HOST MARRIOTT CORP/
Form S-3
July 08, 2004
Table of Contents

As filed with the Securities and Exchange Commission on July 8, 2004

Registration No. 333-

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM S-3

REGISTRATION STATEMENT

UNDER

THE SECURITIES ACT OF 1933

HOST MARRIOTT CORPORATION

(Exact name of registrant as specified in its governing instrument)

Maryland	**53-0085950**
(State of Incorporation)	**(I.R.S. Employer Identification Number)**

6903 Rockledge Drive, Suite 1500

Bethesda, Maryland 20817

(240) 744-1000

(Address and telephone number of principal executive offices)

Elizabeth A. Abdoo, Esq.

Executive Vice President and General Counsel

Host Marriott Corporation

6903 Rockledge Drive, Suite 1500

Bethesda, Maryland 20817

(240) 744-1000

(Name, address and telephone number of agent for service)

Copies to:

Scott C. Herlihy, Esq.

LATHAM & WATKINS

555 11th Street, N.W. Suite 1000

Washington, DC 20004

(202) 637-2200

Approximate date of commencement of proposed sale to the public: From time to time after this registration statement becomes effective.

If the only securities being registered on this form are being offered pursuant to dividend or interest reinvestment plans, please check the following box. ¨

If any of the securities being registered on this form are to be offered on a delayed or continuous basis pursuant to Rule 415 under the Securities Act of 1933, other than securities offered only in connection with dividend or interest reinvestment plans, check the following box. x

If this form is filed to register additional securities for an offering pursuant to Rule 462(b) under the Securities Act, please check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If this form is a post-effective amendment filed pursuant to Rule 462(c) under the Securities Act, check the following box and list the Securities Act registration statement number of the earlier effective registration statement for the same offering. ¨

If delivery of the prospectus is expected to be made pursuant to Rule 434, please check the following box. ¨

CALCULATION OF REGISTRATION FEE

Title of Each Class of Securities to be Registered	Amount To Be Registered(1)	Proposed Maximum Offering Price Per Unit(2)	Proposed Maximum Aggregate Offering Price	Amount of Registration Fee(3) (5)
Common Stock, par value $0.01 per share(1) and Preferred Stock Purchase Rights(4)	27,322,400	$ 12.32	$ 336,611,968	$ 42,648.74

(1) Represents the number of shares of common stock that are currently issuable upon exchange of the 3.25% Exchangeable Senior Debentures due April 25, 2024 of Host Marriott, L.P. (the Debentures). Pursuant to Rule 416(a) under the Securities Act, this registration statement shall be deemed to cover any additional number of shares of common stock as may be issued from time to time upon exchange of the Debentures as a result of stock splits, stock dividends or similar transactions. No additional consideration will be received for the common stock and, therefore, no registration fee is required pursuant to Rule 457(i).

(2) The price is estimated in accordance with Rule 457(c) under the Securities Act, solely for the purpose of calculating the registration fee and is $12.32, the average of the high and low prices of Host Marriott common stock as reported by the New York Stock Exchange on June 30, 2004.

(3) Determined Pursuant to Rule 457(o).

(4) The registration statement also includes the rights to acquire shares of registrant s Series A Junior Participating Preferred Stock associated with the registrant s common stock. These preferred stock purchase rights are initially carried and traded with the common stock and the value of the rights, if any, is reflected in the value of the common stock.

(5) Pursuant to Rule 457(p), $42,648.74 of the filing fee previously paid by Host Marriott, L.P., a subsidiary in which the Company owns more than 50 percent of the outstanding voting securities, upon the initial filing of the registration on Form S-3 (File Number 333-61722) on May 25, 2001, is offset against the currently due filing fee.

The registrant hereby amends this Registration Statement on such date or dates as may be necessary to delay its effective date until the registrant shall file a further amendment which specifically states that this Registration Statement shall thereafter become effective in accordance with Section 8(a) of the Securities Act of 1933 or until the Registration Statement shall become effective on such date as the Securities and Exchange Commission, acting pursuant to said Section 8(a), may determine.

Table of Contents

Subject to completion, dated July 8, 2004

PROSPECTUS

27,322,400 Shares of Common Stock

This prospectus related to 27,322,400 shares of our common stock that may be offered for resale by the persons or entities listed herein who may become stockholders of ours upon issuance of shares of common stock upon exchange of 3.25% Exchangeable Senior Debentures due April 15, 2024 of Host Marriott, L.P. (of which we are the sole general partner and in which we own 94% of the partnership interests). Host Marriott, L.P. issued the debentures in a private offering on March 16, 2004. This prospectus also relates to an indeterminate number of additional shares of our common stock that may be issued from time to time upon exchange of the debentures as a result of exchange rate adjustments under the terms of the debentures.

The selling stockholders named in this prospectus, or in supplements hereto, may sell all or a portion of the common stock, from time to time, in market transactions, in negotiated transactions or otherwise, and at prices and on terms which will be determined by the then prevailing market price for common stock or at negotiated prices directly or through a broker or brokers, who may act as agent or as principal or by a combination of such methods of sale. See Plan of Distribution for additional information on the methods of sale.

No securities are being offered or sold by us pursuant to this prospectus. We will not receive any of the proceeds from the sale of these shares by the selling stockholders.

Our common stock is traded on the New York Stock Exchange under the symbol HMT . On July 7, 2004, the last reported sale price of our common stock was $12.75 per share.

Our principal executive offices are located at 6903 Rockledge Drive, Suite 1500, Bethesda, Maryland, 20817. Our phone number is (240) 744-1000.

Investing in the offered securities involves risks. See Risk Factors beginning on page 2.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the offered securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this prospectus is July , 2004.

Table of Contents

You should rely only on the information contained in or incorporated by reference in this prospectus. We have not authorized anyone to provide you with different information. We are not making an offer of these securities in any state where the offer is not permitted. You should not assume that the information contained in this prospectus or the documents incorporated therein is accurate as of any date other than the date of this prospectus or such documents.

TABLE OF CONTENTS

About This Prospectus	ii
Summary	1
Risk Factors	2
Where You Can Find More Information	16
Forward-Looking Statements	17
Use of Proceeds	19
Price Range of Common Stock	19
Dividend Policy	20
Description of Capital Stock	23
Selling Stockholders	33
Plan of Distribution	35
Legal Matters	37
Independent Registered Public Accounting Firm	37

Table of Contents

ABOUT THIS PROSPECTUS

Unless otherwise indicated or unless the context requires otherwise, all references in this prospectus to we, us, our, Host Marriott, or the Company means Host Marriott Corporation, including our consolidated subsidiaries. References to the Operating Partnership or to Host LP are to Host Marriott, L.P., a Delaware limited partnership.

This prospectus is part of a registration statement that we filed with the Securities and Exchange Commission, or the SEC, using a shelf registration process for the delayed offering and sale of securities pursuant to Rule 415 under the Securities Act of 1933. Under the shelf process, the selling stockholders may, from time to time, sell the offered securities described in this prospectus in one or more offerings.

