Sunstone Hotel Investors, Inc.
Form 10-Q
August 05, 2009
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the quarterly period ended June 30, 2009

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 001-32319

Sunstone Hotel Investors, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Maryland	**20-1296886**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification Number)**
903 Calle Amanecer, Suite 100 San Clemente, California	**92673**
(Address of Principal Executive Offices)	**(Zip Code)**

Registrant s telephone number, including area code: (949) 369-4000

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

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

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

Large accelerated filer x	Accelerated filer ¨	Non-accelerated filer ¨ (Do not check if a smaller reporting company)	Smaller reporting company ¨

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

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

75,170,261 shares of Common Stock, $0.01 par value, as of August 3, 2009

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SUNSTONE HOTEL INVESTORS, INC.

QUARTERLY REPORT ON

FORM 10-Q

For the Quarterly Period Ended June 30, 2009

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements

SUNSTONE HOTEL INVESTORS, INC.

CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

	June 30, 2009 (unaudited)	December 31, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 195,073	$ 176,898
Restricted cash	44,925	40,536
Accounts receivable, net	29,475	34,198
Due from affiliates	92	109
Inventories	2,553	2,781
Prepaid expenses	6,436	7,245
Investment in hotel properties of discontinued operations, net	7,745	78,646
Investment in hotel property of operations held for non-sale disposition, net	29,303	
Other current assets of discontinued operations, net	870	2,000
Other current assets of operations held for non-sale disposition, net	3,620	2,790
Total current assets	320,092	345,203
Investment in hotel properties, net	2,190,619	2,282,963
Investment in hotel property of operations held for non-sale disposition, net		91,202
Other real estate, net	14,176	14,640
Investments in unconsolidated joint ventures	26,693	28,770
Deferred financing costs, net	9,153	11,291
Goodwill	8,659	13,404
Other assets, net	12,833	18,138
Total assets	$ 2,582,225	$ 2,805,611
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	$ 20,936	$ 17,104
Accrued payroll and employee benefits	7,382	7,472
Due to Interstate SHP	14,876	16,088
Dividends payable	5,138	12,499
Other current liabilities	27,722	30,194
Current portion of notes payable	18,668	13,002
Current portion of note payable of operations held for non-sale disposition	65,000	
Other current liabilities of discontinued operations	564	2,980
Other current liabilities of operations held for non-sale disposition	2,504	2,120
Total current liabilities	162,790	101,459
Notes payable, less current portion	1,431,149	1,618,256
Note payable, less current portion of operations held for non-sale disposition		65,000
Other liabilities	6,562	6,388

Total liabilities	1,600,501	1,791,103
Commitments and contingencies *(Note 13)*		
Preferred stock, Series C Cumulative Convertible Redeemable Preferred Stock, $0.01 par value, 4,102,564 shares authorized, issued and outstanding at June 30, 2009 and December 31, 2008, liquidation preference of $24.375 per share	99,796	99,696
Stockholders equity:		
Preferred stock, $0.01 par value, 100,000,000 shares authorized. 8.0% Series A Cumulative Redeemable Preferred Stock, 7,050,000 shares issued and outstanding at June 30, 2009 and December 31, 2008, stated at liquidation preference of $25.00 per share	176,250	176,250
Common stock, $0.01 par value, 500,000,000 shares authorized, 73,841,451 shares issued and outstanding at June 30, 2009 and 47,864,654 shares issued and outstanding at December 31, 2008	738	479
Additional paid in capital	959,157	829,274
Retained earnings	136,964	260,659
Cumulative dividends	(387,253)	(347,922)
Accumulated other comprehensive loss	(3,928)	(3,928)
Total stockholders equity	881,928	914,812
Total liabilities and stockholders equity	$ 2,582,225	$ 2,805,611

See accompanying notes to consolidated financial statements.

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SUNSTONE HOTEL INVESTORS, INC.

UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

	Three Months Ended June 30, 2009	Three Months Ended June 30, 2008	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
REVENUES				
Room	$ 120,325	$ 157,589	$ 235,898	$ 294,272
Food and beverage	48,173	62,882	97,046	118,838
Other operating	14,303	14,736	27,772	29,720
Total revenues of operations held for non-sale disposition	4,013	6,644	7,703	12,247
Total revenues	186,814	241,851	368,419	455,077
OPERATING EXPENSES				
Room	28,614	33,038	55,760	63,807
Food and beverage	34,871	42,984	69,793	84,566
Other operating	7,066	8,159	14,779	16,502
Advertising and promotion	10,841	11,975	22,136	23,776
Repairs and maintenance	7,849	8,485	15,796	16,881
Utilities	6,995	8,188	15,179	16,532
Franchise costs	6,759	8,788	13,081	15,785
Property tax, ground lease, and insurance	12,784	12,818	24,127	25,704
Property general and administrative	21,129	25,472	42,421	49,932
Corporate overhead	4,849	5,244	10,608	11,929
Depreciation and amortization	27,377	26,602	54,492	53,932
Total operating expenses of operations held for non-sale disposition	4,660	5,786	9,350	11,512
Goodwill and other impairment losses	66,977		70,693	
Impairment loss of operations held for non-sale disposition	60,046		60,046	
Total operating expenses	300,817	197,539	478,261	390,858
Operating income (loss)	(114,003)	44,312	(109,842)	64,219
Equity in net losses of unconsolidated joint ventures	(584)	(56)	(2,101)	(1,522)
Interest and other income	254	1,101	876	1,679
Interest expense	(23,116)	(24,429)	(46,748)	(48,761)
Interest expense of operations held for non-sale disposition	(1,011)	(1,012)	(2,012)	(2,024)
Gain on extinguishment of debt	26,559		54,579	
Income (loss) from continuing operations	(111,901)	19,916	(105,248)	13,591
Income (loss) from discontinued operations	(18,304)	48,439	(18,447)	54,957
NET INCOME (LOSS)	(130,205)	68,355	(123,695)	68,548
Dividends paid on unvested restricted stock compensation		(224)	(447)	(463)
Preferred stock dividends and accretion	(5,188)	(5,232)	(10,375)	(10,464)
		(433)		(172)

Undistributed income allocated to unvested restricted stock compensation								
Undistributed income allocated to Series C preferred stock				(2,772)				(1,101)
INCOME AVAILABLE (LOSS ATTRIBUTABLE) TO COMMON STOCKHOLDERS	$	(135,393)	$	59,694	$	(134,517)	$	56,348
Basic per share amounts:								
Income (loss) from continuing operations available (attributable) to common stockholders	$	(1.92)	$	0.19	$	(2.05)	$	0.02
Income (loss) from discontinued operations		(0.31)		0.84		(0.33)		0.94
Basic income available (loss attributable) to common stockholders per common share	$	(2.23)	$	1.03	$	(2.38)	$	0.96
Diluted per share amounts:								
Income (loss) from continuing operations available (attributable) to common stockholders	$	(1.92)	$	0.19	$	(2.05)	$	0.02
Income (loss) from discontinued operations		(0.31)		0.83		(0.33)		0.94
Diluted income available (loss attributable) to common stockholders per common share	$	(2.23)	$	1.02	$	(2.38)	$	0.96
Weighted average common shares outstanding:								
Basic		60,845		58,186		56,549		58,452
Diluted		60,845		58,276		56,549		58,546
Dividends declared per common share	$		$	0.35	$		$	0.70

See accompanying notes to consolidated financial statements.

