ROYAL CARIBBEAN CRUISES LTD
Form 20-F
April 08, 2002

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark One)

[ ]
REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934
OR
[X]
ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the fiscal year ended December 31, 2001 OR
[ ]
TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number: 1-11884

ROYAL CARIBBEAN CRUISES LTD.

(Exact name of Registrant as specified in its charter)

Republic of Liberia

(Jurisdiction of incorporation or organization)

1050 Caribbean Way, Miami, Florida 33132

(Address of principal executive offices)

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

Title of each class	Name of each exchange on which registered
Common Stock, par value $.01 per share	New York Stock Exchange

Liquid Yield Option Notes due February 2, 2021	New York Stock Exchange
Zero Coupon Convertible Notes due May 18, 2021	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report: As of December 31, 2001, the Registrant had outstanding 192,310,198 shares of common stock, par value $.01 per share.

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 o

Indicate by check mark which financial statement item the registrant has elected to follow:

Item 17 o Item 18 x

ROYAL CARIBBEAN CRUISES LTD.

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PART I

As used in this Annual Report on Form 20-F, the terms Royal Caribbean, the Company, we, our and us refe Royal Caribbean Cruises Ltd., the term Celebrity refers to Celebrity Cruise Lines Inc. and the terms Royal Caribbean International and Celebrity Cruises refer to our two cruise brands. In accordance with cruise industry practice, the term berths is determined based on double occupancy per cabin even though some cabins can accommodate three or four guests.

Item 1. *Identity of Directors, Senior Management and Advisers*

Not applicable.

Item 2. *Offer Statistics and Expected Timetable*

Not applicable.

Item 3. *Key Information*

Selected Financial Data

The following selected financial data are for each of the fiscal years in the period 1997 through 2001 and as of the end of each such fiscal year. The financial information presented for fiscal years 2001, 2000, and 1999 and as of the end of fiscal years 2001 and 2000 is derived from our financial statements and should be read together with such financial statements and the related notes included elsewhere herein. The 1997 financial information includes the results of Celebrity commencing July 1, 1997.

	Year Ended December 31,				
	2001	2000	1999	1998	1997
	(in thousands, except per share data)				
Operating Data:					
Revenues	$3,145,250	$2,865,846	$2,546,152	$2,636,291	$1,939,007
Operating income	455,605	569,540	480,174	488,735	303,555
Income before extraordinary item	254,457	445,363	383,853	330,770	182,685
Net income	254,457	445,363	383,853	330,770	175,127
Per Share Data Diluted:					
Operating income	$2.35	$2.95	$2.58	$2.70	$1.99
Income before extraordinary item	$1.32	$2.31	$2.06	$1.83	$1.20
Net income	$1.32	$2.31	$2.06	$1.83	$1.15
Weighted average shares and potentially dilutive shares	193,481	192,935	186,456	181,165	152,174
Dividends declared per common share					

$0.52 $0.48 $0.40 $0.34 $0.29

Balance Sheet Data:

Total assets	$10,368,782	$7,828,465	$6,380,511	$5,686,076	$5,339,748
Total debt, including capital leases	5,646,112	3,410,096	2,342,177	2,469,082	2,572,696
Common stock	1,923	1,921	1,812	1,690	811
Total shareholders equity	3,756,584	3,615,915	3,261,156	2,454,758	2,018,721

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Risk Factors

The Risk Factors noted below and elsewhere in this Annual Report on Form 20-F are important factors, among others, that could cause actual results to differ from expected or historic results. It is not possible to predict or identify all such factors. Consequently, this list should not be considered a complete statement of all potential risks or uncertainties. See Item 5. Operating and Financial Review and Prospects, for a note regarding forward-looking statements.

We may lose business to competitors throughout the vacation market

We operate in the vacation market and cruising is one of many alternatives for people choosing a vacation. We therefore risk losing business not only to other cruise lines, but also to other vacation operators which provide other leisure options including hotels, resorts and package holidays and tours.