This prospectus and any accompanying prospectus supplement do not contain all of the information included in the registration statement. We have omitted parts of the registration statement in accordance with the rules and regulations of the SEC. For further information, we refer you to the registration statement on Form S-3 of which this prospectus is a part, including its exhibits. Statements contained in this prospectus and any accompanying prospectus supplement about the provisions or contents of any agreement or other document are not necessarily complete. If the SEC rules and regulations require that an agreement or document be filed as an exhibit to the registration statement, please see that agreement or document for a complete description of these matters. You should not assume that the information in this prospectus or any prospectus supplement is accurate as of any date other than the date on the front of each document.

You should read both this prospectus and any prospectus supplement together with the additional information described under the heading Where You Can Find More Information in this prospectus.

Table of Contents

SUMMARY

This summary contains a general summary of the information contained in this prospectus. The summary may not contain all of the information that is important to you, and it is qualified in its entirety by the more detailed information and historical consolidated financial statements, including the notes to those financial statements, that are part of the reports we file with the SEC and that are incorporated by reference in this prospectus. You should carefully consider the information contained in and incorporated by reference in this entire prospectus including the information set forth under the heading Risk Factors , beginning on page 2 of this prospectus.

General

We are a Maryland corporation and we operate as a self-managed and self-administered real estate investment trust, or REIT. We own our properties and conduct our operations through Host Marriott, L.P., a Delaware limited partnership of which we are the sole general partner and in which we hold 94% of the partnership interests as of July 1, 2004.

As of July 1, 2004, our lodging portfolio consisted of 111 upper-upscale and luxury full-service hotels containing approximately 56,000 rooms. Our portfolio is geographically diverse with hotels in most of the major metropolitan areas in 28 states, Washington, D.C., Toronto and Calgary, Canada and Mexico City, Mexico. Our locations include central business districts of major cities, near airports and resort/convention locations. Our hotels are operated under such brand names as Marriott, Ritz-Carlton, Hyatt, Four Seasons, Hilton and Westin.

The address of our principal executive office is 6903 Rockledge Drive, Suite 1500, Bethesda, Maryland, 20817. Our phone number is (240) 744-1000. Our Internet website address is www.hostmarriott.com.

The Offering

This prospectus relates to the resale by the selling stockholders of up to 27,322,400 shares of our common stock that we may issue to the selling stockholders upon exchange of the 3.25% Exchangeable Senior Debentures due April 15, 2024 of Host Marriott, L.P. (plus an indeterminate number of additional shares of our common stock that may be issued from time to time upon exchange of the debentures as a result of exchange rate adjustments under the terms of the debentures).

Table of Contents

RISK FACTORS

You should carefully consider the risk factors set forth below and other information included or incorporated by reference in this prospectus before you decide to buy our common stock. This includes the risk factors set forth below and the matters discussed in the section entitled Management s Discussion and Analysis of Financial Condition and Results of Operations in our most recent Annual Report on Form 10-K and Quarterly Report on Form 10-Q and the discussion of material federal income tax consequences applicable to us and holders of our common stock incorporated by reference from our Form 8-K dated March 5, 2004, which are incorporated by reference into this prospectus, as the same may be updated from time to time by our future filings under the Securities Exchange Act of 1934, as amended. For more information, see the section entitled, Where You Can Find More Information in this prospectus.

Risks of Ownership of our Common Stock

There are limitations on the acquisition of our common stock and changes in control. Our charter and bylaws, the partnership agreement of the Operating Partnership, our stockholder rights plan and the Maryland General Corporation Law contain a number of provisions, the exercise of which could delay, defer or prevent a transaction or a change in control of us that might involve a premium price for our stockholders or otherwise be in their best interests, including the following:

Ownership limit. The 9.8% ownership limit described under Risk Factors Risks of Ownership of our Common Stock There are possible adverse consequences of limits on ownership of our common stock may have the effect of precluding a change in control of us by a third party without the consent of our Board of Directors, even if the change in control would be in the interest of our stockholders, and even if the change in control would not reasonably jeopardize our REIT status.

Removal of board of directors. Our charter provides that, except for any directors who may be elected by holders of a class or series of shares of capital stock other than our common stock, directors may be removed only for cause and only by the affirmative vote of stockholders holding at least two-thirds of all the votes entitled to be cast for the election of directors. Vacancies on the Board of Directors may be filled by the concurring vote of a majority of the remaining directors and, in the case of a vacancy resulting from the removal of a director by the stockholders, by at least two-thirds of all the votes entitled to be cast in the election of directors.

Preferred shares; classification or reclassification of unissued shares of capital stock without stockholder approval. Our charter provides that the total number of shares of stock of all classes that we have authority to issue is 800,000,000, initially consisting of 750,000,000 shares of common stock and 50,000,000 shares of preferred stock. Our Board of Directors has the authority, without a vote of stockholders, to classify or reclassify any unissued shares of stock, including common stock into preferred stock or vice versa, and to establish the preferences and rights of any preferred or other class or series of shares to be issued. The issuance of preferred shares or other shares having special preferences or rights could delay, defer or prevent a change in control even if a change in control would be in the interests of our stockholders. Because our Board of Directors has the power to establish the preferences and rights of additional classes or series of shares without a stockholder vote, our Board of Directors may give the holders of any class or series preferences, powers and rights, including voting rights, senior to the rights of holders of our common stock.

Consent rights of the limited partners. Under the partnership agreement of the Operating Partnership, we generally will be able to merge or consolidate with another entity with the consent of partners holding limited percentage interests that are more than 50% of the aggregate percentage interests of the outstanding limited partnership interests entitled to vote on the merger or consolidation, including any limited partnership interests held by us, as long as the holders of limited partnership interests either receive or have the right to receive the same

consideration as our stockholders. We, as holder of a majority of the limited partnership interests, would be able to control the vote. Under our charter, holders of at least two-thirds of our outstanding shares of common stock generally must approve the merger or consolidation.

Maryland business combination law. Under the Maryland General Corporation Law, specified business combinations, including specified issuances of equity securities, between a Maryland corporation and any person who owns 10% or more of the voting power of the corporation s then outstanding shares, or an interested stockholder, or an affiliate of the interested stockholder are prohibited for five years after the most recent date on which the interested stockholder becomes an interested stockholder. Thereafter, any of these specified business combinations must be approved by 80% of the votes entitled to be cast by the holders of outstanding voting shares and by two-thirds of the votes entitled to be cast by the holders of voting shares other than voting shares held by an interested stockholder unless, among other conditions, the corporation s common stockholders receive a minimum price, as defined in the Maryland General Corporation Law, for their shares and the consideration is received in cash or in the same form as previously paid by the interested stockholder. We are subject to the Maryland business combination statute.

Maryland control share acquisition law. Under the Maryland General Corporation Law, control shares acquired in a control share acquisition have no voting rights except to the extent approved by a vote of two-thirds of the votes entitled to be cast on the matter, excluding shares owned by the acquiror, by officers or by directors who are employees of the corporation. Control shares are voting shares which, if aggregated with all other voting shares previously acquired by the acquiror or over which the acquiror is able to exercise or direct the exercise of voting power (except solely by virtue of a revocable proxy), would entitle the acquiror to exercise voting power in electing directors within one of the following ranges of voting power: (1) one-tenth or more but less than one-third, (2) one-third or more but less than a majority or (3) a majority or more of the voting power. Control shares do not include shares the acquiring person is then entitled to vote as a result of having previously obtained stockholder approval. A control share acquisition means the acquisition of control shares, subject to specified exceptions. We are subject to these control share provisions of Maryland law.

