December 2011, we completed tender offers to purchase a portion of our outstanding Preferred Stock. The results of the tender offers are as follows:

	Number of Shares Validly Tended and Accepted for Purchase	Purchase Price (Per Share)
8.50% Series A Cumulative Redeemable Preferred Stock	340,609	\$ 26.70
8.25% Series B Cumulative Redeemable Preferred Stock	984,625	\$ 26.50
8.25% Series C Cumulative Redeemable Preferred Stock	1,922,273	\$ 26.50

We paid the holders approximately \$86.1 million in cash, which was without interest or accrued and unpaid dividends.

New Bank Credit Facility. On June 30, 2011, we entered into a new \$300.0 million secured, bank credit facility, which also includes a \$100.0 million accordion feature. This new facility replaced the \$350.0 million secured bank credit facility that was set to expire in March 2012. The facility's interest rate is based upon a leverage-based pricing grid ranging from London InterBank Offered Rate (LIBOR) plus 275 basis points to LIBOR plus 375 basis points. The facility's current interest rate is LIBOR plus 300 basis points, a reduction from the previous facility's pricing of LIBOR plus 375 basis points. The facility expires on June 30, 2014, with a one-year extension available, subject to certain conditions. See Liquidity and Capital Resources *Bank credit facility*.

Common Stock. On March 11, 2011, we issued 8.0 million shares of our common stock to an affiliate of the seller of the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels in a private placement at a price of \$6.25 per share for approximate net proceeds of \$49.7 million after expenses. These proceeds were used to repay existing indebtedness under our previous bank credit facility.

Termination and De-Designation of Cash Flow Hedges. On June 20, 2011, we paid \$29.7 million to terminate five interest rate swaps with a combined notional amount of \$300.0 million. We recorded a charge of \$27.3 million, which included the immediate write-off of \$25.5 million previously recorded in accumulated other comprehensive loss (OCL) related to interest rates swaps that were designated to hedge cash flows that are no longer probable of occurring and \$1.8 million of mark to market adjustments related to the terminated interest rate swaps. The charge was recorded in loss on early termination of derivative financial instruments in the consolidated statements of operations for the year ended December 31, 2011. In addition, based on changes in the forecasted levels of LIBOR-based debt, we de-designated one interest rate swap with a notional amount of \$100.0 million as a cash flow hedge. We recorded a charge of \$2.0 million to write off amounts previously recorded in accumulated OCL related to this swap. The charge was recorded in loss on early termination of derivative financial instruments in the consolidated statements of operations for the year ended December 31, 2011. Changes in the market value of the interest rate swap will be recorded in earnings subsequent to the de-designation.

On February 11, 2011, we paid approximately \$4.2 million to terminate three interest rate swaps with a combined notional amount of \$125.0 million. There were no immediate charges to earnings based on our forecasted levels of LIBOR-based debt at the time of the transaction.

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Mortgage Loan Agreements. On July 28, 2011, we refinanced and increased the loan secured by the InterContinental Chicago hotel to \$145.0 million with interest payable monthly at an annual fixed rate of 5.61% and a maturity date of August 1, 2021.

On July 20, 2011, we executed a mortgage agreement in the amount of \$130.0 million, which is secured by the Four Seasons Washington, D.C. hotel, that has interest payable monthly at one-month LIBOR plus 3.15% and has a maturity date of July 20, 2014, with two, one-year extension options, subject to certain conditions.

On July 14, 2011, we refinanced and decreased the loan secured by the Loews Santa Monica Beach Hotel to \$110.0 million with interest payable monthly at one-month LIBOR plus 3.85%. The loan has a maturity date of July 14, 2015, with three, one-year extension options, subject to certain conditions.

On July 6, 2011, we refinanced and decreased the loan secured by the InterContinental Miami hotel to \$85.0 million with interest payable monthly at one-month LIBOR plus 3.50%. The loan has a maturity date of July 6, 2016, with two, one-year extension options, subject to certain conditions.

On June 29, 2011, we repaid the \$76.5 million mortgage loan secured by the Ritz-Carlton Half Moon Bay hotel, which became one of the borrowing base properties under the \$300.0 million bank credit facility agreement.

Acquisition of Note Receivable. In January 2012, we acquired, at a discount to par value, a note receivable that is secured by a property adjacent to the Fairmont Chicago hotel for \$10.5 million.

Table of Contents**Comparison of Year Ended December 31, 2011 to Year Ended December 31, 2010****Operating Results**

The following table presents the operating results for the years ended December 31, 2011 and 2010, including the amount and percentage change in these results between the two years of our Total Portfolio and Same Store Assets (in thousands, except operating data).

	Total Portfolio				Same Store Assets			
	2011	2010	Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)	2011	2010	Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)
Revenues:								
Rooms	\$ 410,315	\$ 362,559	\$ 47,756	13.2%	\$ 367,800	\$ 332,301	\$ 35,499	10.7%
Food and beverage	267,194	238,762	28,432	11.9%	235,130	209,856	25,274	12.0%
Other hotel operating revenue	80,907	79,981	926	1.2%	66,280	69,436	(3,156)	(4.5)%
Lease revenue	5,422	4,991	431	8.6%	5,422	4,991	431	8.6%
Total revenues	763,838	686,293	77,545	11.3%	674,632	616,584	58,048	9.4%
Operating Costs and Expenses:								
Hotel operating expenses	592,306	547,449	(44,857)	(8.2)%	520,027	484,346	(35,681)	(7.4)%
Lease expense	4,865	4,566	(299)	(6.5)%	4,865	4,566	(299)	(6.5)%
Depreciation and amortization	112,062	130,601	18,539	14.2%	100,978	106,036	5,058	4.8%
Impairment losses and other charges		141,858	141,858	100.0%				
Corporate expenses	39,856	34,692	(5,164)	(14.9)%				
Total operating costs and expenses	749,089	859,166	110,077	12.8%	625,870	594,948	(30,922)	(5.2)%
Operating income (loss)	14,749	(172,873)	187,622	108.5%	\$ 48,762	\$ 21,636	\$ 27,126	125.4%
Interest expense, net	(86,274)	(85,855)	(419)	(0.5)%				
Loss on early extinguishment of debt	(1,237)	(925)	(312)	(33.7)%				
Loss on early termination of derivative financial instruments	(29,242)	(18,263)	(10,979)	(60.1)%				
Equity in (losses) earnings of unconsolidated affiliates	(9,215)	13,025	(22,240)	(170.7)%				
Foreign currency exchange loss	(2)	(1,410)	1,408	99.9%				
Other income, net	5,767	2,398	3,369	140.5%				
Loss before income taxes and discontinued operations	(105,454)	(263,903)	158,449	60.0%				
Income tax expense	(970)	(1,408)	438	31.1%				
Loss from continuing operations	(106,424)	(265,311)	158,887	59.9%				
Income from discontinued operations, net of tax	101,572	34,511	67,061	194.3%				
Net loss	(4,852)	(230,800)	225,948	97.9%				
Net loss attributable to the noncontrolling interests in SHRS operating partnership	29	1,687	(1,658)	(98.3)%				
Net income attributable to the noncontrolling interests in consolidated affiliates	(383)	(1,938)	1,555	80.2%				
Net loss attributable to SHRS	\$ (5,206)	\$ (231,051)	\$ 225,845	97.7%				

Reconciliation of Same Store Assets Operating Income to Total Portfolio Operating Income (Loss):

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Same Store Assets operating income	\$ 48,762	\$ 21,636	\$ 27,126	125.4%
Corporate expenses	(39,856)	(34,692)	(5,164)	(14.9)%
Corporate depreciation and amortization	(1,141)	(1,217)	76	6.2%
Corporate impairment losses and other charges		(40,600)	40,600	100.0%
Non-Same Store Assets operating income (loss)	6,984	(118,000)	124,984	105.9%
Total Portfolio operating income (loss)	\$ 14,749	\$ (172,873)	\$ 187,622	108.5%

Operating Data (1):

Number of hotels	15	14	13	13
Number of rooms	6,356	6,681	6,032	6,032

(1) Operating data includes the leasehold interest in Marriott Hamburg and excludes unconsolidated affiliates and properties included in discontinued operations.

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Rooms. For the Total Portfolio, rooms revenue increased \$47.8 million, or 13.2%, for the year ended December 31, 2011 from the year ended December 31, 2010. RevPAR from our Total Portfolio for the year ended December 31, 2011 increased by 15.0% from the year ended December 31, 2010. The components of RevPAR from our Total Portfolio for the years ended December 31, 2011 and 2010 are summarized as follows:

	Years Ended December 31,		Change (%) Favorable/ (Unfavorable)
	2011	2010	
Occupancy	72.03%	68.65%	4.9%
ADR	\$ 247.80	\$ 226.01	9.6%
RevPAR	\$ 178.48	\$ 155.16	15.0%

Our Same Store Assets contributed to a \$35.5 million, or 10.7%, increase in rooms revenue, which is more fully explained below as part of our rooms revenue Same Store Assets analysis. RevPAR from our Same Store Assets for the year ended December 31, 2011 increased by 10.7% from the year ended December 31, 2010. The components of RevPAR from our Same Store Assets for the years ended December 31, 2011 and 2010 are summarized as follows:

	Years Ended December 31,		Change (%) Favorable/ (Unfavorable)
	2011	2010	
Occupancy	72.15%	68.97%	4.6%
ADR	\$ 242.76	\$ 229.44	5.8%
RevPAR	\$ 175.16	\$ 158.25	10.7%

The increase in RevPAR for the Same Store Assets resulted from the combination of a 5.8% increase in ADR and a 3.18 percentage-point increase in occupancy. Rooms revenue increased due to improving market conditions across all but one of our Same Store Assets for the year ended December 31, 2011 when compared to the year ended December 31, 2010. The Westin St. Francis and the Ritz-Carlton Laguna Niguel hotels experienced significant increases as a result of higher group occupancy. The Four Seasons Punta Mita Resort was the only consolidated hotel that experienced a significant decrease in rooms revenue due to declining demand resulting from safety concerns in Mexico. The increase in Total Portfolio rooms revenue also includes \$22.4 million of additional rooms revenue generated by the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels, which we acquired in March 2011. The increase in rooms revenue was partially offset by a decrease of \$10.1 million in rooms revenue related to the Fairmont Scottsdale Princess hotel, which became an unconsolidated affiliate in the second quarter of 2011 (see Off-Balance Sheet Arrangements *Fairmont Scottsdale Princess Venture*).

Food and Beverage. Food and beverage revenue increased \$28.4 million, or 11.9%, for the Total Portfolio when comparing the year ended December 31, 2011 to the year ended December 31, 2010. Our Same Store Assets contributed to a \$25.3 million, or 12.0%, increase in food and beverage revenue. The primary factor increasing food and beverage revenue at the Same Store Assets was an increase in group occupancy, which generated higher banquet revenue when compared to the prior year, and increased revenue at the hotels food and beverage outlets, which included increased revenues at the Westin St. Francis hotel resulting from a change in the terms of a restaurant agreement, and the opening of the Michael Jordan Steakhouse at the InterContinental Chicago hotel. The increase in Total Portfolio food and beverage revenue also includes \$15.0 million of additional revenue generated by the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels, which we acquired in March 2011. These increases in Total Portfolio food and beverage revenue were partially offset by an \$11.8 million decrease in food and beverage revenue related to the Fairmont Scottsdale Princess hotel, which became an unconsolidated affiliate in the second quarter of 2011.

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Other Hotel Operating Revenue. Other hotel operating revenue at the Total Portfolio increased \$0.9 million, or 1.2%, for the year ended December 31, 2011 from the year ended December 31, 2010. The increase in Total Portfolio other hotel operating revenue includes \$9.3 million of additional revenue generated by the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels that we acquired in March 2011, which was partially offset by a \$5.2 million decrease in other hotel operating revenue related to the Fairmont Scottsdale Princess hotel, which became an unconsolidated affiliate in the second quarter of 2011. In addition, there was a decrease of \$3.2 million, or 4.5%, in other hotel operating revenue related to the Same Store Assets, which was primarily due to lower cancellation/attrition revenues, a decrease in theatre revenue at the Marriott Lincolnshire Resort, and a decrease in condominium rentals at the Four Seasons Punta Mita Resort.