We face significant competition from other cruise lines, both on the basis of cruise pricing and also in terms of the nature of ships and services we offer to cruise passengers. Our principal competitors within the cruise vacation industry include Carnival Corporation, which owns, among others, Carnival Cruise Lines, Holland America Line, Cunard Line and Costa Cruises; P&O Princess Cruises plc, which owns, among others, Princess Cruises, P&O Cruises, Swan Hellenic and AIDA; Star Cruises, which owns Star Cruises, Norwegian Cruise Line and Orient Line; and others.

In the event that we do not compete effectively with other vacation alternatives and cruise companies, our market share could decrease and our results of operations and financial condition could be adversely affected.

Overcapacity within the cruise vacation industry and a reduction in demand could have a negative impact on yields and may adversely affect profitability

Cruising capacity has grown in recent years and we expect it to continue to increase as all of the major cruise vacation companies are expected to introduce new ships. In order to utilize new capacity, the cruise vacation industry will need to increase its share of the overall vacation market. Failure of the cruise vacation industry to do so could have a negative impact on our yields. Should yields be negatively impacted, we could experience an adverse effect on our results of operations and financial condition.

Demand for cruises and other vacation products has been and is expected to continue to be affected by the public s attitude towards the safety of travel and the political climate of destination countries. In the future, demand for cruises is also likely to be increasingly dependent on the underlying economic strength of the countries in which cruise companies operate. Economic or political changes that reduce disposable income in the countries in which we operate may affect demand for vacations, including cruise vacations, and may lead to price discounting which, in turn, may reduce the profitability of our business.

Furthermore, events such as the terrorist attacks in the United States on September 11, 2001, the resulting political instability and concerns over safety and security aspects of traveling have had a significant adverse impact on demand and pricing in the travel and vacation industry and may continue to do so in the future.

Incidents at sea or adverse publicity concerning the cruise industry could affect our reputation and harm our future sales and profitability

The operation of cruise ships involves the risk of accidents and incidents at sea which may bring into question passenger safety and adversely affect future industry performance. While we make passenger safety our foremost priority in the design and operation of our ships, incidents involving passenger cruise ships could adversely affect future sales and profitability. In addition, adverse media publicity concerning the cruise industry in general could impact demand and consequently have an adverse impact on our profitability.

Environmental and health and safety legislation could affect operations and increase operating costs

Some environmental groups have lobbied for more stringent regulation of cruise ships. Some groups also have generated negative publicity about the cruise industry and its environmental impact. The U.S. Environmental Protection Agency is considering new laws and rules to manage cruise ship waste. Stricter environmental and health and safety regulations could affect our operations, and increase the cost of compliance and adversely affect the cruise industry. It cannot be assured that our costs of complying with current and future environmental, health and safety laws, or liabilities arising from past or future releases of, or exposure to, hazardous substances or to vessel discharges, will not materially adversely affect our business, results of operations or financial condition.

We may not be able to obtain financing on terms that are favorable or consistent with our expectations

To fund our capital expenditures and scheduled debt payments, we rely on a combination of cash flows provided by operations, drawdowns under our available credit facility, the incurrence of additional indebtedness and the sales of equity or debt securities in private or public securities markets. We also anticipate refinancing some of our debt facilities during the period of our current capital expenditure program. Our credit ratings impact our ability to obtain financing in financial markets and the terms of the financing. Any future lowering of our credit ratings may have adverse consequences on our ability to access the financial markets or on our cost of financings. Accordingly, we can not be sure that our cash flows from operations and additional financings will be available in accordance with our expectations.

Conducting business internationally may result in increased costs

We operate our business internationally and plan to continue to develop our international presence. Operating internationally exposes us to a number of risks. Examples include currency fluctuations, interest rate movements, the imposition of trade barriers and restrictions on repatriation of earnings. Additional risks include political risks and risk of increases in duties, taxes and governmental royalties as well as changes in laws and policies affecting cruising, vacation or maritime businesses or the governing operations of foreign-based companies. If we are unable to address these risks adequately, our results of operations and financial condition could be adversely affected.