Merger, consolidation, share exchange and transfer of our assets. Pursuant to our charter, subject to the terms of any outstanding class or series of capital stock, we can merge with or into another entity, consolidate with one or more other entities, participate in a share exchange or transfer our assets within the meaning of the Maryland General Corporation Law if approved (1) by our Board of Directors in the manner provided in the Maryland General Corporation Law and (2) by our stockholders holding two-thirds of all the votes entitled to be cast on the matter, except that any merger of us with or into a trust organized for the purpose of changing our form of organization from a corporation to a trust requires only the approval of our stockholders holding a majority of all votes entitled to be cast on the merger. Under the Maryland General Corporation Law, specified mergers may be approved without a vote of stockholders and a share exchange is only required to be approved by a Maryland corporation by its Board of Directors if the corporation is the successor. Our voluntary dissolution also would require approval of stockholders holding two-thirds of all the votes entitled to be cast on the matter.

Certain amendments to our charter and bylaws. Our charter contains provisions relating to restrictions on transferability of our common stock, fixing the size of our Board of Directors within the range set forth in our charter, removal of directors and the filling of vacancies, all of which may be amended only by a resolution adopted by the Board of Directors and approved by our stockholders holding two-thirds of the votes entitled to be cast on the matter. Any amendments of these provisions of our charter (setting forth the necessary approval requirements) also would require action of our Board of Directors and the approval by stockholders holding two-thirds of all the votes entitled to be cast on the matter. As permitted under the Maryland General Corporation Law, our bylaws provide that directors have the exclusive right to amend our bylaws.

Stockholder rights plan. We adopted a stockholder rights plan which provides, among other things, that when specified events occur, our stockholders will be entitled to purchase from us a newly created class or series of junior preferred shares, subject to our ownership limit described below. The preferred share purchase rights are triggered by the earlier to occur of (1) ten days after the date of a public announcement that a person or group acting in concert has acquired, or obtained the right to acquire, beneficial ownership of 20% or more of our outstanding shares of common stock or (2) ten business days after the commencement of or announcement of an intention to make a tender offer or exchange offer, the consummation of which would result in the acquiring person becoming the beneficial owner of 20% or more of our outstanding common stock. The exercise of the

preferred share purchase rights would cause substantial dilution to a person or group that attempts to acquire us on terms not approved by our Board of Directors.

There are possible adverse consequences of limits on ownership of our common stock. To maintain our qualification as a REIT for Federal income tax purposes, not more than 50% in value of our outstanding shares of capital stock may be owned, directly or indirectly, by five or fewer individuals, as defined in the Internal Revenue Code to include some entities. In addition, a person who owns, directly or by attribution, 10% or more of an interest in a tenant of ours, or a tenant of any partnership in which we are a partner, cannot own, directly or by attribution, 10% or more of our shares without jeopardizing our qualification as a REIT. Primarily to facilitate maintenance of our qualification as a REIT for Federal income tax purposes, the ownership limit under our charter prohibits ownership, directly or by virtue of the attribution provisions of the Internal Revenue Code, by any person or persons acting as a group, of more than 9.8% of the issued and outstanding shares of our common stock, and prohibits ownership, directly or by virtue of the attribution provisions of the Internal Revenue Code, by any person, or persons acting as a group, of more than 9.8% of the issued and outstanding shares of any class or series of our preferred shares or any other class or series of stock. Together, these limitations are referred to as the ownership limit.

Our Board of Directors, in its sole and absolute discretion, may waive or modify the ownership limit with respect to one or more persons who would not be treated as individuals for purposes of the Internal Revenue Code if the Board of Directors is satisfied, based upon information required to be provided by the party seeking the waiver and, if it determines necessary or advisable, upon an opinion of counsel satisfactory to our Board of Directors, that ownership in excess of this limit will not cause a person who is an individual to be treated as owning shares in excess of the ownership limit, applying the applicable constructive ownership rules, and will not otherwise jeopardize our status as a REIT for Federal income tax purposes (for example, by causing any of our tenants to be considered a related party tenant for purposes of the REIT qualification rules). Common stock acquired or held in violation of the ownership limit will be transferred automatically to a trust for the benefit of a designated charitable beneficiary, and the person who acquired the common stock in violation of the ownership limit will not be entitled to any distributions thereon, to vote those shares of common stock or to receive any proceeds from the subsequent sale of the common stock in excess of the lesser of the price paid for the common stock or the amount realized from the sale. A transfer of shares of our common stock to a person who, as a result of the transfer, violates the ownership limit may be void under certain circumstances, and, in any event, would deny that person any of the economic benefits of owning shares of our common stock in excess of the ownership limit. The ownership limit may have the effect of delaying, deferring or preventing a change in control and, therefore, could adversely affect the stockholders ability to realize a premium over the then-prevailing market price for our common stock in connection with such transaction.

Shares of our common stock that are or become available for sale could affect the price for shares of our common stock. Sales of a substantial number of shares of our common stock, or the perception that sales could occur, could adversely affect prevailing market prices for our common stock. In addition, holders of units of limited partnership interest in the Operating Partnership (referred to as OP Units), whose OP Units are redeemed by the Operating Partnership in exchange for common stock, will be able to sell those shares freely, unless the person is our affiliate and resale of the affiliate s shares is not covered by an effective registration statement. Further, a substantial number of shares of our common stock have been and will be issued or reserved for issuance from time to time under our employee benefit plans, including shares of our common stock reserved for options, or pursuant to securities we may issue that are convertible into shares of our common stock or securities (other than OP Units) that the Operating Partnership has issued that are exchangeable for shares of our common stock. These shares of common stock would be available for sale in the public markets from time to time pursuant to exemptions from registration or upon registration. As of July 1, 2004, (i) there are approximately 23 million OP Units outstanding that are currently redeemable, and (ii) there are outstanding $500 million aggregate principal amount of 3.25% Exchangeable Senior Debentures of the Operating Partnership exchangeable under certain conditions for shares of our common stock at a price of approximately $18.30 per share. Moreover, additional shares of our common stock issued by us would be available in the future for sale in

the public markets. We can make no prediction about the effect that future sales of our common stock would have on the market price of our common stock.

Our earnings and cash distributions will affect the market price of shares of our common stock. We believe that the market value of a REIT s equity securities is based primarily upon the market s perception of the REIT s growth potential and its current and potential future cash distributions, whether from operations, sales, acquisitions, development or refinancings, and is secondarily based upon the value of the underlying assets. For that reason, shares of our common stock may trade at prices that are higher or lower than the net asset value per share. To the extent we retain operating cash flow for investment purposes, working capital reserves or other purposes rather than distributing the cash flow to stockholders, these retained funds, while increasing the value of our underlying assets, may negatively impact the market price of our common stock. Our failure to meet the market s expectation with regard to future earnings and cash distributions would likely adversely affect the market price of our common stock.

Market interest rates may affect the price of shares of our common stock. We believe that one of the factors that investors consider important in deciding whether to buy or sell shares of a REIT is the distribution rate on the shares, considered as a percentage of the price of the shares, relative to market interest rates. If market interest rates increase, prospective purchasers of REIT shares may expect a higher distribution rate. Thus, higher market interest rates could cause the market price of our shares to go down.