Hotel Operating Expenses. The following table presents the components of our hotel operating expenses for the years ended December 31, 2011 and 2010, including the amount and percentage changes in these expenses between the two years of our Total Portfolio and Same Store Assets (in thousands):

	Total Portfolio				Same Store Assets			
	2011	2010	Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)	2011	2010	Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)
Hotel operating expenses:								
Rooms	\$ 114,087	\$ 105,142	\$ (8,945)	(8.5)%	\$ 102,886	\$ 95,966	\$ (6,920)	(7.2)%
Food and beverage	192,028	171,279	(20,749)	(12.1)%	171,018	152,830	(18,188)	(11.9)%
Other departmental expenses	207,664	199,336	(8,328)	(4.2)%	179,085	174,023	(5,062)	(2.9)%
Management fees	24,719	22,911	(1,808)	(7.9)%	21,084	19,426	(1,658)	(8.5)%
Other hotel expenses	53,808	48,781	(5,027)	(10.3)%	45,954	42,101	(3,853)	(9.2)%
Total hotel operating expenses	\$ 592,306	\$ 547,449	\$ (44,857)	(8.2)%	\$ 520,027	\$ 484,346	\$ (35,681)	(7.4)%

For the Total Portfolio, hotel operating expenses increased by \$44.9 million, or 8.2%, for the year ended December 31, 2011 when compared to the year ended December 31, 2010, primarily due to our Same Store Assets which contributed to an increase of \$35.7 million, or 7.4%. For the Same Store Assets, hotel operating expenses were impacted by \$16.9 million higher payroll costs resulting from higher occupancy and wage increases at the hotels, \$5.7 million higher food and beverage costs due to increased food and beverage consumption, change in terms of a restaurant agreement at the Westin St. Francis and the new Michael Jordan Steakhouse at the InterContinental Chicago, \$3.0 million higher credit card and travel agent commissions, which increased due to higher occupancy, rates and food and beverage volume, \$1.8 million higher management fees, and a \$1.2 million increase in real estate taxes. Additionally, the Total Portfolio hotel operating expenses includes approximately \$40.2 million of expenses related to the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels, which we acquired in March 2011. The increase in Total Portfolio hotel operating expenses was partially offset by a \$30.8 million decrease related to the Fairmont Scottsdale Princess hotel, which became an unconsolidated affiliate in the second quarter of 2011.

Depreciation and Amortization. For the Total Portfolio, depreciation and amortization decreased \$18.5 million, or 14.2%, for year ended December 31, 2011 when compared to the year ended December 31, 2010. This was primarily driven by a decrease in depreciation expense of \$17.0 million related to the Fairmont Scottsdale Princess hotel due to an impairment of this asset in the fourth quarter of 2010, which decreased depreciation expense subsequent to the impairment, and the hotel becoming an unconsolidated affiliate in the second quarter of 2011. In addition, the depreciation and amortization for the Same Store Assets decreased by \$5.1 million primarily due to certain assets becoming fully depreciated. The decrease in depreciation and amortization was partially offset by a \$3.6 million increase related to the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels, which we acquired in March 2011.

Impairment Losses and Other Charges. There were no impairment losses and other charges recorded during the year ended December 31, 2011. During the year ended December 31, 2010, we performed an

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impairment test of long-lived assets at the Fairmont Scottsdale Princess hotel due to the fact that its fair value at December 31, 2010 was below its carrying value and the uncertainty surrounding our intent and ability to continue to hold the property beyond the underlying mortgage maturity date and recorded a non-cash impairment charge of \$101.3 million. We also recorded a non-cash impairment charge of \$40.6 million related to an other-than-temporary decline in value of our investment in SHC KSL Partners, LP (Hotel Venture) and HdC North Beach Development, LLLP (North Beach Venture).

Corporate Expenses. Corporate expenses increased \$5.2 million, or 14.9%, for the year ended December 31, 2011 when compared to the year ended December 31, 2010. These expenses consist primarily of payroll and related costs, professional fees, travel expenses and office rent. The increase in corporate expenses is primarily due to a \$6.0 million increase in the charge related to the Value Creation Plan. See Item 8. Financial Statements and Supplementary Data 12. Share-Based Employee Compensation Plans Value Creation Plan for further description of this plan. The amounts recorded in corporate expenses related to the Value Creation Plan are based on the fair value of the Value Creation Plan awards, which are based directly on our market capitalization and fluctuate as a result of changes in our stock price and issuances of shares of our common stock.

Interest Expense, Net. The \$0.4 million, or 0.5%, increase in interest expense, net for the year ended December 31, 2011 when compared to the year ended December 31, 2010, was primarily due to:

a \$33.7 million increase due to the net impact of higher average interest rates offset by a decrease in amortization of interest rate swap costs, and

a \$0.3 million decrease in interest income, partially offset by

a \$19.0 million decrease attributable to lower average borrowings,

a \$11.2 million decrease in expense related to the mark to market of certain interest rate swaps,

a \$2.9 million decrease in the amortization of deferred financing costs, and

a \$0.4 million increase in capitalized interest.

The components of interest expense, net for the years ended December 31, 2011 and 2010 are summarized as follows (in thousands):

	Years Ended December 31,	
	2011	2010
Mortgages and other debt	\$ (67,528)	\$ (35,874)
Bank credit facility	(2,353)	(5,457)
Exchangeable Notes		(2,783)
Amortization of Exchangeable Notes discount		(1,865)
Amortization of deferred financing costs	(3,721)	(6,634)
Amortization of interest rate swap costs	(16,111)	(25,317)
Mark to market of certain interest rate swaps	2,183	(9,013)
Interest income	173	430
Capitalized interest	1,083	658
 Total interest expense, net	 \$ (86,274)	 \$ (85,855)

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The weighted average debt outstanding for the years ended December 31, 2011 and 2010 amounted to \$1.06 billion and \$1.30 billion, respectively. At December 31, 2011, including the effect of interest rate swaps, approximately 93.1% of our total debt had fixed interest rates.

Loss on Early Extinguishment of Debt. During the year ended December 31, 2011, we recognized a loss on early extinguishment of debt of \$1.2 million primarily due to write offs of unamortized deferred financing costs

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and other closing costs related to refinancing of certain mortgages and a new bank credit facility. During the year ended December 31, 2010, we tendered all outstanding Exchangeable Notes and recognized a loss on early extinguishment of debt of \$0.9 million.

Loss on Early Termination of Derivative Financial Instruments. During the year ended December 31, 2011, we terminated interest rate swaps, and recorded a charge of \$27.3 million, which included the immediate write-off of \$25.5 million previously recorded in accumulated OCL related to interest rate swaps that were designated to hedge cash flows that are no longer probable of occurring and \$1.8 million of mark to market adjustments related to the terminated interest rate swaps. In addition, based on changes in the forecasted levels of LIBOR-based debt, we de-designated one interest rate swap as a cash flow hedge. We recorded an additional charge of \$2.0 million for the year ended December 31, 2011 to write off amounts previously recorded in accumulated OCL related to this swap.

During the year ended December 31, 2010, we terminated five interest rate swaps and recognized a charge of \$18.3 million, which included amounts previously recorded in accumulated OCL related to these swaps.

Equity in (Losses) Earnings of Unconsolidated Affiliates. The following tables present equity in (losses) earnings and certain components included in the calculation of equity in (losses) earnings resulting from our unconsolidated affiliates.

Year ended December 31, 2011 (in thousands):

	Fairmont Scottsdale Princess Venture(1)	Hotel del Coronado Venture(2)	Hotel/North Beach Ventures(3)	Four Seasons Residence Club Punta Mita (RCPM)	Total
Equity in losses	\$ (5,703)	\$ (2,914)	\$ (511)	\$ (87)	\$ (9,215)
Depreciation and amortization	4,022	7,105	544	92	11,763
Interest expense	452	10,677	778	100	12,007
Income tax expense (benefit)		164	(668)	(45)	(549)

Year ended December 31, 2010 (in thousands):

	Hotel /North Beach Ventures(3)	Four Seasons RCPM	BuyEfficient(4)	Total
Equity in earnings	\$ 12,175	\$ 271	\$ 579	\$ 13,025
Depreciation and amortization	7,894	79		7,973
Interest expense	7,753	244		7,997
Income tax (benefit) expense	(503)	95		(408)

- (1) On June 9, 2011, the Fairmont Scottsdale Princess Venture, which consists of FMT Scottsdale Holdings, L.L.C. and Walton/SHR FPH Holdings, L.L.C., was formed. See Off-Balance Sheet Arrangements *Fairmont Scottsdale Princess Venture* for further detail regarding the ownership of the Fairmont Scottsdale Princess hotel.
- (2) The Hotel del Coronado Venture is BSK Del Partners, L.P., the owner of the Hotel del Coronado as of February 4, 2011. See Off-Balance Sheet Arrangements *Hotel del Coronado Venture* for further detail regarding the ownership of the Hotel del Coronado.
- (3) These ventures include SHC KSL Partners, LP (Hotel Venture), the owner of the Hotel del Coronado through February 3, 2011, and HdC North Beach Development, LLLP (North Beach Venture), the owner of a residential condominium-hotel development adjacent to the hotel. See Off-Balance Sheet Arrangements *Hotel and North Beach Ventures* for further detail regarding the ownership of the Hotel del Coronado.
- (4) On January 21, 2011, we sold our 50.0% interest in BuyEfficient for \$9.0 million.

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We recorded \$9.2 million of equity in losses during the year ended December 31, 2011, which is a \$22.2 million decrease from the \$13.0 million equity in earnings recorded during the year ended December 31, 2010, primarily due to our share of an \$11.0 million gain on extinguishment of debt at the Hotel Venture, as a result of a discounted payoff on one of the loans in 2010. The equity in losses in 2011 is primarily due to a higher interest rate on the new loan secured as part of the Hotel del Coronado recapitalization, and operating losses at the Fairmont Scottsdale Princess, which became an unconsolidated affiliate during the second quarter of 2011.

Foreign Currency Exchange Loss. The foreign currency exchange loss decreased by \$1.4 million during the year ended December 31, 2011 when compared to the prior year. The change was primarily related to changing foreign exchange rates related to a GBP-denominated loan associated with the Marriott London Grosvenor Square.

Other Income, Net. Other income, net includes asset management fee income, non-income related state, local and franchise taxes, as well as miscellaneous income and expenses. The increase in other income, net of \$3.4 million for the year ended December 31, 2011 when compared to the prior year is primarily due to a \$2.6 million gain we recognized on the sale of our interest in BuyEfficient and an increase in asset management fee income, which includes financing and other fees received related to the Hotel del Coronado; partially offset by a refund of a local use tax related to the Fairmont Scottsdale Princess hotel received in 2010.

Income Tax Expense. Income tax expense decreased \$0.4 million, or 31.1%, during the year ended December 31, 2011 when compared to the year ended December 31, 2010. The change in income taxes primarily relates to a decrease in hotel operations in Mexico.

Income from Discontinued Operations, Net of Tax. We sold our leasehold interest in the Paris Marriott hotel during the second quarter of 2011. We sold the InterContinental Prague hotel during the fourth quarter of 2010. The results of operations of these hotels were reclassified as discontinued operations for the periods presented.

The income from discontinued operations, net of tax of \$101.6 million for the year ended December 31, 2011 consisted primarily of a \$101.3 million gain, net of tax, recognized on the sale of the Paris Marriott hotel primarily resulting from the recognition of a deferred gain. The income from discontinued operations, net of tax, of \$34.5 million for the year ended December 31, 2010 primarily consisted of the operating results of the Paris Marriott and the InterContinental Prague hotels as well as a \$28.4 million gain recognized on the sale of the InterContinental Prague hotel and the recognition of a \$1.9 million deferred gain related to the sale of the Hyatt Regency New Orleans hotel, partially offset by a \$0.6 million loss recognized on the sale of the Four Seasons Mexico City hotel.