Ship construction delays or faults may result in cancellation of cruises and unscheduled drydocks and repairs

We depend on the shipyards to construct and deliver our cruise ships on a timely basis and in good working order. The inherent nature of building a ship involves risks similar to those encountered in other sophisticated projects. Delays or faults in ship construction may result in delays or cancellation of cruises or necessitate unscheduled drydocks and repairs of the ship. Shipyard insolvency and other industrial actions could also delay or indefinitely postpone the timely delivery of new ships. These events together with any related adverse publicity could, to the extent they are not covered by contractual provisions or insurances, adversely affect our financial results.

Unavailability of ports of call may adversely affect our profits

We believe that port destinations are a major reason why guests choose to go on a particular cruise or on a cruise vacation. The availability of ports is affected by a number of factors, including, but not limited to, existing capacity constraints, security concerns, adverse weather conditions and natural disasters, financial limitations on port development, local governmental regulations and local community concerns about port development and other adverse impacts on their communities from additional tourists. The inability to continue to maintain and increase our ports of call could adversely affect our profits.

A change in our tax status under the U.S. Internal Revenue Code may have adverse effects on our income

We and our wholly owned subsidiary, Celebrity Cruises Inc., the operator of Celebrity Cruises, are foreign corporations engaged in a trade or business in the United States, and our vessel-owning subsidiaries are foreign corporations that, in many cases, depending upon the itineraries of their vessels, receive income from sources within the United States. However, Drinker Biddle & Reath LLP, our United States tax counsel, has delivered to us an opinion to the effect that, pursuant to Section 883 of the Internal Revenue Code, our income, the income of Celebrity Cruises Inc. and the vessel-owning subsidiaries, in each case derived from or incidental to the international operation of a ship or ships, is exempt from United States income tax. We believe that substantially all of our income, the income of Celebrity Cruises Inc. and our vessel-owning subsidiaries is derived from or incidental to the international operation of a ship or ships within the meaning of Section 883 of the Internal Revenue Code.

Our tax counsel is of the opinion based on certain representations and assumptions that we, Celebrity Cruises Inc., and our vessel-owning subsidiaries currently qualify for the Section 883 exemption because each of them is incorporated in a qualifying jurisdiction and our stock is primarily and regularly traded on an established securities market in the United States or Norway. To date, however, no final Treasury regulations or other definitive interpretations of the relevant portions of Section 883 have been promulgated, although regulations have been proposed. As noted in our tax counsel s opinion, such regulations or official interpretations could differ materially from our tax counsel s interpretation of this Internal Revenue Code provision and, even in the absence of such regulations or official interpretations, the Internal Revenue Service might successfully challenge such interpretation. In addition, the provisions of Section 883 are subject to change at any time by legislation. Moreover, changes could occur in the future with respect to the identity, residence, or holdings of our direct or indirect shareholders that could affect us and our subsidiaries eligibility for the Section 883 exemption. Accordingly, there can be no assurance that we and our subsidiaries are, and will in the future be, exempt from United States income tax on United States source shipping income.

If we, Celebrity Cruises Inc., and our vessel-owning subsidiaries were not entitled to the benefit of Section 883 of the Internal Revenue Code, each would be subject to United States taxation on a portion of its income. See *Taxation of the Company* within Item 4. for a discussion of the taxation of us, Celebrity Cruises Inc., and our vessel-owning subsidiaries in the absence of an exemption under Section 883 of the Internal Revenue Code.