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SUNSTONE HOTEL INVESTORS, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY

(In thousands, except share data)

	Preferred Stock		Common Stock						
	Number of Shares	Amount	Number of Shares	Amount	Additional Paid in Capital	Retained Earnings	Cumulative Dividends	Accumulated Other Comprehensive Loss	Total
Balance at December 31, 2008	7,050,000	$ 176,250	47,864,654	$ 479	$ 829,274	$ 260,659	$ (347,922)	$ (3,928)	$ 914,812
Net proceeds from sale of common stock (unaudited)			20,700,000	207	98,491				98,698
Vesting of restricted common stock (unaudited)			227,640	2	2,486				2,488
Common stock dividends at $0.60 per share year to date (unaudited)			5,049,157	50	29,006		(29,056)		
Series A preferred dividends and dividends payable at $1.00 per share year to date (unaudited)							(7,050)		(7,050)
Series C preferred dividends and dividends payable at $0.786 per share year to date (unaudited)							(3,225)		(3,225)
Accretion of discount on Series C preferred stock (unaudited)					(100)				(100)
Net loss and comprehensive loss (unaudited)						(123,695)			(123,695)
Balance at June 30, 2009 (unaudited)	7,050,000	$ 176,250	73,841,451	$ 738	$ 959,157	$ 136,964	$ (387,253)	$ (3,928)	$ 881,928

See accompanying notes to consolidated financial statements.

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SUNSTONE HOTEL INVESTORS, INC.

UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Six Months Ended June 30, 2009	Six Months Ended June 30, 2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income (loss)	$ (123,695)	$ 68,548
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Bad debt expense	230	255
(Gain) loss on sale of hotel properties and other assets	12,716	(42,108)
Gain on extinguishment of debt	(54,579)	
Depreciation	58,261	59,086
Amortization of deferred franchise fees and other intangibles	215	2,061
Amortization of deferred financing costs	1,204	838
Amortization of loan discounts	1,339	1,725
Amortization of deferred stock compensation	2,348	2,138
Goodwill and other impairment losses	135,657	
Equity in net losses of unconsolidated joint ventures	2,101	1,522
Changes in operating assets and liabilities:		
Restricted cash	(3,943)	(3,855)
Accounts receivable	5,337	1,560
Due from affiliates	17	854
Inventories	455	200
Prepaid expenses and other assets	2,379	4,148
Accounts payable and other liabilities	(2,638)	(377)
Accrued payroll and employee benefits	(780)	(7,646)
Due to Interstate SHP	(1,212)	(1,451)
Discontinued operations	173	698
Operations held for non-sale disposition	(925)	(938)
Net cash provided by operating activities	34,660	87,258
CASH FLOWS FROM INVESTING ACTIVITIES		
Proceeds from sale of hotel properties and other assets	56,289	358,761
Cash proceeds held by accommodator		(361,017)
Restricted cash replacement reserve	(515)	8,514
Cash received from unconsolidated joint ventures		5,107
Acquisitions of hotel properties		25
Renovations and additions to hotel properties and other real estate	(26,059)	(59,696)
Net cash provided by (used in) investing activities	29,715	(48,306)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from common stock offering	103,500	
Payment of common stock offering costs	(4,802)	
Payment for repurchases of outstanding common stock		(11,827)
Proceeds from notes payable	60,000	40,000
Payments on notes payable	(66,781)	(44,048)
Payments for repurchases of notes payable and costs	(117,377)	
Payments of deferred financing costs	(3,104)	(10)
Dividends paid	(17,636)	(51,779)

Net cash used in financing activities		(46,200)		(67,664)
Net increase (decrease) in cash and cash equivalents		18,175		(28,712)
Cash and cash equivalents, beginning of period		176,898		64,967
Cash and cash equivalents, end of period	$	195,073	$	36,255
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION				
Cash paid for interest	$	49,995	$	49,255
NONCASH INVESTING ACTIVITY				
Amortization of deferred stock compensation construction activities	$	124	$	332
Amortization of deferred stock compensation unconsolidated joint venture	$	16	$	64
NONCASH FINANCING ACTIVITY				
Issuance of stock dividend	$	29,056	$	
Dividends payable	$	5,138	$	25,775

See accompanying notes to consolidated financial statements.