Net Loss Attributable to the Noncontrolling Interests in SHR's Operating Partnership. We record net loss or income attributable to noncontrolling interests in SHR's operating partnership based on the percentage of SH Funding we do not own. The decrease in net loss attributable to noncontrolling interests in SHR's operating partnership of \$1.7 million for the year ended December 31, 2011 when compared to the prior year was primarily due to a decrease in net loss recognized during the year ended December 31, 2011 when compared to the year ended December 31, 2010. Additionally, our ownership percentage of SH Funding increased when compared to the prior period due to the issuance of shares of common stock in connection with i) the acquisition of interests in the InterContinental Chicago and Hyatt Regency La Jolla hotels in June 2011, ii) the acquisition of the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels in March 2011, and iii) a private placement and common stock offering in March 2011 and May 2010, respectively.

Net Income Attributable to the Noncontrolling Interests in Consolidated Affiliates. We record net loss or income attributable to noncontrolling interests in consolidated affiliates for the non-ownership interests in hotels that are partially owned by us. Net income attributable to noncontrolling interests in consolidated affiliates decreased by \$1.6 million for the year ended December 31, 2011 when compared to the prior year due to a

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decrease in net income at the InterContinental Chicago and the acquisition of the remaining interest in this hotel, which gave us 100% ownership of the hotel in June 2011. The decrease was partially offset by an increase in net income at the Hyatt Regency La Jolla hotel.

Comparison of Year Ended December 31, 2010 to Year Ended December 31, 2009**Operating Results**

The following table presents the operating results for the years ended December 31, 2010 and 2009, including the amount and percentage change in these results between the two years (in thousands, except operating data).

	2010	2009	Total Portfolio Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)
Revenues:				
Rooms	\$ 362,559	\$ 343,891	\$ 18,668	5.4%
Food and beverage	238,762	216,982	21,780	10.0%
Other hotel operating revenue	79,981	89,525	(9,544)	(10.7)%
Lease revenue	4,991	4,858	133	2.7%
Total revenues	686,293	655,256	31,037	4.7%
Operating Costs and Expenses:				
Hotel operating expenses	547,449	530,364	(17,085)	(3.2)%
Lease expense	4,566	4,752	186	3.9%
Depreciation and amortization	130,601	130,955	354	0.3%
Impairment losses and other charges	141,858	99,740	(42,118)	(42.2)%
Corporate expenses	34,692	23,910	(10,782)	(45.1)%
Total operating costs and expenses	859,166	789,721	(69,445)	(8.8)%
Operating loss	(172,873)	(134,465)	(38,408)	(28.6)%
Interest expense, net	(85,855)	(93,289)	7,434	8.0%
Loss on early extinguishment of debt	(925)	(883)	(42)	(4.8)%
Loss on early termination of derivative financial instruments	(18,263)		(18,263)	(100.0)%
Equity in earnings of unconsolidated affiliates	13,025	1,718	11,307	658.1%
Foreign currency exchange loss	(1,410)	(896)	(514)	(57.4)%
Other income (expenses), net	2,398	(137)	2,535	1,850.4%
Loss before income taxes and discontinued operations	(263,903)	(227,952)	(35,951)	(15.8)%
Income tax expense	(1,408)	(3,344)	1,936	57.9%
Loss from continuing operations	(265,311)	(231,296)	(34,015)	(14.7)%
Income (loss) from discontinued operations, net of tax	34,511	(15,137)	49,648	328.0%
Net loss	(230,800)	(246,433)	15,633	6.3%
Net loss attributable to the noncontrolling interests in SHR's operating partnership	1,687	3,129	(1,442)	(46.1)%
Net income attributable to the noncontrolling interests in consolidated affiliates	(1,938)	(641)	(1,297)	(202.3)%
Net loss attributable to SHR	\$ (231,051)	\$ (243,945)	\$ 12,894	5.3%

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Operating Data (1):

Number of hotels	14	14
Number of rooms	6,681	6,681

- (1) Operating data includes the leasehold interest in the Marriott Hamburg and excludes unconsolidated affiliates and properties included in discontinued operations.

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Rooms. Rooms revenue increased \$18.7 million, or 5.4%, for the year ended December 31, 2010 from the year ended December 31, 2009. RevPAR for the year ended December 31, 2010 increased by 5.4% from the year ended December 21, 2009. The components of RevPAR for the years ended December 31, 2010 and 2009 are summarized as follows:

	Years Ended December 31,		Change (%) Favorable/ (Unfavorable)
	2010	2009	
Occupancy	68.65%	66.27%	3.6%
ADR	\$ 226.01	\$ 222.08	1.8%
RevPAR	\$ 155.16	\$ 147.17	5.4%

Rooms revenue increased across most of our hotels for the year ended December 31, 2010 from the year ended December 31, 2009. Hotels that had significant increases in rooms revenue include the Ritz-Carlton Half Moon Bay, Marriott London Grosvenor Square and Loews Santa Monica Beach hotels, which had increases of 20.9%, 17.3%, and 16.1%, respectively. These hotels have had higher group demand and improved ADR due to improving market conditions compared to 2009. There were no significant declines in rooms revenue at individual hotel properties.

Food and Beverage. Food and beverage revenue increased \$21.8 million, or 10.0%, for the year ended December 31, 2010 from the year ended December 31, 2009. With the exception of the Hyatt Regency La Jolla hotel, all hotels experienced an increase in food and beverage revenue. The primary factor increasing food and beverage revenue at the hotels was an increase in group occupancy, which generated higher banquet revenue when compared to prior year. The Hyatt Regency La Jolla hotel experienced a decrease in food and beverage revenue as a result of lower group demand in 2010 and social catering activity in 2009, which was not repeated in 2010.

Other Hotel Operating Revenue. Other hotel operating revenue decreased \$9.5 million, or 10.7%, for the year ended December 31, 2010 from the year ended December 31, 2009. The decrease is primarily due to a \$11.2 million decline in cancellation revenue when compared to prior year. During 2009, there were significant group cancellations, particularly at the Fairmont Scottsdale Princess, Ritz-Carlton Half Moon Bay, and Ritz-Carlton Laguna Niguel hotels due to corporate cost-cutting initiatives during the economic downturn and the negative perception of companies staying at luxury hotels.

Hotel Operating Expenses. The following table presents the components of our hotel operating expenses for the years ended December 31, 2010 and 2009, including the amount and percentage change in these expenses between the two years (in thousands):

	2010	2009	Total Portfolio	
			Change (\$) Favorable/ (Unfavorable)	Change (%) Favorable/ (Unfavorable)
Hotel operating expenses:				
Rooms	\$ 105,142	\$ 100,642	\$ (4,500)	(4.5)%
Food and beverage	171,279	160,252	(11,027)	(6.9)%
Other departmental expenses	199,336	193,699	(5,637)	(2.9)%
Management fees	22,911	23,386	475	2.0%
Other hotel expenses	48,781	52,385	3,604	6.9%
Total hotel operating expenses	\$ 547,449	\$ 530,364	\$ (17,085)	(3.2)%

Hotel operating expenses increased \$17.1 million, or 3.2%. Hotel operating expenses were impacted by higher payroll costs due to increases in occupancy, which resulted in higher variable-labor costs and bonus increases, and higher food and beverage costs due to increased food and beverage consumption. In addition,

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credit card and travel agent commissions increased due to higher occupancy and rates. These increases were partially offset by lower real estate tax, insurance, and utility costs and lower management fees due to management agreement amendments at certain of our hotels.

Impairment Losses and Other Charges. During the year ended December 31, 2010, we performed an impairment test of long-lived assets at the Fairmont Scottsdale Princess hotel due to the fact that its fair value at December 31, 2010 was below its carrying value and the uncertainty surrounding our intent and ability to continue to hold the property beyond the underlying mortgage maturity date of September 2011. Due to the uncertainty of the hold period, we performed a probability weighted analysis, which included various scenarios, including a potential sale on the property. Based on this analysis, the carrying value exceeded the undiscounted cash flows. As such we recognized a non-cash impairment charge of \$101.3 million for the difference between the carrying value and the fair value of the hotel. We also recorded a non-cash impairment charge of \$40.6 million related to an other-than-temporary decline in value of our investment in the Hotel and North Beach Ventures.

During the year ended December 31, 2009, we recorded a non-cash goodwill impairment charge of \$41.9 million. The charge related to the Four Seasons Washington, D.C. (\$23.9 million), Ritz-Carlton Half Moon Bay (\$15.5 million) and Marriott London Grosvenor Square (\$2.5 million) hotels. We recorded a non-cash long-lived asset impairment charge of \$23.2 million related to two Mexican development sites based on uncertainties surrounding the development of this land in a manner consistent with our original plan. We also recorded a non-cash impairment charge of \$26.5 million related to an other-than-temporary decline in value of our investment in the Hotel and North Beach Ventures.

During the year ended December 31, 2009, we abandoned several capital projects due to unfavorable market conditions and recorded a charge of approximately \$8.0 million to write off capitalized costs and deposits related to these projects. For the year ended December 31, 2009, we also recorded a charge of \$0.2 million to write off our investment in Luxury Leisure Properties International, L.L.C. (LLPI). Our interest in the LLPI venture was redeemed in May 2009.

Corporate Expenses. Corporate expenses increased \$10.8 million, or 45.1%, for the year ended December 31, 2010 when compared to the prior year. These expenses consist primarily of payroll and related costs, professional fees, travel expenses and office rent. The increase in corporate expenses is due to a \$12.5 million increase in the charge related to the Value Creation Plan. See Item 8. Financial Statements and Supplementary Data 12. Share-Based Employee Compensation Plans Value Creation Plan for further description of this plan. This expense is directly related to the Company's market capitalization and increased during the year as a result of our May 2010 equity offering, increases in our stock price during the year, and continued volatility in the stock price. The increase was partially offset by a decrease in expense related to our restricted stock units (RSUs). In 2009, we accelerated the vesting of certain RSUs issued prior to December 31, 2008 resulting in a one-time charge of approximately \$3.6 million to recognize the remaining unamortized deferred compensation costs related to these vested RSUs.

Interest Expense, Net. The \$7.4 million, or 8.0%, decrease in interest expense, net for the year ended December 31, 2010 when compared to the year ended December 31, 2009 was primarily due to:

a \$16.5 million decrease attributable to lower average borrowings, partially offset by

a \$7.8 million increase in expense related to the mark to market of certain interest rate swaps,

a \$1.1 million decrease in capitalized interest, and

a \$0.2 million decrease in interest income.

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The components of interest expense, net for the years ended December 31, 2010 and 2009 are summarized as follows (in thousands):

	Years Ended December 31,	
	2010	2009
Mortgages and other debt	\$ (35,874)	\$ (47,049)
Bank credit facility	(5,457)	(10,998)
Exchangeable Notes	(2,783)	(6,311)
Amortization of Exchangeable Notes discount	(1,865)	(4,296)
Amortization of deferred financing costs	(6,634)	(6,610)
Amortization of interest rate swap costs	(25,317)	(19,191)
Mark to market of certain interest rate swaps	(9,013)	(1,197)
Interest income	430	640
Capitalized interest	658	1,723
 Total interest expense, net	 \$ (85,855)	 \$ (93,289)

The weighted average debt outstanding for the years ended December 31, 2010 and 2009 amounted to \$1.30 billion and \$1.60 billion, respectively, and the weighted average interest rate for both the years ended December 31, 2010 and 2009, including the effect of net settlements of interest rate swaps but excluding the mark to market of certain interest rate swaps, was 5.5%. At December 31, 2010, including the effect of interest rate swaps, approximately 100.0% of our total debt had fixed interest rates.

Loss on Early Extinguishment of Debt. During the year ended December 31, 2010, we tendered all outstanding Exchangeable Notes and recognized loss on early extinguishment of debt of \$0.9 million. During the year ended December 31, 2009, we amended the terms of our bank credit facility and wrote off \$0.9 million of deferred financing costs.

Loss on Early Termination of Derivative Financial Instruments. During the year ended December 31, 2010, we terminated five interest rate swaps and recognized a charge of \$18.3 million, which included amounts previously recorded in accumulated OCL related to these swaps.

Equity in Earnings of Unconsolidated Affiliates. The following tables present equity in earnings and certain components included in the calculation of equity in earnings resulting from our unconsolidated affiliates.