Financial Risks and Risks of Operation

We depend on external sources of capital for future growth and we may be unable to access capital when necessary. Unlike corporations, our ability to reduce our debt and finance our growth largely must be funded by external sources of capital because we are generally required to distribute to our stockholders at least 90% of our taxable income in order to qualify as a REIT, including taxable income we recognize for tax purposes but with regard to which we do not receive corresponding cash. Our ability to access the external capital we require could be hampered by a number of factors many of which are outside of our control, including, without limitation, declining general market conditions, unfavorable market perception of our growth potential, decreases in our current and estimated future earnings, excessive cash distributions or decreases in the market price of our common stock. In addition, our ability to access additional capital may also be limited by the terms of our existing indebtedness, which, among other things, restricts our incurrence of debt and the payment of distributions. The occurrence of any of these above-mentioned factors, individually or in combination, could prevent us from being able to obtain the external capital we require on terms that are acceptable to us or at all and the failure to obtain necessary external capital could have a material adverse affect on our ability to finance our future growth.

We have substantial leverage. We have a significant amount of indebtedness and that could have important consequences. It currently requires us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, which reduces the availability of our cash flow to fund working capital, capital expenditures, expansion efforts, distributions to our stockholders and other general purposes. Additionally, our high level of indebtedness could:

limit our ability in the future to undertake refinancings of our indebtedness or obtain financing for expenditures, acquisitions, development or other general corporate or business purposes; or

affect adversely our ability to compete effectively or operate successfully under adverse economic conditions.

If our cash flow and working capital were not sufficient to fund our expenditures or service our indebtedness, we would have to raise additional funds through:

- the sale of our equity;
- the incurrence of additional permitted indebtedness by the Operating Partnership; or

Table of Contents

the sale of our assets.

We cannot assure you that any of these sources of funds would be available to us or, if available, would be on terms that we would find acceptable or in amounts sufficient for us to meet our obligations or fulfill our business plan.

Our revenues and the value of our properties are subject to conditions affecting the lodging industry. The lodging industry has experienced a difficult period, and operations generally declined from 2001 to 2003, which caused declines in our revenue per available room, or RevPAR, and profit margins. The decline in the lodging industry was attributed to a number of factors including a weak economy, the effect of terrorist attacks, terror alerts and potential terrorist activity in the United States and the war in Iraq, all of which changed the travel patterns of both business and leisure travelers. While our operations have improved and RevPAR increased in the first quarter of 2004, it is not clear whether the changes in travel patterns of both business and leisure travelers are permanent or whether they will continue to evolve creating new opportunities or difficulties for the industry. Any forecast we make regarding our results of operations may be affected and can change based on the following risks:

- changes in the national, regional and local economic climate;
- reduced demand and increased operating costs and other conditions resulting from terrorist threats;
- changes in business and leisure travel patterns;
- local market conditions such as an oversupply of hotel rooms or a reduction in lodging demand;
- the attractiveness of our hotels to consumers relative to our competition;
- the performance of the managers of our hotels;
- changes in room rates and increases in operating costs due to inflation and other factors; and
- unionization of the labor force at our hotels.

Our expenses may not decrease if our revenue drops. Many of the expenses associated with owning and operating hotels, such as debt payments, property taxes, insurance, utilities, and employee wages and benefits, are relatively inflexible and do not necessarily decrease in tandem with a reduction in revenue at the property. Because of weak economic conditions from 2001 to 2003, particularly in the lodging industry, we have been working with our managers to reduce the operating costs of our hotels. While we have achieved reductions in operating costs as a result of these efforts, further cost reductions could be difficult to achieve if operating levels were to decline further. Some of the cost reduction efforts undertaken may eventually need to be reversed even if operations again declined to reduced levels. Regardless of these efforts to reduce costs, our expenses will be affected by inflationary increases, and in the case of certain costs, such as wages, benefits and insurance, may exceed the rate of inflation in any given period. Our managers may be unable to offset any such increased expenses with higher room rates. Any of our efforts to reduce operating costs or failure to make scheduled capital expenditures could adversely affect the growth of our business and the value of our hotel properties.

Our revenues may be affected by increased use of reservation systems based on the Internet. Although a majority of the room reservations made on the Internet are made through websites maintained by our managers, a growing number of reservations are also made through independent Internet sites. These independent Internet sites often purchase room reservations at a negotiated discount from participating properties, which could result in lower average room rates compared to the room rates offered by the manager on its website. While we do not believe that price is the only factor considered when choosing our properties, if the room rate available to consumers using the independent Internet sites were to be significantly lower than those offered by our managers on their websites our revenues and results of operations could be adversely affected.

Our ground lease payments may increase faster than the revenues we receive on the hotels situated on the leased properties. As of July 1, 2004, forty-four of all or a portion of our hotels are subject to ground leases.

These ground leases generally require increases in ground rent payments every five years. Our ability to service our debt could be adversely affected to the extent that our revenues do not increase at the same or a greater rate than the increases in rental payments under the ground leases. In addition, if we were to sell a hotel encumbered by a ground lease, the buyer would have to assume the ground lease, which may result in a lower sales price.

We do not control our hotel operations and we are dependent on the managers of our hotels. Because Federal income tax laws restrict REITs and their subsidiaries from operating a hotel, we do not manage our hotels. Instead, we lease substantially all of our full-service properties to subsidiaries which qualify as taxable REIT subsidiaries under applicable REIT laws, and our taxable REIT subsidiaries retain third-party managers to manage our hotels pursuant to management agreements. Our income from the hotels may be adversely affected if our managers fail to provide quality services and amenities or if they fail to maintain a quality brand name. While our taxable REIT subsidiaries monitor the hotel managers performance, we have limited specific recourse under our management agreements if we believe that the hotel managers are not performing adequately. In addition, from time to time, we have had, and continue to have, differences with the managers of our hotels over their performance and compliance with the terms of our management agreements. We generally resolve issues with our managers through discussions and negotiations. However, if we are unable to reach satisfactory results through discussions and negotiations, we may choose to litigate such a dispute. Failure by our hotel managers to fully perform the duties agreed to in our management agreements could adversely affect our results of operations. In addition, our hotel managers manage, and in some cases own or have invested in, hotels that compete with our hotels, which may result in conflicts of interest. As a result, our hotel managers have in the past made and may in the future make decisions regarding competing lodging facilities that are not or would not be in our best interests.

The terms of our debt place restrictions on us and our subsidiaries, reducing operational flexibility and creating default risks. The documents governing the terms of the senior notes and credit facility of the Operating Partnership contain covenants that place restrictions on us and our subsidiaries. The activities upon which such restrictions exist include, but are not limited to:

- acquisitions, mergers and consolidations;
- the incurrence of additional debt;
- the creation of liens;
- the sale of assets;
- capital expenditures;
- raising capital from the issuance of certain types of mandatorily redeemable capital stock;
- the payment of dividends; and
- transactions with affiliates.