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SUNSTONE HOTEL INVESTORS, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Organization and Description of Business

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

As a REIT, certain tax laws limit the amount of non-qualifying income the Company can earn, including income derived directly from the operation of hotels. As a result, the Company leases all of its hotels to its TRS Lessee, which in turn enters into long-term management agreements with third parties to manage the operations of the Company s hotels. As of June 30, 2009, the Company owned 41 hotels, and its third-party managers included Sunstone Hotel Properties, Inc., a division of Interstate Hotels & Resorts, Inc. (Interstate SHP), manager of 23 of the Company s hotels; subsidiaries of Marriott International, Inc. or Marriott Hotel Services, Inc. (collectively, Marriott), managers of 13 of the Company s hotels; and Hyatt Corporation (Hyatt), Fairmont Hotels & Resorts (U.S.) (Fairmont), Hilton Hotels Corporation (Hilton) and Starwood Hotels & Resorts Worldwide, Inc. (Starwood), collectively manager of five of the Company s hotels. In addition to its wholly owned hotels, the Company has a 38% equity interest in a joint venture that owns one hotel.

2. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying consolidated financial statements as of June 30, 2009 and December 31, 2008, and for the three and six months ended June 30, 2009 and 2008, include the accounts of the Company, the Operating Partnership, the TRS Lessee and their subsidiaries. All significant intercompany balances and transactions have been eliminated.

The accompanying interim financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) and in conformity with the rules and regulations of the Securities and Exchange Commission. In the Company s opinion, the interim financial statements presented herein reflect all adjustments, consisting solely of normal and recurring adjustments, which are necessary to fairly present the interim financial statements. These financial statements should be read in conjunction with the financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended December 31, 2008, filed with the Securities and Exchange Commission on February 12, 2009. Certain prior period amounts have been reclassified to conform to the current presentation, including changes resulting from the adoptions of FSP APB 14-1 (defined below) and FSP EITF 03-6-1 (defined below), as well as from the reclassification of the W San Diego Hotel to operations held for non-sale disposition discussed later in this Note 2.

The Company has evaluated subsequent events through the date of issuance of these financial statements, August 5, 2009.

Adjustment of Previously Issued Financial Statements

In May 2008, the Financial Accounting Standards Board (FASB) issued Staff Position No. APB 14-1, *Accounting for Convertible Debt Instruments that may be Settled in Cash Upon Conversion* (FSP APB 14-1). FSP APB 14-1 requires that the liability and equity components of convertible debt instruments that may be settled in cash upon conversion (including partial cash settlement) be separately accounted for in a manner that reflects an issuer s non-convertible debt borrowing rate at the time of issuance. As a result, the liability component is recorded at a discount reflecting its below market interest rate. The liability component is subsequently accreted to its par value over its expected life based on a rate of interest that reflects the issuer s non-convertible debt borrowing rate at the time of issuance, and is reflected in the results of operations as interest expense. FSP APB 14-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008, and interim periods within those fiscal years. Retrospective application to all periods presented is required and early adoption was prohibited. The Operating Partnership s 4.60% exchangeable senior notes due 2027 (the Senior Notes) are within the scope of FSP APB 14-1. This change in methodology affects the Company s calculations of net income and earnings per share as the interest rate increases to 6.5% based on the Company s non-convertible debt borrowing rate at the time of issuance. This change in methodology does not increase the Company s cash interest payments.

On January 1, 2009, the Company adopted FASB Staff Position No. EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* (FSP EITF 03-6-1). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment awards are participating securities prior to vesting, and therefore, need to be included in the earnings allocation when computing earnings per share under the two-class method as described in FASB Statement No. 128,

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Earnings per Share (FAS 128). In accordance with FSP EITF 03-6-1, unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. Upon adoption, all prior-period earnings per share data presented were adjusted retrospectively.