Year ended December 31, 2010 (in thousands):

	Hotel /North Beach Ventures	Four Seasons RCPM	BuyEfficient	Total
Equity in earnings	\$ 12,175	\$ 271	\$ 579	\$ 13,025
Depreciation	7,894	79		7,973
Interest expense	7,753	244		7,997
Income tax (benefit) expense	(503)	95		(408)

Year ended December 31, 2009 (in thousands):

	Hotel /North Beach Ventures	Four Seasons RCPM	BuyEfficient	Total
Equity in earnings	\$ 936	\$ 254	\$ 528	\$ 1,718
Depreciation	7,736	128		7,864
Interest expense	7,799	104		7,903
Income tax expense	82	86		168

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We recorded \$13.0 million of equity in earnings during the year ended December 31, 2010, which is an \$11.3 million increase from the \$1.7 million equity in earnings recorded during the year ended December 31, 2009. The change was primarily due to our \$11.0 million share of the gain on extinguishment of debt at the Hotel Venture, as a result of a discounted payoff on one of the loans. See Off-Balance Sheet Arrangements for further details.

Foreign Currency Exchange Loss. We recorded a foreign currency exchange loss of \$1.4 million during the year ended December 31, 2010, which is a \$0.5 million increase from the \$0.9 million foreign currency exchange loss recorded in the prior year. The change was primarily related to changing foreign exchange rates related to a GBP-denominated loan associated with the Marriott London Grosvenor Square and working capital at certain foreign hotel properties.

Other Income (Expenses), Net. Other income (expenses), net includes asset management fee income, non-income related state, local and franchise taxes, as well as miscellaneous income and expenses. The increase in income of \$2.5 million for the year ended December 31, 2010 when compared to the prior year is primarily due to a refund of a local use tax related to the Fairmont Scottsdale Princess hotel and an increase in asset management fee income.

Income Tax Expense. Income tax expense decreased \$1.9 million, or 57.9%, during the year ended December 31, 2010 when compared to the year ended December 31, 2009. The change in income taxes primarily relates to the Four Seasons Punta Mita hotel. We recorded a charge in the first quarter of 2009 to adjust 2008 deferred items related to the newly enacted Mexican flat tax. There was no similar charge in 2010.

Income (Loss) from Discontinued Operations, Net of Tax. We sold the Paris Marriott hotel during the second quarter of 2011, the InterContinental Prague hotel during the fourth quarter of 2010 and both the Four Seasons Mexico City and Renaissance Paris hotels during the fourth quarter of 2009. The results of operations of these hotels were reclassified as discontinued operations for the periods presented. The income (loss) from discontinued operations amounted to \$34.5 million of income and \$15.1 million of loss for the years ended December 31, 2010 and 2009, respectively.

The income from discontinued operations for the year ended December 31, 2010 primarily consisted of the operating results of the InterContinental Prague hotel and Paris Marriott hotel as well as a \$28.4 million gain recognized on the sale of the InterContinental Prague hotel and a \$1.9 million deferred gain related to the sale of the Hyatt Regency New Orleans hotel, partially offset by a \$0.6 million loss recognized on the sale of the Four Seasons Mexico City hotel.

The \$15.1 million loss from discontinued operations for the year ended December 31, 2009 primarily consisted of the operating results of the InterContinental Prague hotel and the Renaissance Paris hotel, which included a non-cash long-lived asset impairment charge of \$30.8 million, partially offset by a \$6.5 million gain recognized on the sale of the Four Seasons Mexico City hotel and a \$11.7 million gain recognized on the sale of the Renaissance Paris hotel as well as operating results at the Paris Marriott hotel and Four Seasons Mexico City hotel.

Net Loss Attributable to the Noncontrolling Interests in SHR's Operating Partnership. We record net loss or income attributable to noncontrolling interest in SHR's operating partnership based on the percentage of SH Funding we do not own. Net loss attributable to noncontrolling interests in SHR's operating partnership decreased by \$1.4 million when compared to the prior year. This change was due to the decrease in net loss recognized during the year ended December 31, 2010 when compared to the prior year. Additionally, our ownership percentage of SH Funding increased when compared to the prior year due to a common stock offering in May 2010.

Net Income Attributable to the Noncontrolling Interests in Consolidated Affiliates. We record net loss or income attributable to noncontrolling interests in consolidated affiliates for the non-ownership interests in hotels

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that are partially owned by us. Net income attributable to noncontrolling interests in consolidated affiliates increased by \$1.3 million for the year ended December 31, 2010 when compared to the year ended December 31, 2009 due to an increase in net income of our consolidated affiliates.

Liquidity and Capital Resources

Our short-term liquidity requirements consist primarily of funds necessary to pay for operating expenses and other expenditures, including:

recurring maintenance and capital expenditures necessary to maintain our properties properly;

interest expense and scheduled principal payments on outstanding indebtedness; and

future distributions to our preferred stockholders.

Historically, we have satisfied our short-term liquidity requirements through our existing working capital, cash provided by operations, and our bank credit facility. On June 30, 2011, we entered into a new \$300.0 million bank credit facility agreement, which includes a \$100.0 million accordion feature. The new facility will continue to provide sufficient borrowing capacity to meet our short-term liquidity requirements during 2012. As of December 31, 2011, we were in compliance with our financial and other restrictive covenants contained in the bank credit facility. Additionally, as of December 31, 2011, we had approximately \$16.6 million of available corporate level cash.

Our available capacity under the bank credit facility and compliance with financial covenants in future periods will depend substantially on the financial results of our hotels, and in particular, the operating results and appraised values of the borrowing base assets, which include the Four Seasons Punta Mita Resort, the Marriott Lincolnshire Resort, the Ritz-Carlton Half Moon Bay hotel, and the Ritz-Carlton Laguna Niguel hotel. As of February 22, 2012, the outstanding borrowings and letters of credit in the aggregate were \$55.9 million.

In the second quarter of 2010, we completed a common stock offering and raised net proceeds of approximately \$331.8 million. These proceeds were used to fund our tender offer for Exchangeable Notes and repay existing indebtedness under the previous bank credit facility. In the fourth quarter of 2010, we sold the InterContinental Prague hotel to a buyer who assumed the mortgage debt and related interest rate swap liability. The transaction resulted in net sales proceeds of \$3.6 million. On March 11, 2011, we acquired the Four Seasons Silicon Valley and the Four Seasons Jackson Hole hotels in exchange for an aggregate of 15.2 million shares of our common stock at a price of \$6.08 per share based on our March 11, 2011 common share closing price and concurrently privately placed and issued an additional 8.0 million shares of our stock to an affiliate of the seller of the two hotels at a price of \$6.25 per share. The net proceeds from the concurrent private placement were used to repay existing indebtedness under the previous bank credit facility. On April 6, 2011, we sold our leasehold interest in the Paris Marriott hotel for consideration of 29.2 million (\$41.6 million) and received an additional 11.9 million (\$16.9 million) related to a security deposit that was released back to us and other closing adjustments. In July 2011, we refinanced certain of our mortgage loans whereby we staggered and extended maturities from 2016 through 2021, assuming extension options are exercised (see *Mortgages and other debt payable* below). We believe that the measures we have taken, as described above, should be sufficient to satisfy our liquidity needs for the next 12 months.

In November 2008, our board of directors elected to suspend the quarterly dividend to holders of shares of our common stock beginning in the fourth quarter of 2008. In February 2009, our board of directors elected to suspend the quarterly dividend to holders of our Preferred Stock as a measure to preserve liquidity. In the fourth quarter of 2011, our board of directors authorized, and we declared, the payment of accrued and unpaid dividends through September 30, 2011, and dividends for the quarter ended December 31, 2011, (collectively, the Unpaid Dividends), and a sum sufficient for the payment of the Unpaid Dividends, has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. However, the Unpaid

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Dividends are not payable until June 29, 2012, are payable to holders of record as of the close of business on June 15, 2012 and are contingent upon our ability to meet, on the June 29, 2012 Unpaid Dividends payment date, the Maryland Dividend Requirement. In addition, in February 2012, our board of directors authorized, and we declared, preferred dividends for the quarter ending March 31, 2012, payable on June 29, 2012, to holders of record as of the close of business on June 15, 2012, contingent upon our ability to meet the Maryland Dividend Requirement on such payment date. A sum sufficient for the payment of the preferred dividends for the quarter ending March 31, 2012 has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. The board of directors will continue to evaluate the dividend policy in light of the REIT provisions of the Tax Code, restrictions under the bank credit facility, and the overall economic climate.

In December 2011, we completed tender offers to purchase a portion of our outstanding Preferred Stock. We tendered approximately 0.3 million shares of our 8.50% Series A Cumulative Redeemable Preferred Stock for a purchase price of \$26.70 per share, 1.0 million shares of our 8.25% Series B Cumulative Redeemable Preferred Stock for a purchase price of \$26.50 per share, and 1.9 million shares of our 8.25% Series C Cumulative Redeemable Preferred Stock for a purchase price of \$26.50 per share. We paid the holders approximately \$86.1 million in cash, which was without interest or accrued and unpaid dividends.

Capital expenditures for the years ended December 31, 2011, 2010 and 2009 amounted to \$49.8 million, \$33.0 million and \$75.4 million, respectively. Included in the 2011, 2010 and 2009 amounts were \$1.1 million, \$0.7 million and \$1.7 million of capitalized interest, respectively. For the year ending December 31, 2012, we expect to spend approximately \$35.0 million on hotel property and equipment replacement projects in accordance with hotel management or lease agreements and approximately \$30.0 million to \$40.0 million on owner-funded projects, subject to adjustments based on continued evaluation.

Bank credit facility. On June 30, 2011, we entered into a \$300.0 million secured bank credit facility agreement. The agreement contains an accordion feature allowing for additional borrowing capacity up to \$400.0 million, subject to the satisfaction of customary conditions set forth in the agreement. The following summarizes key financial terms and conditions of the bank credit facility:

interest on the facility is payable monthly at LIBOR plus an applicable margin in the case of each LIBOR loan and base-rate plus an applicable margin in the case of each base rate loan whereby the applicable margins are dependent on the ratio of consolidated debt to gross asset value (Leverage Ratio) as follows:

Leverage Ratio	Applicable Margin of each LIBOR Loan (% per annum)	Applicable Margin of each Base Rate Loan (% per annum)
Greater than or equal to 60%	3.75%	2.75%
Greater than or equal to 55% but less than 60%	3.50%	2.50%
Greater than or equal to 50% but less than 55%	3.25%	2.25%
Greater than or equal to 45% but less than 50%	3.00%	2.00%
Less than 45%	2.75%	1.75%

an unused commitment fee is payable monthly based on the unused revolver balance at a rate of 0.45% per annum in the event that the bank credit facility usage is less than 50% and a rate of 0.25% per annum in the event that the bank credit facility usage is equal to or greater than 50%;

maturity date of June 30, 2014, with the right to extend the maturity date for an additional one-year period with an extension fee equal to 25 basis points, subject to certain conditions;

lenders received collateral in the form of mortgages over four borrowing base properties, which initially include the Ritz-Carlton Laguna Niguel hotel, the Ritz-Carlton Half Moon Bay hotel, the Four Seasons Punta Mita Resort, and the Marriott Lincolnshire Resort, in addition to pledges of the Company's interest in SH Funding and SH Funding's interest in certain subsidiaries and guarantees of the loan from the Company and certain of its subsidiaries;

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maximum availability is determined by the lesser of 60% advance rate against the appraised value of the borrowing base properties (provided at any time the total fixed charge coverage ratio is less than 1.25 times, the percentage shall be reduced to 55%) or a 1.20 times debt service coverage on the borrowing base properties (based on the trailing 12 months net operating income for these assets divided by the greater of the in-place interest rate or 7.0% debt constant on the balance outstanding under the bank credit facility) provided not more than 40% of aggregate appraised value and 40% of trailing 12 month net operating income is attributable to borrowing base properties located outside the United States;

minimum corporate fixed charge coverage of 1.00 times from the closing date through the fourth quarter of 2012, 1.10 times through 2013, 1.20 times from the first quarter of 2014 through the initial maturity date, and 1.30 times during the extension year, which will permanently increase to 1.35 times if cash dividends are reinstated on our common stock;

maximum corporate leverage of 65% during the initial term and 60% during any extension period;

minimum tangible net worth of \$700.0 million, excluding goodwill and currency translation adjustments, plus an amount equal to 75% of the net proceeds of any new issuances of our common stock, which is not used to reduce indebtedness or used in a transaction or series of transactions to redeem outstanding capital stock;

restrictions on SHR and SH Funding's ability to pay dividends. Such restrictions include:

prohibitions on SHR and SH Funding and their respective subsidiaries' ability to pay any dividends unless certain ratios and other conditions are met; and

prohibitions on SHR and SH Funding's ability to issue dividends in cash or in kind at any time an event of default shall have occurred.