In addition, certain covenants in the credit facility of the Operating Partnership require it and our other subsidiaries to meet financial performance tests. The restrictive covenants in the indenture, the credit facility and the documents governing our other debt (including our mortgage debt) may reduce our flexibility in conducting our operations and may limit our ability to engage in activities that may be in our long-term best interest. The Operating Partnership s failure to comply with these restrictive covenants could result in an event of default that, if

not cured or waived, could result in the acceleration of all or a substantial portion of our debt.

Our mortgage debt contains provisions that may reduce our liquidity. Certain of our mortgage debt requires that, to the extent cash flow from the hotels which secure such debt drops below stated levels, we escrow cash flow after the payment of debt service until operations improve above the stated levels. In some cases, the escrowed amount may be applied to the outstanding balance of the mortgage debt. When such provisions are triggered, there can be no assurance that the affected properties will achieve the minimum cash flow levels required to trigger a release of any escrowed funds. The amounts required to be escrowed may be material and

Table of Contents

may negatively affect our liquidity by limiting our access to cash flow after debt service from these mortgaged properties.

Our ability to pay dividends on our common stock may be limited or prohibited by the terms of our indebtedness. We and our subsidiaries, including the Operating Partnership, are, and may in the future become, parties to agreements and instruments which restrict or prevent the payment of dividends on our classes and series of capital stock. For example, under the terms of our credit facility and our senior notes indenture, distributions to us by the Operating Partnership, which we depend upon in order to obtain the cash necessary to pay dividends, are permitted only to the extent that, at the time of the distributions, the Operating Partnership can satisfy certain financial covenant tests and meet other requirements which are summarized below in Dividend Policy Dividend and Redemption Restrictions Under Our Debt Instruments and Our Preferred Stock. At any time during which it fails to meet these requirements, the Operating Partnership will only be able to make cash distributions to us in the amounts required to maintain our qualification as a REIT (subject to limitations on the Operating Partnership s ability to pay these permitted REIT distributions described below in Dividend Policy Dividend and Redemption Restrictions Under Our Debt Instruments and Our Preferred Stock).

Beginning in the third quarter of 2002 and continuing through the fiscal quarter ended March 26, 2004, the Operating Partnership was prohibited from making distributions and other restricted payments, other than permitted REIT distributions, because the Operating Partnership s EBITDA-to-interest coverage ratio as calculated under the indenture governing its senior notes (which measures the Operating Partnership s ratio of its pro forma consolidated EBITDA to pro forma consolidated interest expense) was below 2.0 to 1.0. Accordingly, during this period, the Operating Partnership was only able to make distributions to us, and we only have been able to pay dividends to the extent that we had taxable income and were required to make distributions to maintain our status as a REIT. Our income distribution requirements for 2002 were satisfied, in part, by the full payment of regular dividends on our outstanding classes of preferred stock in 2002 and in the first three quarters of 2003, but our distribution requirements were not sufficient enough to permit us to pay any dividend on our common stock. We did not generate any taxable income from regular operations during 2003; however, taxable income generated by our insurance recovery on the New York Marriott World Trade Center and Financial Center hotels was sufficient to allow us to pay the regular quarterly dividend due on our outstanding classes of preferred stock for the fourth quarter of 2003 and the first quarter of 2004. We expect that the taxable income generated by the insurance recovery will be sufficient to allow us to pay the regular quarterly dividend on our outstanding classes of preferred stock through the third quarter of 2004. We will likely need to distribute a small dividend on our common stock in 2004 to complete the final required distribution of 2003 taxable income.

Currently, our EBITDA-to-interest coverage ratio is slightly above 2.0 to 1.0, based upon our results of operations for the four fiscal quarters ended March 26, 2004, and after giving effect to certain acquisition, disposition, financing and other transactions that occurred subsequent to March 26, 2004. Under the terms of the senior notes indenture, the ability to consider the aggregate pro forma effect of transactions occurring subsequent to March 26, 2004, such as our redemption of approximately, $560 million of outstanding indebtedness, hotel acquisitions and dispositions and our redesignation by the Operations Partnership of JWDC Limited Partnership, through which we own the JW Marriott hotel in Washington, D.C. as a restricted subsidiary under the senior notes indenture, had the effect of improving the Operating Partnership s EBITDA-to-interest coverage ratio. As a result, and because we expect operations to continue to improve, we currently expect to be able to pay dividends on our outstanding classes of preferred stock without regard to whether we generate any taxable income. However, we currently do not expect to pay a meaningful dividend on our common stock during 2004. Notwithstanding our current expectations, a decline in our operations or an increase in our consolidated interest expense, or any combination thereof, or, if the Operating Partnership is required to give pro forma effect to any other transactions that have a similar effect, could cause the Operating Partnership s EBITDA-to-interest coverage ratio to again fall below 2.0 to 1.0. This could once again limit the amount of the Operating Partnership s distributions to us (and our payment of dividends on our capital stock) to only permitted REIT distributions. Since, based on current estimates, we do not currently expect to generate taxable income during 2004, if the Operating Partnership s EBITDA-to-interest coverage ratio again falls below 2.0 to 1.0, or the Operating Partnership is otherwise limited in the amount of distributions it can make to us under the terms of the senior notes indenture, we cannot provide any assurance that we would be able to pay dividends on any class of our capital stock.

Accordingly, our ability to resume paying dividends on our common stock will depend on several factors outside of our control, such as our liquidity, the extent of our taxable income or loss from operations in 2004 and thereafter, our ability to meet the minimum EBITDA-to-interest coverage ratio and to satisfy the other requirements for making distributions set forth in the senior notes indenture and our credit facility and the amount of cumulative accrued dividends, if any, that remain unpaid on our outstanding classes of preferred stock (as discussed below).

Our ability to pay dividends on our common stock may also be limited or prohibited by the terms of our preferred stock. Under the terms of each of our outstanding classes of preferred stock, we are not permitted to pay dividends on our common stock unless cumulative dividends have been paid (or funds for payment have been set aside for payment) on each such class of preferred stock. Not counting our 10% Class A cumulative redeemable preferred stock (which we have called for redemption on August 3, 2004), the amount of aggregate dividends that accrue on our outstanding classes of preferred stock each quarter is approximately $8.5 million.

In the event that we fail to pay the accrued dividends on our preferred stock for any reason, including because we are prevented from paying such dividends under the terms of the Operating Partnership s debt instruments (as discussed above), dividends will continue to accrue on all outstanding classes of our preferred stock and we will be prohibited from paying any dividends on our common stock until all such accrued but unpaid dividends on our preferred stock have been paid (or funds for such payment have been set aside).

Rating Agency downgrades may increase our cost of capital. Both our corporate debt and our preferred stock are rated by independent rating agencies, such as Moody s and Standard & Poor s. These rating agencies may elect to downgrade their ratings on our corporate debt and our preferred stock at any time. These downgrades may negatively affect our access to the capital markets and increase our cost of capital.

Our management agreements could impair the sale or financing of our hotels. Under the terms of our management agreements, we generally may not sell, lease or otherwise transfer the hotels unless the transferee is not a competitor of the manager and the transferee assumes the related management agreements and meets specified other conditions. Our ability to finance or sell any of the properties, depending upon the structure of such transactions, may require the manager s consent. If, in these circumstances, the manager does not consent, we would be prohibited from taking actions in our best interest without breaching the management agreement.