In June 2009, the Company elected to cease the subsidization of debt service on the non-recourse mortgage for its W San Diego Hotel, or the hotel, which resulted in a default under the mortgage. As a consequence of the significant and continuing deterioration in demand for luxury lodging and the introduction of numerous new competitive hotels in the San Diego market, the Company believes the value of the hotel is now significantly less than the principal amount of the mortgage. Prior to electing this default, the Company made several attempts to work with the special servicer handling the W San Diego Hotel s loan to amend the terms of the mortgage to provide for a reduction in current interest payments. The special servicer declined the Company s proposed modifications. At this point, the Company does not expect further negotiation with the special servicer, and the Company is prepared to convey the hotel to the lender in lieu of repayment of the debt. In conjunction with this default, the Company has reclassified the assets, liabilities and results of operations of the W San Diego Hotel to operations held for non-sale disposition on its balance sheets, statements of operations and statements of cash flows.

As a result of the adoptions of FSP APB 14-1 and FSP EITF 03-6-1 on January 1, 2009 and the reclassification of the W San Diego Hotel to operations held for non-sale disposition, the Company has restated its December 31, 2008 consolidated balance sheet, as well as its statement of operations for the three and six months ended June 30, 2008, as follows (in thousands, except per share data):

		Adjustments		
	As previously reported (1)	FSP APB 14-1	FSP EITF 03-6-1	As adjusted
As of December 31, 2008:				
Notes payable, less current portion	$ 1,634,763	$ (16,507)	$	$ 1,618,256
Additional paid in capital	$ 807,475	$ 21,799	$	$ 829,274
Retained earnings	$ 265,951	$ (5,292)	$	$ 260,659
For the three months ended June 30, 2008:				
Interest expense	$ 23,566	$ 863	$	$ 24,429
Net income	$ 69,218	$ (863)	$	$ 68,355
Net income per share basic	$ 1.05	$ (0.02)	$	$ 1.03
Net income per share diluted	$ 1.05	$ (0.02)	$ (0.01)	$ 1.02
For the six months ended June 30, 2008:				
Interest expense	$ 47,036	$ 1,725	$	$ 48,761
Net income	$ 70,273	$ (1,725)	$	$ 68,548
Net income per share basic and diluted	$ 1.00	$ (0.03)	$ (0.01)	$ 0.96

(1) The amounts shown in the As previously reported column have been adjusted to reflect the reclassification of the W San Diego Hotel to operations held for non-sale disposition.

Use of Estimates

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

Reporting Periods

The results the Company reports in its consolidated statements of operations are based on results reported to the Company by its hotel managers. These hotel managers use different reporting periods. Marriott uses a fiscal year ending on the Friday closest to December 31 and reports twelve weeks of operations for each of the first three quarters of the year, and sixteen or seventeen weeks of operations for the fourth quarter of the year. The Company s other hotel managers report operations on a standard monthly calendar. The Company has elected to adopt quarterly close periods of March 31, June 30 and September 30, and an annual year end of December 31. As a result, the Company s 2009 results of operations for the Marriott-managed hotels include results from January 3 through March 27 for the first quarter, March 28 through June 19 for the second quarter, June 20 through September 11 for the third quarter, and September 12 through January 1 for the fourth quarter. The Company s 2008 results of operations for the Marriott- managed hotels include results from December 29 through March 21 for the first quarter, March 22 through June 13 for the second quarter, June 14 through September 5 for the third quarter, and September 6 through January 2 for the fourth quarter.

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Fair Value of Financial Instruments

As of June 30, 2009 and December 31, 2008, the carrying amount of certain financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses were representative of their fair values due to the short-term maturity of these instruments.