Notwithstanding the dividend restrictions described above, for so long as the Company qualifies, or has taken all other actions necessary to qualify as a REIT, SH Funding may authorize, declare, and pay quarterly cash dividends to the Company when and to the extent necessary for the Company to distribute cash dividends to its shareholders generally in an aggregate amount not to exceed the minimum amount necessary for the Company to maintain its tax status as a REIT, unless certain events of default exist. In addition, provided no event of default exists, dividends on Preferred Stock that accrue with regard to the current fiscal quarter may be paid to holders of Preferred Stock. Additionally, provided no event of default exists, the Company is permitted to pay the outstanding cumulative accrued but unpaid preferred dividends at any time on or prior to June 30, 2012. Subsequent to June 30, 2012, provided no event of default exists, the Company is permitted to pay the outstanding cumulative accrued but unpaid preferred dividends subject to certain conditions set forth in the bank credit facility agreement.

Other terms and conditions exist including provisions to release assets from the borrowing base and limitations on our ability to incur costs for discretionary capital programs and redeem, retire or repurchase common stock. Under the agreement, SH Funding has a letter of credit sub-facility of \$75.0 million, which is secured by the \$300.0 million bank credit facility. Letters of credit reduce the borrowing capacity under the bank credit facility.

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Mortgages and other debt payable. The following table summarizes our outstanding debt and scheduled maturities, including extension options, related to mortgages and other debt payable as of December 31, 2011 (in thousands):

	Balance as of December 31, 2011	2012	2013	2014	2015	2016	Thereafter
Mortgages payable							
Hyatt Regency La Jolla, LIBOR plus 1.00%	\$ 97,500	\$ 97,500	\$	\$	\$	\$	\$
Marriott London Grosvenor Square, 3-month GBP LIBOR plus 1.10%(1)	113,659	3,202	110,457				
Four Seasons Washington, D.C., LIBOR plus 3.15%(1)(2)	130,000					130,000	
Fairmont Chicago, 6.09%(1)	97,750	2,583	2,745	2,917	3,099	3,294	83,112
Westin St. Francis, 6.09%(1)	220,000	5,814	6,178	6,564	6,976	7,413	187,055
Loews Santa Monica Beach Hotel, LIBOR plus 3.85%(1)(2)	110,000		1,000	2,000	2,000	2,000	103,000
InterContinental Miami, LIBOR plus 3.50%(1)(2)	85,000			422	889	952	82,737
InterContinental Chicago, 5.61%(1)(2)	145,000		943	1,969	2,082	2,202	137,804
Total mortgages payable	998,909	109,099	121,323	13,872	15,046	145,861	593,708
Other debt, 5.00%(3)	1,476		1,476				
Total mortgages and other debt payable	\$ 1,000,385	\$ 109,099	\$ 122,799	\$ 13,872	\$ 15,046	\$ 145,861	\$ 593,708

- (1) These loan agreements require maintenance of financial covenants, all of which we were in compliance with at December 31, 2011.
- (2) In July 2011, we refinanced or executed mortgage loans related to these hotels. See Item 8. Financial Statements and Supplementary Data 9. Indebtedness *Mortgages and Other Debt Payable* for further details related to these mortgage loans.
- (3) The North Beach Venture (see Off-Balance Sheet Arrangements *Hotel and North Beach Ventures*) assumed the mortgage loan on a hotel-condominium unit, which is secured by the hotel-condominium unit.

Our long-term liquidity requirements consist primarily of funds necessary to pay for scheduled debt maturities, renovations, expansions and other non-recurring capital expenditures that need to be made periodically to our properties and the costs associated with acquisitions of properties. In addition, we may use cash to buy back outstanding debt or common or preferred securities from time to time when market conditions are favorable through open market purchases, privately negotiated transactions, or a tender offer, although the terms of our bank credit facility may impose certain conditions or restrictions in connection therewith.

Historically, we have satisfied our long-term liquidity requirements through various sources of capital, including our existing working capital, cash provided by operations, sales of properties, long-term property mortgage indebtedness, bank credit facilities, issuance of senior unsecured debt instruments and through the issuance of additional equity securities. Credit markets have improved and access to mortgage and corporate level debt is more readily available. However, the capital markets continue to be fragile and there are no guarantees our maturing debt will be readily refinanced. Our ability to raise funds through the issuance of equity securities is dependent upon, among other things, general market conditions for both REITs in general and us specifically, including market perceptions regarding the Company.

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On May 19, 2010, we completed a public offering of 75.9 million shares of common stock at a price of \$4.60 per share and raised net proceeds of approximately \$331.8 million. In addition, on March 11, 2011, we issued 8.0 million shares of common stock in a private placement at a price of \$6.25 per share and raised net proceeds of approximately \$49.7 million and concurrently issued 15.2 million shares of common stock at a price of \$6.08 based on our March 11, 2011 common share closing price to acquire the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels for \$92.4 million. On June 9, 2011, we completed a recapitalization of the Fairmont Scottsdale Princess hotel, whereby we contributed the assets and liabilities of the hotel and cash of \$34.9 million in exchange for a 50% ownership interest in the Fairmont Scottsdale Princess Venture. On June 24, 2011, we acquired the remaining 49% interest in the InterContinental Chicago hotel and an additional 2.5% ownership interest in the Hyatt Regency La Jolla hotel for total consideration of approximately \$90.2 million, which included the issuance of an aggregate of approximately 10.8 million shares of common stock at a price of \$6.51 per share based on our June 24, 2011 common share closing price, approximately \$19.4 million of cash, which includes working capital, and post-closing adjustments of \$0.5 million.

We will continue to analyze which source of capital is most advantageous to us at any particular point in time, but equity and debt financing may not be consistently available to us on terms that are attractive or at all.

Equity Securities

As of December 31, 2011, we had 1,836,041 RSUs outstanding, of which 524,115 were vested. In addition, as of December 31, 2011, we had 669,797 options to purchase shares of our common stock (Options) outstanding.

The following table presents the changes in our issued and outstanding shares of common stock and SH Funding operating partnership units (OP Units) since December 31, 2010 (excluding RSUs):

	Common Shares	OP Units Represented by Noncontrolling Interests	Total
Outstanding at December 31, 2010	151,305,314	954,571	152,259,885
RSUs redeemed for shares of our common stock	221,929		221,929
OP Units redeemed for shares of our common stock	101,110	(101,110)	
Common stock issued	33,998,846		33,998,846
Outstanding at December 31, 2011	185,627,199	853,461	186,480,660

Cash Flows

Operating Activities. Net cash provided by operating activities was \$75.7 million, \$81.3 million and \$46.6 million for the years ended December 31, 2011, 2010 and 2009, respectively. Cash flows from operations decreased from 2010 to 2011 primarily due to higher cash interest payments in 2011 when compared to 2010 and working capital changes, partially offset by an increase in hotel operating income in 2011 when compared to 2010. Cash flows from operations increased from 2009 to 2010 primarily due to an overall increase in operating income and a decrease in cash paid for interest as a result of the interest rate swap buy down transactions.

Investing Activities. Net cash used in investing activities was \$61.6 million and \$45.0 million for the years ended December 31, 2011 and 2010, respectively, compared to net cash provided by investing activities of \$66.3 million for the year ended December 31, 2009. The significant investing activities during these years are summarized below:

We sold our 50.0% interest in BuyEfficient for \$9.0 million during the year ended December 31, 2011.

We sold our leasehold interest in the Paris Marriott hotel during the year ended December 31, 2011 for \$58.0 million.

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We acquired unrestricted cash of \$30.6 million through the recapitalization of the Hotel and North Beach Ventures and acquisition of the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels during the year ended December 31, 2011.

We paid \$93.8 million related to the recapitalization of the Hotel and North Beach Ventures and the Fairmont Scottsdale Princess Venture during the year ended December 31, 2011.

We sold the InterContinental Prague hotel during the year ended December 31, 2010 for net sales proceeds of \$3.6 million and the Four Seasons Mexico City and Renaissance Paris hotels during the year ended December 31, 2009 for net sales proceeds of \$52.2 million and \$50.3 million, respectively.

We received a payment on a promissory note from the purchaser of the Hyatt Regency New Orleans hotel of \$1.9 million during the year ended December 31, 2010.

We sold two apartment buildings associated with the InterContinental Prague hotel for net sales proceeds of \$6.6 million during the year ended December 31, 2009.

We received \$10.1 million of cash from our investments in unconsolidated affiliates during the year ended December 31, 2009.

In 2009, we received a return of \$3.8 million of a deposit made in connection with a potential hotel acquisition.

We disbursed \$49.8 million, \$33.0 million and \$75.4 million during the years ended December 31, 2011, 2010 and 2009, respectively, for capital expenditures primarily related to room renovations and food and beverage facilities.

Restricted cash and cash equivalents increased by \$9.9 million and \$15.2 million during the years ended December 31, 2011 and 2010, respectively. Restricted cash and cash equivalents decreased by \$14.5 million during the year ended December 31, 2009.

Financing Activities. Net cash used in financing activities was \$22.9 million, \$66.8 million and \$78.8 million for the years ended December 31, 2011, 2010 and 2009, respectively. The significant financing activities during these years are summarized below:

We paid approximately \$87.8 million for the repurchase of a portion of our outstanding Preferred Stock during the year ended December 31, 2011.

We purchased the remaining 49% interest in the InterContinental Chicago hotel and an additional 2.5% interest in the Hyatt Regency La Jolla hotel for common stock and cash of \$19.5 million during the year ended December 31, 2011.

We received proceeds from a private placement and common stock offering, net of offering costs, of approximately \$49.2 million and \$331.8 million during the years ended December 31, 2011 and 2010, respectively.

During the year ended December 31, 2011, we had net borrowings of \$22.0 million on our bank credit facility. During the years ended December 31, 2010 and 2009, we made net payments of \$150.0 million and \$28.0 million, respectively, on our bank credit facility.

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During the year ended December 31, 2011, we received net proceeds of \$61.0 million on mortgages and other debt. During the year ended December 31, 2010, we made payments of \$32.5 million on mortgages and other debt.

We paid \$33.3 million, \$35.2 million and \$37.2 million to terminate and buy down interest rate swaps during the years ended December 31, 2011, 2010 and 2009, respectively.

During the years ended December 31, 2011, 2010 and 2009, we paid financing costs of \$12.5 million, \$0.2 million and \$8.3 million, respectively.

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During the year ended December 31, 2010, we tendered the outstanding Exchangeable Notes for \$180.0 million.

We paid distributions to the noncontrolling interest holders in our consolidated affiliates in the amount of \$1.3 million and \$4.8 million for the years ended December 31, 2011 and 2009, respectively.

Dividend Policy

We generally intend to distribute each year substantially all of our taxable income (which does not necessarily equal net income as calculated in accordance with GAAP) to our shareholders so as to comply with REIT provisions of the Tax Code. If necessary for REIT qualification purposes, we may need to distribute any taxable income in cash or by a special dividend. Our dividend policy is subject to revision at the discretion of our board of directors. All distributions will be made at the discretion of our board of directors and will depend on our taxable income, our financial condition, our maintenance of REIT status and other factors as our board of directors deems relevant.