The acquisition contracts relating to some hotels limit our ability to sell or refinance those hotels. For reasons relating to tax considerations of the former and current owners of nine hotels, we have agreed to restrictions on selling the hotels, or repaying or refinancing the mortgage debt for varying periods depending on the hotel. We have also agreed not to sell more than 50% of the original allocated value attributable to the former owners of a portfolio of 11 additional hotels, or to take other actions that would result in the recognition and allocation of gain to the former owners of such hotels for income tax purposes. We anticipate that, in specified circumstances, we may agree to similar restrictions in connection with future hotel acquisitions. As a result, even if it were in our best interests to sell these hotels or repay or otherwise reduce the level of the mortgage debt on such hotels, it may be difficult or costly to do so during their respective lock-out periods.

We may be unable to sell properties because real estate investments are illiquid. Real estate investments generally cannot be sold quickly. We may not be able to vary our portfolio promptly in response to economic or other conditions. The inability to respond promptly to changes in the performance of our investments could adversely affect our financial condition and our ability to service our debt. In addition, there are limitations under the federal tax laws applicable to REITs that may limit our ability to recognize the full economic benefit from a sale of our assets.

We depend on our key personnel. Our success depends on the efforts of our executive officers and other key personnel. None of our key personnel have employment agreements and we do not maintain key person life insurance for any of our executive officers. We cannot assure

you that these key personnel will remain employed

Table of Contents

by us. While we believe that we could find replacements for these key personnel, the loss of their services could have a significant adverse effect on our financial performance.

Litigation judgments or settlements could have a material adverse effect on our financial condition. We are a party to various lawsuits, including lawsuits relating to our conversion into a REIT. While we and the other defendants to such lawsuits believe all of the lawsuits in which we are a defendant are without merit and we are vigorously defending against such claims, we can give no assurance as to the outcome of any of the lawsuits. If any of the lawsuits were to be determined adversely to us or a settlement involving a payment of a material sum of money were to occur, there could be a material adverse effect on our financial condition.

We may acquire hotel properties through joint ventures with third parties that could result in conflicts. Instead of purchasing hotel properties directly, we may invest as a co-venturer. Co-venturers often share control over the operation of a joint venture. For example, we entered into a joint venture with Marriott International that owns two limited partnerships holding, in the aggregate, 120 Courtyard by Marriott hotels. Subsidiaries of Marriott International manage these Courtyard by Marriott hotels and other subsidiaries of Marriott International serve as ground lessors and mezzanine lender to the partnerships. Actions by a co-venturer could subject the assets to additional risk, including:

- our co-venturer in an investment might have economic or business interests or goals that are inconsistent with our, or the joint venture s, interests or goals;

- our co-venturer may be in a position to take action contrary to our instructions or requests or contrary to our policies or objectives; or

- our co-venturer could go bankrupt, leaving us liable for its share of joint venture liabilities.

Although we generally will seek to maintain sufficient control of any joint venture to permit our objectives to be achieved, we might not be able to take action without the approval of our joint venture partners. Also, our joint venture partners could take actions binding on the joint venture without our consent.

Environmental problems are possible and can be costly. We believe that our properties are in compliance in all material respects with applicable environmental laws. Unidentified environmental liabilities could arise, however, and could have a material adverse effect on our financial condition and performance. Federal, state and local laws and regulations relating to the protection of the environment may require a current or previous owner or operator of real estate to investigate and clean up hazardous or toxic substances or petroleum product releases at the property. The owner or operator may have to pay a governmental entity or third parties for property damage and for investigation and clean-up costs incurred by the parties in connection with the contamination. These laws typically impose clean-up responsibility and liability without regard to whether the owner or operator knew of or caused the presence of the contaminants. Even if more than one person may have been responsible for the contamination, each person covered by the environmental laws may be held responsible for all of the clean-up costs incurred. In addition, third parties may sue the owner or operator of a site for damages and costs resulting from environmental contamination emanating from that site. Environmental laws also govern the presence, maintenance and removal of asbestos. These laws require that owners or operators of buildings containing asbestos properly manage and maintain the asbestos, that they notify and train those who may come into contact with asbestos and that they undertake special precautions, including removal or other abatement, if asbestos would be disturbed during renovation or demolition of a building. These laws may impose fines and penalties on building owners or operators who fail to comply with these requirements and may allow third parties to seek recovery from owners or operators for personal injury associated with exposure to asbestos fibers.

Compliance with other government regulations can be costly. Our hotels are subject to various other forms of regulation, including Title III of the Americans with Disabilities Act, building codes and regulations pertaining to fire safety. Compliance with those laws and regulations could require substantial capital expenditures. These regulations may be changed from time to time, or new regulations adopted, resulting in

Table of Contents

additional costs of compliance, including potential litigation. Any increased costs could have a material adverse effect on our business, financial condition or results of operations.

Future terrorist attacks or changes in terror alert levels could adversely affect us. Previous terrorist attacks in the United States have adversely affected the travel and hospitality industries, including the full-service portion of the hotel industry. The impact which terrorist attacks in the United States or elsewhere could have on our business in particular and the U.S. economy, the global economy and global financial markets in general is indeterminable. It is possible that such attacks or the threat of such attacks could have a material adverse effect on our business, our ability to finance our business, our ability to insure our properties and on our results of operations and financial condition as a whole.

Some potential losses are not covered by insurance. We carry comprehensive insurance coverage for general liability, property, business interruption and other risks with respect to all of our hotels and other properties. These policies offer coverage features and insured limits that we believe are customary for similar type properties. Generally, our all-risk property policies provide coverage that is available on a per occurrence basis and that, for each occurrence, has an overall limit as well as various sub-limits on the amount of insurance proceeds we can receive. Sub-limits exist for certain types of claims such as service interruption, abatement, earthquakes, expediting costs or landscaping replacement, and the dollar amounts of these sub-limits are significantly lower than the dollar amounts of the overall coverage limit. Our property policies also provide that all of the claims from each of our properties resulting from a particular insurable event must be combined together for purposes of evaluating whether the aggregate limits and sub-limits contained in our policies have been exceeded and, in the case of four of our hotels where the manager provides this coverage, any such claims will also be combined with the claims of other owners participating in the managers program for the same purpose. That means that, if an insurable event occurs that affects more than one of our hotels, or, in the case of hotels where coverage is provided by the management company, affects hotels owned by others, the claims from each affected hotel will be added together to determine whether the aggregate limit or sub-limits, depending on the type of claim, have been reached and each affected hotel may only receive a proportional share of the amount of insurance proceeds provided for under the policy if the total value of the loss exceeds the aggregate limits available. We may incur losses in excess of insured limits and, as a result, we may be even less likely to receive sufficient coverage for risks that affect multiple properties such as earthquakes or certain types of terrorism.

In addition, there are other risks such as war, certain forms of terrorism such as nuclear, biological or chemical terrorism and some environmental hazards that may be deemed to fall completely outside the general coverage limits of our policies or may be uninsurable or may be too expensive to justify insuring against. If any such risk were to materialize and materially adversely affect one or more of our properties, we would likely not be able to recover our losses.