Effective January 1, 2008, the Company adopted FASB Statement No. 157, *Fair Value Measurements* (FAS 157) for financial assets and liabilities, and effective January 1, 2009, the Company adopted FAS 157 for all nonfinancial assets and liabilities. FAS 157 establishes a framework for measuring fair value and expands disclosures about fair value measurements by establishing a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and lowest priority to unobservable inputs (Level 3 measurements). The three levels of the fair value hierarchy under FAS 157 are described below:

Basis of Fair Value Measurement

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

The Company currently pays the premiums for a $5,000,000 split life insurance policy for its former Chief Executive Officer and current Executive Chairman, Robert A. Alter. Under the terms of the policy, the Company is entitled to receive the greater of the cash surrender value of the policy or the premiums paid by the Company following the termination of Mr. Alter s employment with the Company. Within 60 days following the date of the termination of the split dollar policy during Mr. Alter s lifetime, Mr. Alter may obtain a release of such obligation by paying the Company the greater of the total amount of the premiums paid by the Company or the then-current cash surrender value. The Company has valued this policy using Level 1 measurements at $1.7 million as of both June 30, 2009 and December 31, 2008. These amounts are included in other assets, net in the accompanying balance sheets.

The Company also has a Retirement Benefit Agreement with Mr. Alter. Pursuant to the Retirement Benefit Agreement, Mr. Alter may defer a portion of his compensation. Mr. Alter may amend the amount of his compensation to be deferred from time to time; provided, however, that any such amendment must be in compliance with Section 409A of the Internal Revenue Code. The Company will match 50% of Mr. Alter s deferrals for each year, up to a maximum of $1,500 for that year. Earnings on Mr. Alter s deferrals and the Company s matching contributions are an amount equal to the amount which would have been earned on such deferrals and matching contributions had they been paid as premiums on the life insurance policy noted above in accordance with the investment designations made by Mr. Alter. The balance in Mr. Alter s deferred compensation account is payable over a period of time following the termination of his employment with the Company, regardless of the reason for such termination. The Company has valued this agreement using Level 1 measurements at $1.7 million as of both June 30, 2009 and December 31, 2008. These amounts are included in accrued payroll and employee benefits in the accompanying balance sheets.

The Company has analyzed the carrying values of its hotel properties using Level 3 measurements, including a discounted cash flow analysis to estimate the fair value of its hotel properties taking into account each property s expected cash flow from operations, holding period and estimated proceeds from the disposition of the property. The factors addressed in determining estimated proceeds from disposition included anticipated operating cash flow in the year of disposition and terminal capitalization rate.

The Company has analyzed the carrying value of its goodwill using Level 3 measurements, including a discounted cash flow analysis taking into account each related property s expected cash flow from operations, holding period and proceeds from the potential disposition of the property. The factors addressed in determining estimated proceeds from disposition include anticipated operating cash flow in the year of potential disposition and terminal capitalization rate. The Company s judgment is required in determining the discount rate applied to estimated cash flows, the terminal capitalization rate, the growth rate of each property s projected revenues and expenses, the need for capital expenditures, as well as specific market and economic conditions.

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As of June 30, 2009 and December 31, 2008, all of the Company s outstanding debt had fixed interest rates. The Company s carrying value of its debt, including the W San Diego Hotel, totaled $1.5 billion and $1.7 billion as of June 30, 2009 and December 31, 2008, respectively. Using Level 3 measurements, the Company estimates that the fair market value of its debt as of June 30, 2009 and December 31, 2008 totaled $1.2 billion and $1.4 billion, respectively.

The following table presents the impairment charges recorded as a result of applying Level 3 measurements included in earnings for the three and six months ended June 30, 2009 and 2008 (in thousands):

	Three Months Ended June 30, 2009 (Unaudited)	Three Months Ended June 30, 2008 (Unaudited)	Six Months Ended June 30, 2009 (Unaudited)	Six Months Ended June 30, 2008 (Unaudited)
Investment in hotel properties, net	$ 64,415	$	$ 64,532	