In the fourth quarter of 2011, our board of directors authorized, and we declared, the payment of the Unpaid Dividends, and a sum sufficient for the payment of the Unpaid Dividends has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. However, the Unpaid Dividends are not payable until June 29, 2012, are payable to holders of record as of the close of business on June 15, 2012 and are contingent upon our ability to meet, on the June 29, 2012 Unpaid Dividends payment date, the Maryland Dividend Requirement. In addition, in February 2012, our board of directors authorized, and we declared, preferred dividends for the quarter ending March 31, 2012, payable on June 29, 2012, to holders of record as of the close of business on June 15, 2012, contingent upon our ability to meet the Maryland Dividend Requirement on such payment date. A sum sufficient for the payment of the preferred dividends for the quarter ending March 31, 2012 has been set apart for payment through the recording of a distribution payable in accordance with the terms of our charter. Our board of directors has continued the suspension of the quarterly dividend to holders of shares of our common as a measure to preserve liquidity due to the uncertainty in the economic environment and no projected taxable distribution requirement. Based on our current forecasts, we would not be required to make any distributions during 2012 in order to maintain our REIT status. The board of directors continues to evaluate the dividend policy in light of the REIT provisions of the Tax Code, restrictions under the bank credit facility, and the overall economic climate.

Contractual Obligations

The following table summarizes our future payment obligations and commitments as of December 31, 2011 (in thousands):

	Payments Due by Period				
	Total	Less than 1 year ⁽¹⁾	1 to 3 years	4 to 5 years	More than 5 years
Long-term debt obligations ⁽²⁾	\$ 1,050,385	\$ 109,099	\$ 201,717	\$ 421,378	\$ 318,191
Interest on long-term debt obligations ⁽³⁾	333,401	70,132	174,478	57,599	31,192
Operating lease obligations - ground leases and office space	9,282	683	2,141	1,347	5,111
Operating leases - Marriott Hamburg	87,611	4,736	14,207	9,471	59,197
Construction contracts	3,260	3,260			
Total	\$ 1,483,939	\$ 187,910	\$ 392,543	\$ 489,795	\$ 413,691

(1) These amounts represent obligations that are due within fiscal year 2012.

(2) Long-term debt obligations include our mortgages and other debt and bank credit facility. Maturity dates assume all extension options are exercised, including conditional options.

(3) Interest on variable-rate debt obligations is calculated based on the variable rates at December 31, 2011 and includes the effect of our interest rate swaps.

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Reserve Funds for Capital Expenditures

We maintain each of our hotels in excellent condition and in conformity with applicable laws and regulations and in accordance with the agreed upon requirements in our management agreements with our preferred operators.

We are obligated to maintain reserve funds for capital expenditures at the majority of our hotels (including the periodic replacement or refurbishment of furniture, fixtures and equipment) as determined pursuant to the management agreements with our preferred operators. As of December 31, 2011, \$19.1 million was in restricted cash reserves for future capital expenditures. Generally, our agreements with hotel operators require us to reserve funds at amounts ranging between 4.0% and 5.0% of the individual hotel's annual revenues and require the funds to be set aside in restricted cash. Expenditures are capitalized as incurred and depreciation begins when the related asset is placed in service. Any unexpended amounts will remain our property upon termination of the management and operating contracts.

Off-Balance Sheet Arrangements

Fairmont Scottsdale Princess Venture

On June 9, 2011, we completed a recapitalization of the Fairmont Scottsdale Princess hotel. We entered into agreements with an unaffiliated third party, an affiliate of Walton Street Capital, L.L.C. (Walton Street), to form FMT Scottsdale Holdings, L.L.C. and Walton/SHR FPH Holdings, L.L.C. (together, the Fairmont Scottsdale Princess Venture) to own the Fairmont Scottsdale Princess hotel. We contributed the assets and liabilities of the hotel and cash of approximately \$34.9 million in exchange for a 50% ownership interest in the Fairmont Scottsdale Princess Venture and now account for our investment under the equity method of accounting. We jointly control the venture with Walton Street and serve as the managing member. We also continue to serve as the hotel's asset manager and earn a quarterly base management fee equal to 1.0% of total revenues during years one and two following the formation of the Fairmont Scottsdale Princess Venture, 1.25% of total revenues during years three and four, and 1.5% of total revenues thereafter, as well as certain project management fees. In connection with the Fairmont Scottsdale Princess Venture, we are entitled to certain promote payments after Walton Street achieves a specified return.

As part of the recapitalization, the Fairmont Scottsdale Princess Venture retired the hotel's \$40.0 million mezzanine debt. In addition, the hotel's \$140.0 million first mortgage was amended and extended. The amendment included a \$7.0 million principal payment and the debt was extended through December 2013 with an option for a second extension through April 9, 2015, subject to certain conditions. Interest remains payable monthly at LIBOR plus 0.36%. Our investment in the Fairmont Scottsdale Princess Venture amounted to \$27.4 million as of December 31, 2011. Our equity in losses of the Fairmont Scottsdale Princess Venture was \$5.7 million for the year ended December 31, 2011.

Hotel and North Beach Ventures

Prior to February 4, 2011, we had a 45.0% ownership interest in the Hotel Venture, the then owner of the Hotel del Coronado in San Diego, California, and the North Beach Venture, the owner of an adjacent residential condominium-hotel development. We accounted for our investments in the Hotel and North Beach Ventures under the equity method of accounting. Our investment in the Hotel and North Beach Ventures amounted to \$7.8 million as of December 31, 2010. We recognized equity in (losses) earnings related to the Hotel and North Beach Ventures of \$(0.5) million for the period from January 1, 2011 through February 3, 2011 and \$12.2 million for the year ended December 31, 2010. We earned asset management, development and financing fees under agreements with the Hotel and North Beach Ventures. We recognized income of 55.0% of these fees, representing the percentage of the Hotel and North Beach Ventures not owned by us.

The Hotel Venture obtained \$610.0 million of non-recourse mortgage and mezzanine debt financings and a \$20.0 million non-recourse revolving credit facility, which were secured by, among other things, a mortgage on

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the Hotel del Coronado. In December 2010, the Hotel Venture purchased a \$37.5 million mezzanine layer of the debt structure for a discounted payoff of \$13.0 million. The remaining principal on the mortgage and mezzanine debt financings and revolving credit facility had a maturity date of January 7, 2011. On January 7, 2011, the Hotel Venture obtained an extension of the maturity date to February 9, 2011.

Hotel del Coronado Venture

On February 4, 2011, the Hotel and North Beach Ventures completed a recapitalization (the Transaction) through a series of contemporaneous transactions. Under the terms of the Transaction, we acquired the ownership interest of an existing member of the Hotel and North Beach Ventures, and, along with the remaining members of the Hotel Venture, formed a partnership, BSK Del Partners, L.P. (Hotel del Coronado Venture) with an unaffiliated third party, an affiliate of Blackstone Real Estate Advisors VI L.P. (Blackstone), to own the Hotel del Coronado. As part of the Transaction, we contributed \$57.4 million of cash drawn from our bank credit facility to fund our contribution. This payment included the purchase of the existing member's ownership in the Hotel and North Beach Ventures and is net of a \$1.7 million financing fee earned as part of the Transaction. The Hotel Venture contributed substantially all of the assets and liabilities to the Hotel del Coronado Venture. The Hotel del Coronado Venture then settled all contributed debts outstanding by paying balances off in full or agreeing to convert debt to equity. In connection with the Transaction, we also acquired our partner's interest in HdC DC Corporation, a taxable corporation, with assets of \$25.6 million and an existing deferred tax liability of approximately \$48.6 million. As a result of the Transaction, we recorded an equity method investment of \$97.6 million. Pursuant to the terms of the Transaction, Blackstone is the general partner of the Hotel del Coronado Venture with a 60.0% ownership interest and we are a limited partner with an indirect 34.3% ownership interest. Our investment in the Hotel del Coronado Venture amounted to \$94.9 million as of December 31, 2011. Our equity in losses of the Hotel del Coronado Venture was \$2.9 million for the year ended December 31, 2011.

The Hotel del Coronado Venture secured \$425.0 million of five-year debt financing at a weighted average rate of LIBOR plus 480 basis points, subject to a 1.0% LIBOR floor. After the third year of the loan, the final two one-year extensions require payment to the lender of a 25 basis point extension fee. Additionally, the Hotel del Coronado Venture purchased a two-year 2.0% LIBOR cap, which was required by the loan.

We continue to act as asset manager and earn a quarterly asset management fee equal to 1.0% of gross revenue, certain development fees, and when applicable, an incentive fee equal to one-third of the incentive fee paid to the hotel operator under the hotel management agreement. As part of the Hotel del Coronado Venture with Blackstone, the remaining members of the Hotel Venture earn a profit-based incentive fee of 20.0% of all distributions of the Hotel del Coronado Venture that exceed both a 20.0% internal rate of return and two times return on invested equity.

Four Seasons RCPM

We own a 31.0% interest in and act as asset manager for a venture with two unaffiliated parties that is developing the Four Seasons RCPM, a luxury vacation home product sold in fractional ownership interests on the property adjacent to our Four Seasons Punta Mita Resort hotel in Mexico. We account for this investment under the equity method of accounting. At December 31, 2011 and December 31, 2010, our investment in the unconsolidated affiliate amounted to \$3.8 million and \$3.9 million, respectively. Our equity in (losses) earnings of the unconsolidated affiliate was \$(0.1) million and \$0.3 million for the years ended December 31, 2011 and 2010, respectively.

BuyEfficient

We owned a 50.0% interest in an electronic purchasing platform venture called BuyEfficient with an unaffiliated third party. This platform allows members to procure food, operating supplies, furniture, fixtures and equipment. We accounted for this investment under the equity method of accounting. At December 31, 2010, our

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investment in the unconsolidated affiliate amounted to \$6.3 million. Our equity in earnings of the unconsolidated affiliate was \$0.6 million for the year ended December 31, 2010. On January 21, 2011, we sold our 50.0% interest in this venture for \$9.0 million.

Related Party Transactions

We have in the past engaged in and currently engage in transactions with related parties. See Item 8. Financial Statements and Supplementary Data 15. Related Party Transactions for a discussion of our transactions with related parties.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses and related disclosure of contingent assets and liabilities.

We evaluate our estimates on an ongoing basis. We base our estimates on historical experience, information that is currently available to us and on various other assumptions that we believe are reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. We believe the following critical accounting policies affect the most significant judgments and estimates used in the preparation of our consolidated financial statements.

Impairment

Investment in Hotel Properties (Long-Lived Assets). We review our long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment recognized is measured by the amount by which the carrying amount of the assets exceeds the estimated fair value of the assets. In our analysis of fair value, we use discounted cash flow analysis to estimate the fair value of our properties taking into account each property's expected cash flow from operations, holding period and proceeds from disposing of the property. In addition to the discounted cash flow analysis, management also considers external independent appraisals to estimate fair value. The analysis and appraisals used by management are consistent with those used by a market participant. The factors addressed in determining estimated proceeds from disposition include anticipated operating cash flow in the year of disposition, terminal capitalization rate and selling price per room. Judgment is required in determining the discount rate applied to estimated cash flows, growth rate of the properties, the need for capital expenditures, as well as specific market and economic conditions. Additionally, the classification of assets as held for sale requires the recording of assets at their net realizable value which can affect the amount of impairment recorded.

There were no indicators of potential impairment during the year ended December 31, 2011. However, if deterioration in economic and market conditions occurs, it may present a potential for impairment charges on our hotel properties subsequent to December 31, 2011. Any such adjustments could be material, but will be non-cash.

Intangible Assets. Intangible assets are reviewed for impairment whenever circumstances or events indicate potential impairment, as part of our investment in hotel properties impairment process described above.

There were no indicators of potential impairment during the year ended December 31, 2011. However, if deterioration in economic and market conditions occurs, it may present a potential for impairment charges on our intangible assets subsequent to December 31, 2011. Any such adjustments could be material, but will be non-cash.