We may also encounter challenges with an insurance provider regarding whether it will pay a particular claim that we believe to be covered under our policy. Should a loss in excess of insured limits or an uninsured loss occur or should we be unsuccessful in obtaining coverage from an insurance carrier, 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 hotel. In that event, we might nevertheless remain obligated for any mortgage debt or other financial obligations related to the property.

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. We obtain terrorism insurance as part of our all-risk property insurance program. However, as noted above, our all-risk policies have limitations such as per occurrence limits and sublimits which might have to be shared proportionally across participating hotels under certain loss scenarios. Also, all-risk insurers only have to provide terrorism coverage to the extent mandated by the Terrorism Risk Insurance Act (TRIA) for certified acts of terrorism namely those which are committed on behalf of non-United States persons or interests. Furthermore,

we do not have full replacement coverage at all of our properties for acts of terrorism committed on behalf of United States persons or interests (noncertified events) as our coverage for such incidents is subject to sublimits and annual aggregate limits. In addition, property damage related to war and to nuclear, biological and chemical incidents is excluded under our policies. While TRIA will reimburse insurers for losses resulting from nuclear, biological and chemical perils, TRIA 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. In addition, TRIA terminates on December 31, 2005, and there is no guarantee that the terrorism coverage that it mandates will be readily available or affordable thereafter. As a result of the above, there remains considerable 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.

Federal Income Tax Risks

Recent changes in taxation of corporate dividends may adversely affect the value of our stock. While corporate dividends have traditionally been taxed at ordinary income rates, dividends received by individuals through December 31, 2008 from regular C corporations generally will be taxed at the maximum capital gains tax rate of 15% as opposed to the maximum ordinary income tax rate of 35%. REIT dividends are not eligible for the lower capital gains rates, except in certain circumstances where the dividends are attributable to income that has been subject to corporate-level tax. While the earnings of a REIT that are distributed to its stockholders generally will be subject to less Federal income taxation than earnings of a non-REIT C corporation that are distributed to its stockholders net of corporate-level income tax, this difference in the taxation of dividends could cause individual investors to view the stock of regular C corporations as more attractive relative to the stock of REITs. Individual investors could hold this view because the dividends from regular C corporations will generally be taxed at a lower rate while dividends from REITs will generally be taxed at the same rate as the individual s other ordinary income. We cannot predict what effect, if any, this difference in the taxation of dividends may have on the value of the stock of REITs, either in terms of price or relative to other potential investments.

To qualify as a REIT, we are required to distribute at least 90% of our taxable income, irrespective of our available cash or outstanding obligations. To continue to qualify as a REIT, we currently are required to distribute to our stockholders with respect to each year at least 90% of our taxable income, excluding net capital gain. In addition, we will be subject to a 4% nondeductible excise tax on the amount, if any, by which distributions made by us with respect to the calendar year are less than the sum of 85% of our ordinary income and 95% of our capital gain net income for that year and any undistributed taxable income from prior periods less excess distributions from prior years. We intend to make distributions, subject to the availability of cash and in compliance with any debt covenants, to our stockholders to comply with the distribution requirement and to avoid the nondeductible excise tax and will rely for this purpose on distributions from the Operating Partnership. However, there are differences in timing between our recognition of taxable income and our receipt of cash available for distribution due to, among other things, the seasonality of the lodging industry and the fact that some taxable income will be phantom income, which is taxable income that is not matched by cash flow to us. Due to some transactions entered into in years prior to the REIT conversion, we could recognize substantial amounts of phantom income. It is possible that these timing differences could require us to borrow funds or to issue additional equity to enable us to meet the distribution requirement and, therefore, to maintain our REIT status, and to avoid the nondeductible excise tax. In addition, because the REIT distribution requirements prevent us from retaining earnings, we will generally be required to refinance debt that matures with additional debt or equity. We cannot assure you that any of the sources of funds, if available at all, would be sufficient to meet our distribution and tax obligations.

Adverse tax consequences would apply if we failed to qualify as a REIT. We believe that we have been organized and have operated in such a manner so as to qualify as a REIT under the Internal Revenue Code, commencing with our taxable year beginning January 1, 1999, and we currently intend to continue to operate as a REIT during future years. No assurance can be provided, however, that we qualify as a REIT or that new

legislation, treasury regulations, administrative interpretations or court decisions will not significantly change the tax laws with respect to our qualification as a REIT or the federal income tax consequences of our REIT qualification. If we fail to qualify as a REIT, we will not be allowed to take a deduction for distributions to stockholders in computing our taxable income, and we will be subject to Federal and state income tax, including any applicable alternative minimum tax, on our taxable income at regular corporate rates. In addition, unless entitled to statutory relief, we would not qualify as a REIT for the four taxable years following the year during which REIT qualification is lost. Any determination that we do not qualify as a REIT would have a materially adverse effect on our results of operations and could reduce the value of our common stock materially. The additional tax liability to us for the year or years in which we did not qualify would reduce our net earnings available for investment, debt service or distribution to our stockholders. Furthermore, we would no longer be required to make any distributions to stockholders as a condition to REIT qualification and all of our distributions to stockholders would be taxable as regular corporate dividends to the extent of our current and accumulated earnings and profits, or E&P. This means that stockholders taxed as individuals currently would be taxed on those dividends at capital gains rates and corporate stockholders generally would be entitled to the dividends received deduction with respect to such dividends, subject in each case, to applicable limitations under the Internal Revenue Code. Our failure to qualify as a REIT also would cause an event of default under our credit facility that could lead to an acceleration of the amounts due under the credit facility, which, in turn, would constitute an event of default under our outstanding debt securities.

If our leases are not respected as true leases for Federal income tax purposes, we would fail to qualify as a REIT. To qualify as a REIT, we must satisfy two gross income tests, under which specified percentages of our gross income must be passive income, like rent. For the rent paid pursuant to the leases, which constitutes substantially all of our gross income, to qualify for purposes of the gross income tests, the leases must be respected as true leases for Federal income tax purposes and not be treated as service contracts, joint ventures or some other type of arrangement. In addition, the lessees must not be regarded as related party tenants, as defined in the Internal Revenue Code. We believe that the leases will be respected as true leases for Federal income tax purposes. There can be no assurance, however, that the IRS will agree with this view. We also believe that Crestline Capital Corporation, the lessee of substantially all of our full service hotels prior to January 1, 2001, was not a related party tenant and, as a result of changes in the tax laws effective January 1, 2001, HMT Lessee, LLC, or HMT Lessee, will not be treated as a related party tenant so long as it qualifies as a taxable REIT subsidiary. If the leases were not respected as true leases for federal income tax purposes or if the lessees were regarded as related party tenants, we would not be able to satisfy either of the two gross income tests applicable to REITs and we would lose our REIT status. See Risk Factors Federal Income Tax Risks Adverse tax consequences would apply if we failed to qualify as a REIT above.