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Goodwill. We review goodwill for impairment at least annually as of December 31 and whenever circumstances or events indicate potential impairment. Goodwill has an indefinite useful life that should not be amortized but should be reviewed annually for impairment, or more frequently if events or changes in circumstances indicate that goodwill might be impaired. The measurement of impairment of goodwill consists of two steps. In the first step, we compare the fair value of each reporting unit, which in our case is each hotel property, to its carrying value. In the second step of the impairment test, the impairment loss is determined by comparing the implied fair value of goodwill to the recorded amount of goodwill. The activities in the second step include hypothetically allocating the fair value of the reporting unit used in step one to all of the assets and liabilities, including all intangible assets, even if no intangible assets are currently recorded, of that reporting unit as if the reporting unit had been acquired in a business combination and the fair value of the reporting unit was the price paid to acquire the reporting unit. For reporting units with zero or negative carrying values, the second step is only performed if qualitative factors indicate that it is more likely than not that a goodwill impairment exists.

We performed our annual impairment test for goodwill as of December 31, 2011. We did not record any non-cash goodwill impairment charges for the year ended December 31, 2011 based on the outcome of this test. However, if deterioration in economic and market conditions occurs, it may present a potential for impairment charges on our hotel properties with goodwill subsequent to December 31, 2011. Any such adjustments could be material, but will be non-cash.

Investment in Unconsolidated Affiliates. A series of operating losses of an investee or other factors may indicate that a decrease in value of a company's investment in unconsolidated affiliates has occurred which is other-than-temporary. Accordingly, the investment in each of the unconsolidated affiliates is evaluated periodically and as deemed necessary for recoverability and valuation declines that are other-than-temporary. If the investment is other than temporarily impaired, the investment is written down to its estimated fair value. Also taken into consideration when testing for impairment is the value of the underlying real estate investments, the ownership and distribution preferences and limitations and rights to sell and repurchase of its ownership interests. There were no other-than-temporary declines in value of investments in unconsolidated affiliates during the year ended December 31, 2011. However, if deterioration in economic and market conditions occurs, it may present a potential for other-than-temporary declines in value subsequent to December 31, 2011. Any such adjustments could be material, but will be non-cash.

Acquisition Related Assets and Liabilities. Accounting for the acquisition of a hotel property as a purchase transaction requires an allocation of the purchase price to the assets acquired and the liabilities assumed in the transaction at their respective estimated fair values. The most difficult estimations of individual fair values are those involving long-lived assets, such as property and equipment and intangible assets. We use all available information to make these fair value determinations and, for hotel acquisitions, engage an independent valuation specialist to assist in the fair value determination of the acquired long-lived assets. Due to inherent subjectivity in determining the estimated fair value of long-lived assets, we believe that the recording of acquired assets and liabilities is a critical accounting policy. We acquired the Four Seasons Silicon Valley and Four Seasons Jackson Hole hotels during the year ended December 31, 2011.

Depreciation and Amortization Expense. Depreciation expense is based on the estimated useful life of our assets. The life of the assets is based on a number of assumptions, including cost and timing of capital expenditures to maintain and refurbish the asset, as well as specific market and economic conditions. While management believes its estimates are reasonable, a change in the estimated lives could affect depreciation expense and net income or the gain or loss on the sale of any of the assets.

Derivative Instruments and Hedging Activities. Derivative instruments and hedging activities require management to make judgments on the nature of its derivatives and their effectiveness as hedges. These judgments determine if the changes in fair value of the derivative instruments are reported in our

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consolidated statements of operations as a component of net income or as a component of comprehensive income and as a component of equity on our consolidated balance sheets. While management believes its judgments are reasonable, a change in a derivative's effectiveness as a hedge could affect expenses, net income and equity.

If the notional amount of the derivative instruments exceeds the forecasted LIBOR-based debt, an over-hedged position results. To alleviate the over-hedged position, the derivative instruments may be terminated and/or de-designated as hedges. Future changes to our overall floating rate debt could have implications to our overall hedging position. In February 2011, we paid \$4.2 million to terminate three interest rate swaps with a combined notional amount of \$125.0 million. There were no immediate charges to earnings in February 2011 based on our forecasted levels of LIBOR-based debt at the time of the transaction. In June 2011, we paid \$29.7 million to terminate five interest rate swaps with a combined notional amount of \$300.0 million. We also de-designated one interest rate swap with a notional amount of \$100.0 million as a cash flow hedge. We recorded a charge of \$29.2 million, which included the immediate write-off of \$27.4 million previously recorded in accumulated OCL related to interest rate swaps that were designated to hedge cash flows that are no longer probable of occurring and \$1.8 million of mark to market adjustments related to the terminated interest rate swaps. The charge was recorded in loss on early termination of derivative financial instruments in the consolidated statements of operations for the year ended December 31, 2011. Changes in the market value of the de-designated interest rate swap will be recorded in earnings subsequent to the de-designation. Depending on the capital markets and the availability of floating rate debt, the remaining swap portfolio may need to be reassessed in the future for additional terminations.

Disposal of Long-Lived Assets. We classify assets as held for sale in accordance with GAAP. Assets identified as held for sale are reclassified on our balance sheet and the related results of operations are reclassified as discontinued operations on our statement of operations. While these classifications do not have an effect on total assets, net equity or net income, they affect the classifications within each statement. Additionally, a determination to classify an asset as held for sale affects depreciation expense as long-lived assets are not depreciated while classified as held for sale.

Seasonality

The lodging business is seasonal in nature, and we experience some seasonality in our business. Revenues for hotels in tourist areas, those with significant group business, and in areas driven by greater climate changes are generally seasonal. Quarterly revenues also may be adversely affected by events beyond our control, such as extreme weather conditions and other acts of nature, terror attacks or alerts, airline strikes, economic factors and other considerations affecting travel.

The Marriott domestic hotels report their results of operations using a fiscal year consisting of thirteen four-week periods. As a result, for our domestic Marriott branded property, for all years presented, the first three quarters consist of 12 weeks each and the fourth quarter consists of 16 weeks.

To the extent that cash flows from operations are insufficient during any quarter, due to temporary or seasonal fluctuations in revenues, we may have to enter into short-term borrowings to pay operating expenses and make distributions to our stockholders.

New Accounting Guidance

In September 2011, the Financial Accounting Standards Board (FASB) amended its guidance on the testing of goodwill impairment to allow an entity the option to first assess qualitative factors to determine whether the current two-step process is necessary. Under the amended guidance, the calculation of the reporting unit's fair value (step one of the goodwill impairment test) is not required unless, as a result of the qualitative assessment, it is more likely than not that the fair value of the reporting unit is less than the unit's carrying amount. If it is not

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more likely than not that the fair value of the reporting unit is less than the carrying amount, further testing of goodwill for impairment would not be performed. The amendment is effective for fiscal years and interim periods within such years beginning after December 15, 2011, which for us will be our 2012 first quarter, with early adoption permitted. The adoption of this guidance is not expected to have a material impact on our financial statements.

In June 2011, the FASB issued new guidance that amends current comprehensive income guidance. The new guidance eliminates the option to present the components of other comprehensive income as part of the statement of shareholders' equity. Instead, we must report comprehensive income in either a single continuous statement of comprehensive income which contains two sections, net income and other comprehensive income, or in two separate but consecutive statements. Additionally, the guidance requires an entity to present on the face of the financial statements reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement(s) where the components of net income and the components of other comprehensive income are presented. We adopted the new guidance on January 1, 2012, except for the presentation requirements for reclassification adjustments, which has been deferred indefinitely. The adoption of the new guidance will not have a material impact on our financial statements.

In December 2010, the FASB issued new guidance that amends the criteria for performing the second step of the goodwill impairment test (described above) for reporting units with zero or negative carrying amounts and requires performing the second step if qualitative factors indicate that it is more likely than not that a goodwill impairment exists. We adopted the new guidance on January 1, 2011. The new guidance did not have a material impact on our financial statements.

Non-GAAP Financial Measures

We present five non-GAAP financial measures that we believe are useful to management and investors as key measures of our operating performance: FFO; FFO Fully Diluted; Comparable FFO; EBITDA; and Comparable EBITDA. Amounts presented in accordance with our definitions of FFO, FFO Fully Diluted, Comparable FFO, EBITDA, and Comparable EBITDA may not be comparable to similar measures disclosed by other companies, since not all companies calculate these non-GAAP measures in the same manner. FFO, FFO Fully Diluted, Comparable FFO, EBITDA, and Comparable EBITDA should not be considered as an alternative measure of our net income (loss) or operating performance. FFO, FFO Fully Diluted, Comparable FFO, EBITDA, and Comparable EBITDA may include funds that may not be available for our discretionary use due to functional requirements to conserve funds for capital expenditures and property acquisitions and other commitments and uncertainties. Although we believe that FFO, FFO Fully Diluted, Comparable FFO, EBITDA, and Comparable EBITDA can enhance the understanding of our financial condition and results of operations, these non-GAAP financial measures, when viewed individually, are not necessarily better indicators of any trend as compared to comparable GAAP measures such as net income (loss) attributable to SHR common shareholders. In addition, adverse economic and market conditions might negatively impact our cash flow. We have provided a quantitative reconciliation of FFO, FFO Fully Diluted, Comparable FFO, EBITDA, and Comparable EBITDA to the most directly comparable GAAP financial performance measure, which is net income (loss) attributable to SHR common shareholders.

EBITDA and Comparable EBITDA

EBITDA represents net income (loss) attributable to SHR common shareholders excluding: (i) interest expense, (ii) income taxes, including deferred income tax benefits and expenses applicable to our foreign subsidiaries and income taxes applicable to sale of assets; (iii) depreciation and amortization; and (iv) preferred stock dividends. EBITDA also excludes interest expense, income taxes and depreciation and amortization of our unconsolidated affiliates. EBITDA is presented on a full participation basis, which means we have assumed conversion of all redeemable noncontrolling interests of our operating partnership into our common stock. We believe this treatment of noncontrolling interests provides useful information for management and our investors.

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and appropriately considers our current capital structure. We also present Comparable EBITDA, which eliminates the effect of realizing deferred gains on our sale leasebacks, as well as the effect of gains or losses on sales of assets, early extinguishment of debt, impairment losses, foreign currency exchange gains or losses and certain other charges that are highly variable from year to year.

We believe EBITDA and Comparable EBITDA are useful to management and investors in evaluating our operating performance because they provide management and investors with an indication of our ability to incur and service debt, to satisfy general operating expenses, to make capital expenditures and to fund other cash needs or reinvest cash into our business. We also believe they help management and investors meaningfully evaluate and compare the results of our operations from period to period by removing the impact of our asset base (primarily depreciation and amortization) from our operating results. Our management also uses EBITDA and Comparable EBITDA as measures in determining the value of acquisitions and dispositions.

The following table provides a reconciliation of net loss attributable to SHR common shareholders to Comparable EBITDA (in thousands):

	Years Ended December 31,		
	2011	2010	2009
Net loss attributable to SHR common shareholders	\$ (23,688)	\$ (261,937)	\$ (274,831)
Depreciation and amortization continuing operations	112,062	130,601	130,955
Depreciation and amortization discontinued operations		5,980	13,307
Interest expense continuing operations	86,447	86,285	93,929
Interest expense discontinued operations		9,706	8,592
Income taxes continuing operations	970	1,408	3,344
Income taxes discontinued operations	379	476	(540)
Noncontrolling interests	(29)	(1,687)	(3,129)
Adjustments from consolidated affiliates	(6,733)	(7,609)	(9,460)
Adjustments from unconsolidated affiliates	23,221	15,563	15,934
Preferred shareholder dividends	18,482	30,886	30,886
EBITDA	211,111	9,672	8,987
Realized portion of deferred gain on sale leaseback continuing operations	(217)	(207)	(217)
Realized portion of deferred gain on sale leaseback discontinued operations	(1,214)	(4,465)	(4,685)
(Gain) loss on sale of assets continuing operations	(2,640)		477
Gain on sale of assets discontinued operations	(101,287)	(29,713)	(18,164)
Impairment losses and other charges continuing operations		141,858	99,740
Impairment losses and other charges discontinued operations			31,064
Impairment losses and other charges adjustments from consolidated affiliates			(169)
Loss on early extinguishment of debt continuing operations	1,237	925	883
Loss on early extinguishment of debt discontinued operations		95	
Loss on early termination of derivative financial instruments	29,242	18,263	
Gain on extinguishment of debt of unconsolidated affiliate		(11,025)	
Foreign currency exchange loss continuing operations	2	1,410	896
Foreign currency exchange (gain) loss discontinued operations	(51)	(7,392)	1,141
Adjustment for Value Creation Plan	18,607	12,614	108
Comparable EBITDA	\$ 154,790	\$ 132,035	\$ 120,061

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FFO, FFO-Fully Diluted, and Comparable FFO

We compute FFO in accordance with standards established by the National Association of Real Estate Investment Trusts, or NAREIT, with the exception of impairment of depreciable real estate. NAREIT adopted a definition of FFO in order to promote an industry-wide standard measure of REIT operating performance. NAREIT defines FFO as net income (loss) (computed in accordance with GAAP) excluding losses or gains from sales of depreciable property, impairment of depreciable real estate, real estate-related depreciation and amortization, and our portion of these items related to unconsolidated affiliates. We also present FFO Fully Diluted, which is FFO plus income or loss on income attributable to redeemable noncontrolling interests of our operating partnership. We also present Comparable FFO, which is FFO Fully Diluted excluding the impact of any gains or losses on early extinguishment of debt, impairment losses, foreign currency exchange gains or losses and certain other charges that are highly variable from year to year.