If HMT Lessee fails to qualify as a taxable REIT subsidiary, we would fail to qualify as a REIT. For our taxable years beginning on and after January 1, 2001, as a result of REIT tax law changes under the specific provisions of the Ticket to Work and Work Incentives Improvement Act of 1999, which we refer to as the REIT Modernization Act , we are permitted to lease our hotels to a subsidiary of the Operating Partnership that is taxable as a corporation and that elects to be treated as a taxable REIT subsidiary. Accordingly, HMT Lessee has directly or indirectly acquired all of the full-service hotel leasehold interests from third parties. So long as HMT Lessee and other affiliated lessees qualify as taxable REIT subsidiaries of ours, they will not be treated as related party tenants. We believe that HMT Lessee qualifies to be treated as a taxable REIT subsidiary for Federal income tax purposes. We cannot assure you, however, that the IRS will not challenge its status as a taxable REIT subsidiary for Federal income tax purposes, or that a court would not sustain such a challenge. If the IRS were successful in disqualifying HMT Lessee from treatment as a taxable REIT subsidiary, we would fail to meet the asset tests applicable to REITs and substantially all of our income would fail to qualify for the gross income tests and, accordingly, we would cease to qualify as a REIT. See Risk Factors Federal Income Tax Risks Adverse tax consequences would apply if we failed to qualify as a REIT above.

Despite our REIT status, we remain subject to various taxes, including substantial deferred and contingent tax liabilities. Notwithstanding our status as a REIT, we are subject, through our ownership interest

Table of Contents

in the Operating Partnership, to certain Federal, state, local and foreign taxes on our income and property. In addition, we will be required to pay Federal income tax at the highest regular corporate rate upon our share of any built-in gain recognized as a result of any sale before January 1, 2009, by the Operating Partnership of assets, including the hotels, in which interests were acquired by the Operating Partnership from our predecessor and its subsidiaries as part of our conversion into a REIT (referred to as the REIT Conversion). Built-in gain is the amount by which an asset s fair market value exceeded our adjusted basis in the asset on January 1, 1999, the first day of our first taxable year as a REIT. The total amount of gain on which we would be subject to corporate income tax if the assets that we held at the time of the REIT Conversion were sold in a taxable transaction prior to January 1, 2009 would be material to us. In addition, at the time of the REIT Conversion, we expected that we or Rockledge Hotel Properties, Inc. or Fernwood Hotel Assets, Inc., or Rockledge and Fernwood, respectively (each of which is a taxable corporation in which the Operating Partnership owned a 95% nonvoting interest and, as of April, 2001, acquired 100% of the voting interests and each of which elected to be a taxable REIT subsidiary effective January 1, 2001), likely would recognize substantial built-in gain and deferred tax liabilities in the next ten years without any corresponding receipt of cash by us or the Operating Partnership. We may have to pay certain state income taxes because not all states treat REITs the same as they are treated for federal income tax purposes. We may also have to pay certain foreign taxes to the extent we own assets or conduct operations in foreign jurisdictions. The Operating Partnership is obligated under its partnership agreement to pay all such taxes (and any related interest and penalties) incurred by us, as well as any liabilities that the IRS or the tax authorities successfully may assert against us for corporate income taxes for taxable years prior to the time we qualified as a REIT. Our taxable REIT subsidiaries, including Rockledge, Fernwood and HMT Lessee, are taxable as corporations and will pay federal, state and local income tax on their net income at the applicable corporate rates, and foreign taxes to the extent they own assets or conduct operations in foreign jurisdictions.

If the IRS were to challenge successfully the Operating Partnership s status as a partnership for federal income tax purposes, we would cease to qualify as a REIT and suffer other adverse consequences. We believe that the Operating Partnership qualifies to be treated as a partnership for federal income tax purposes. As a partnership, it is not subject to federal income tax on its income. Instead, each of its partners, including us, is required to pay tax on its allocable share of the Operating Partnership s income. No assurance can be provided, however, that the IRS will not challenge its status as a partnership for federal income tax purposes, or that a court would not sustain such a challenge. If the IRS were successful in treating the Operating Partnership as a corporation for tax purposes, we would fail to meet the income tests and certain of the asset tests applicable to REITs and, accordingly, cease to qualify as a REIT. If the Operating Partnership fails to qualify as a partnership for federal income tax purposes or we fail to qualify as a REIT, either failure would cause an event of default under our credit facility that, in turn, could constitute an event of default under our outstanding debt securities. Also, the failure of the Operating Partnership to qualify as a partnership would cause it to become subject to federal and state corporate income tax, which would reduce significantly the amount of cash available for debt service and for distribution to its partners, including us. Finally, the classification of the Operating Partnership as a corporation would cause us to recognize gain at least equal to our negative capital account, if any.

As a REIT, we are subject to limitations on our ownership of debt and equity securities. Subject to the exceptions discussed in this paragraph, a REIT is prohibited from owning securities in any one issuer to the extent that the value of those securities exceeds 5% of the value of the REIT s total assets or the securities owned by the REIT represent more than 10% of the issuer s outstanding voting securities or more than 10% of the value of the issuer s outstanding securities. A REIT is permitted to own securities of a subsidiary in an amount that exceeds the 5% value test and the 10% vote or value test if the subsidiary elects to be a taxable REIT subsidiary, which is taxable as a corporation. However, a REIT may not own securities of taxable REIT subsidiaries that represent in the aggregate more than 20% of the value of the REIT s total assets.

Our taxable REIT subsidiaries are subject to special rules that may result in increased taxes. Several Internal Revenue Code provisions ensure that a taxable REIT subsidiary is subject to an appropriate level of federal income taxation. For example, a taxable REIT subsidiary is limited in its ability to deduct interest payments made to an affiliated REIT. In addition, the REIT has to pay a 100% penalty tax on some payments

that it receives if the economic arrangements between the REIT and the taxable REIT subsidiary are not comparable to similar arrangements between unrelated parties.

We may be required to pay a penalty tax upon the sale of a hotel. The 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 existing law, whether property, including hotels, is held as inventory or primarily for sale to customers in the ordinary course of business is a question of fact that depends upon all of the facts and circumstances with respect to the particular transaction. The Operating Partnership intends that it and its subsidiaries will hold the hotels for investment with a view to long-term appreciation, to engage in the business of acquiring and owning hotels and to make occasional sales of hotels as are consistent with the Operating Partnership s investment objectives. We cannot assure you, however, that the IRS might not contend that one or more of these sales is subject to the 100% penalty tax.

Table of Contents

WHERE YOU CAN FIND MORE INFORMATION

We are subject to the informational requirements of the Securities Exchange Act of 1934 and, in accordance therewith, file annual, quarterly and current reports, proxy statements and other information with the SEC. Such reports, proxy statements and other information can be inspected and copied at the Public Reference Room of the SEC located at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. Copies of such material can be obtained from the Public Reference Section of the SEC at prescribed rates. Such material may also be accessed electronically by means of the SEC s home page on the internet (http://www.sec.gov) and on our website (http://www.hostmarriott.com). You can also inspect reports and other information we file with the SEC at the office of the New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005.

We have filed a registration statement and related exhibits with the SEC under the Securities Act of 1933, as amended (the Securities Act). The registration statement contains additional information about us and our common stock. You can inspect or access electronically the registration statement and exhibits by the means described in the paragraph above.

The SEC allows us to incorporate by reference information that we file with it, which means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is an important part of this prospectus and the information that we file later with the SEC may update and supersede the information we incorporated by reference. We incorporate by reference the documents listed below and any filings made by us with the SEC pursuant to Section 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of this prospectus and before we stop offering the securities under this prospectus (in each case, other than information in such documents that is deemed not to be filed):