We believe that the presentation of FFO, FFO Fully Diluted and Comparable FFO provides useful information to management and investors regarding our results of operations because they are measures of our ability to fund capital expenditures and expand our business. In addition, FFO is widely used in the real estate industry to measure operating performance without regard to items such as depreciation and amortization.

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The following table provides a reconciliation of net loss attributable to SHR common shareholders to Comparable FFO (in thousands):

	Years Ended December 31,		
	2011	2010	2009
Net loss attributable to SHR common shareholders	\$ (23,688)	\$ (261,937)	\$ (274,831)
Depreciation and amortization continuing operations	112,062	130,601	130,955
Depreciation and amortization discontinued operations		5,980	13,307
Corporate depreciation	(1,141)	(1,217)	(1,217)
(Gain) loss on sale of assets continuing operations	(2,640)		477
Gain on sale of assets discontinued operations	(101,287)	(29,713)	(18,164)
Realized portion of deferred gain on sale leaseback continuing operations	(217)	(207)	(217)
Realized portion of deferred gain on sale leaseback discontinued operations	(1,214)	(4,465)	(4,685)
Deferred tax expense on realized portion of deferred gain on sale leasebacks	379	1,393	1,462
Noncontrolling interests adjustments	(575)	(1,159)	(1,928)
Adjustments from consolidated affiliates	(4,486)	(5,979)	(7,619)
Adjustments from unconsolidated affiliates	11,763	7,973	7,864
FFO	(11,044)	(158,730)	(154,596)
Redeemable noncontrolling interests	546	(528)	(1,201)
FFO Fully Diluted	(10,498)	(159,258)	(155,797)
Impairment losses and other charges continuing operations		141,858	99,740
Impairment losses and other charges discontinued operations			31,064
Impairment losses and other charges adjustments from consolidated affiliates			(169)
Non-cash mark to market of interest rate swaps continuing operations	(2,183)	9,014	
Non-cash mark to market of interest rate swaps discontinued operations		25	
Loss on early extinguishment of debt continuing operations	1,237	925	883
Loss on early extinguishment of debt discontinued operations		95	
Loss on early termination of derivative financial instruments	29,242	18,263	
Gain on extinguishment of debt of unconsolidated affiliate		(11,025)	
Foreign currency exchange loss continuing operations	2	1,410	896
Foreign currency exchange (gain) loss, net of tax discontinued operations	(51)	(7,421)	596
Adjustment for Value Creation Plan	18,607	12,614	108
Comparable FFO	\$ 36,356	\$ 6,500	\$ (22,679)

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.**Interest Rate Risk**

Our future income, cash flows and fair values relevant to financial instruments are dependent upon prevailing market interest rates. Market risk refers to the risk of loss from adverse changes in market prices and interest rates. The majority of our outstanding debt, after considering the effect of interest rate swaps, has a fixed interest rate. We use derivative financial instruments to manage, or hedge, interest rate risks related to our borrowings, from lines of credit to medium- and long-term financings. We generally require that hedging derivative instruments be effective in reducing the interest rate risk exposure that they are designed to hedge. We do not use derivatives for trading or speculative purposes and only enter into contracts with major financial

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institutions based on their credit rating and other factors. We use methods which incorporate standard market conventions and techniques such as discounted cash flow analysis and option pricing models to determine fair value. All methods of estimating fair value result in general approximation of value and such value may or may not actually be realized.

See Item 8. Financial Statements and Supplementary Data 11. Derivatives for information on our interest rate cap and swap agreements outstanding as of December 31, 2011.

As of December 31, 2011, our total outstanding mortgages and other debt and indebtedness under the bank credit facility totaled approximately \$1.05 billion, of which approximately 93.1% was fixed-rate debt when including the effect of interest rate swaps.

Currency Exchange Risk

As we have international operations, currency exchange risk arises as a normal part of our business. In particular, we are subject to fluctuations due to changes in foreign exchange rates in the British pound, euro and Mexican peso. We reduce this risk by transacting our international business in local currencies. In this manner, assets and liabilities are matched in the local currency, which reduces the need for dollar conversion. Generally, we do not enter into forward or option contracts to manage our currency exchange risk exposure applicable to net operating cash flows.

To manage the currency exchange risk applicable to equity positions in foreign hotels, we may use long-term mortgage debt denominated in the local currency. In addition, we may enter into forward or option contracts. We do not currently have any currency forward or option contracts.

Our exposure to foreign currency exchange rates relates primarily to our foreign hotels. For our foreign hotels, exchange rates impact the U.S. dollar value of our reported earnings, our investments in the hotels and the intercompany transactions with the hotels.

For the year ended December 31, 2011, approximately 9.9% of our total revenues, were generated outside of the United States, with approximately 4.8% of total revenues generated from the Marriott London Grosvenor Square (which uses the British pound), approximately 4.4% of total revenues generated from the Four Seasons Punta Mita Resort (which uses the Mexican peso), and approximately 0.7% of total revenues generated from the Marriott Hamburg (which uses the euro). As a result, fluctuations in the value of foreign currencies against the U.S. dollar may have a significant impact on our reported results. Revenues and expenses denominated in foreign currencies are translated into U.S. dollars at a weighted average exchange rate for the period. Consequently, as the value of the U.S. dollar changes relative to the currencies of these markets, our reported results vary.

If the U.S. dollar had strengthened an additional 10.0% during the year ended December 31, 2011, total revenues and operating income would have changed from the amounts reported by (in millions):

	Mexican Peso	British Pound	Euro	Total
Decrease in total revenues	\$ 3.4	\$ 3.7	\$ 0.5	\$ 7.6
Decrease in operating income	\$ 0.1	\$ 0.5	\$	\$ 0.6

Fluctuations in foreign currency exchange rates also impact the U.S. dollar amount of our shareholders' equity. The assets and liabilities of our non-U.S. hotels are translated into U.S. dollars at exchange rates in effect at the end of the period. The resulting translation adjustments are recorded in shareholders' equity as a component of accumulated other comprehensive loss. If the U.S. dollar had strengthened by 10.0% as of December 31, 2011, resulting translation adjustments recorded in shareholders' equity would have increased by approximately \$2.4 million from the amounts reported.

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**ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.
REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Shareholders of

Strategic Hotels & Resorts, Inc.

Chicago, Illinois

We have audited the accompanying consolidated balance sheets of Strategic Hotels & Resorts, Inc. and subsidiaries (the Company) as of December 31, 2011 and 2010, and the related consolidated statements of operations and comprehensive income (loss), equity, and cash flows for each of the three years in the period ended December 31, 2011. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the consolidated financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Strategic Hotels & Resorts, Inc. and subsidiaries as of December 31, 2011 and 2010, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2011, based on the criteria established in *Internal Control - Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated February 23, 2012 expressed an unqualified opinion on the Company's internal control over financial reporting.

/s/ DELOITTE & TOUCHE LLP

Chicago, Illinois

February 23, 2012

Table of Contents**STRATEGIC HOTELS & RESORTS, INC. AND SUBSIDIARIES (SHR)****CONSOLIDATED BALANCE SHEETS****(In Thousands, Except Share Data)**

	December 31,	
	2011	2010
Assets		
Investment in hotel properties, net	\$ 1,692,431	\$ 1,835,451
Goodwill	40,359	40,359
Intangible assets, net of accumulated amortization of \$8,915 and \$6,536	30,635	32,620
Assets held for sale		45,145
Investment in unconsolidated affiliates	126,034	18,024
Cash and cash equivalents	72,013	78,842
Restricted cash and cash equivalents	39,498	34,618
Accounts receivable, net of allowance for doubtful accounts of \$1,698 and \$1,922	43,597	35,250
Deferred financing costs, net of accumulated amortization of \$3,488 and \$15,756	10,845	3,322
Deferred tax assets	2,230	4,121
Prepaid expenses and other assets	29,047	34,564
Total assets	\$ 2,086,689	\$ 2,162,316
Liabilities, Noncontrolling Interests and Equity		
Liabilities:		
Mortgages and other debt payable	\$ 1,000,385	\$ 1,118,281
Bank credit facility	50,000	28,000
Liabilities of assets held for sale		93,206
Accounts payable and accrued expenses	249,179	270,703
Distributions payable	72,499	
Deferred tax liabilities	47,623	1,732
Total liabilities	1,419,686	1,511,922
Noncontrolling interests in SHR's operating partnership	4,583	5,050
Equity:		
SHR's shareholders' equity:		
8.50% Series A Cumulative Redeemable Preferred Stock (\$0.01 par value per share; 4,148,141 and 4,488,750 shares issued and outstanding; liquidation preference \$25.00 per share plus accrued distributions and \$130,148 and \$131,296 in the aggregate)	99,995	108,206
8.25% Series B Cumulative Redeemable Preferred Stock (\$0.01 par value per share; 3,615,375 and 4,600,000 shares issued and outstanding; liquidation preference \$25.00 per share plus accrued distributions and \$112,755 and \$133,975 in the aggregate)	87,064	110,775
8.25% Series C Cumulative Redeemable Preferred Stock (\$0.01 par value per share; 3,827,727 and 5,750,000 shares issued and outstanding; liquidation preference \$25.00 per share plus accrued distributions and \$119,377 and \$167,469 in the aggregate)	92,489	138,940
Common shares (\$0.01 par value per share; 250,000,000 common shares authorized; 185,627,199 and 151,305,314 common shares issued and outstanding)	1,856	1,513
Additional paid-in capital	1,634,067	1,553,286
Accumulated deficit	(1,190,621)	(1,185,294)
Accumulated other comprehensive loss	(70,652)	(107,164)
Total SHR's shareholders' equity	654,198	620,262
Noncontrolling interests in consolidated affiliates	8,222	25,082

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Total equity	662,420	645,344
Total liabilities, noncontrolling interests and equity	\$ 2,086,689	\$ 2,162,316

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

Table of Contents**STRATEGIC HOTELS & RESORTS, INC. AND SUBSIDIARIES (SHR)****CONSOLIDATED STATEMENTS OF OPERATIONS AND****COMPREHENSIVE INCOME (LOSS)****(In Thousands, Except Per Share Data)**

	For the years ended December 31,		
	2011	2010	2009
Revenues:			
Rooms	\$ 410,315	\$ 362,559	\$ 343,891
Food and beverage	267,194	238,762	216,982
Other hotel operating revenue	80,907	79,981	89,525
Lease revenue	5,422	4,991	4,858
Total revenues	763,838	686,293	655,256
Operating Costs and Expenses:			
Rooms	114,087	105,142	100,642
Food and beverage	192,028	171,279	160,252
Other departmental expenses	207,664	199,336	193,699
Management fees	24,719	22,911	23,386
Other hotel expenses	53,808	48,781	52,385
Lease expense	4,865	4,566	4,752
Depreciation and amortization	112,062	130,601	130,955
Impairment losses and other charges		141,858	99,740
Corporate expenses	39,856	&n	