We are controlled by principal shareholders that have the power to determine our policies, management and actions requiring shareholder approval

As of February 22, 2002, A. Wilhelmsen AS., a Norwegian corporation indirectly owned by members of the Wilhelmsen family of Norway, owned approximately 24.1% of our common stock and Cruise Associates, a Bahamian general partnership indirectly owned by various trusts primarily for the benefit of certain members of the Pritzker family of Chicago, Illinois, and various trusts primarily for the benefit of certain members of the Ofer family, owned approximately 25.1% of our common stock. A. Wilhelmsen AS. and Cruise Associates have the power to determine, among other things:

our policies and the policies of our subsidiaries,

the persons who will be our directors and officers and the directors and officers of our subsidiaries and

all actions requiring shareholder approval.

A. Wilhelmsen AS. and Cruise Associates are parties to a shareholders agreement. The agreement provides that our board of directors will consist of the following persons:

four nominees of A. Wilhelmsen AS.,

four nominees of Cruise Associates and

our Chief Executive Officer.

The shareholders agreement provides that the boards of directors of our subsidiaries shall have substantially similar composition. As a result of our acquisition of Celebrity, A. Wilhelmsen AS. and Cruise Associates have also agreed to vote their shares of our common stock to elect one additional director to our board of directors to be nominated by Archinav Holdings, Ltd., a former shareholder of Celebrity, for a specified period until 2004. In addition, until either of them should decide otherwise, A. Wilhelmsen AS. and Cruise Associates have agreed to vote their shares of common stock in favor of two additional named directors of our board of directors. During the term of the shareholders agreement, certain corporate actions require the approval of at least one director nominated by A. Wilhelmsen AS. and one director nominated by Cruise Associates. Our principal shareholders are not prohibited from engaging in a business that may compete with our business, subject to certain exceptions. The failure of A. Wilhelmsen AS., and Cruise Associates to continue to own a specified percentage of our common stock might obligate us to prepay indebtedness outstanding under and/or result in the termination of some of our credit facilities.

In connection with the proposed dual-listed company merger with P&O Princess Cruises plc, in December 2001, A. Wilhelmsen AS. and Cruise Associates entered into a voting agreement with, and delivered irrevocable proxies to, P&O Princess Cruises plc, obligating them to, among other things, vote an aggregate of 44.5% of our outstanding common stock held by them in favor of the transactions required to effect the dual-listed company merger.

We are not a U.S. corporation and our shareholders may be subject to the uncertainties of a foreign legal system in protecting their interests

Our corporate affairs are governed by our Restated Articles of Incorporation and By-Laws and by the Business Corporation Act of Liberia. The provisions of the Business Corporation Act of Liberia resemble provisions of the corporation laws of a number of states in the United States. However, while most states have a fairly well developed body of case law interpreting their respective corporate statutes, there are very few judicial cases in Liberia interpreting the Business Corporation Act of Liberia. For example, the rights and fiduciary responsibilities of directors under Liberian law are not as clearly established as the rights and fiduciary responsibilities of directors under statutes or judicial precedent in existence in certain United States jurisdictions. Thus, our public shareholders may have more difficulty in protecting their interests in the face of actions by the management, directors or controlling shareholders than would shareholders of a corporation incorporated in a United States jurisdiction.

Our proposed dual-listed company merger with P&O Princess Cruises plc may not be completed as contemplated. If completed as contemplated, it will have certain risks that may have an adverse effect on the performance of the combined company

We believe that our proposed dual-listed company merger with P&O Princess Cruises plc (P&O Princess) will provide us with a strong fleet profile and greater access to capital markets, and that the dual-listed company merger will create opportunities for significant costs savings and other financial and operating benefits through the planned integration of the two companies operations. However, completion of the dual-listed company merger by both Royal Caribbean and P&O Princess is subject to the satisfaction of various conditions, including approval by the shareholders of each of P&O Princess and Royal Caribbean and approvals from governmental authorities. If the dual-listed company merger is not completed by November 16, 2002, either party can terminate the agreement if it is not in material breach of its obligations thereunder.

As of this date, we are unable to estimate when or if these conditions to the dual-listed company merger will be satisfied or, if satisfied, the terms and conditions of such approvals. The governmental entities from whom approvals are required may impose conditions on the completion of the dual-listed company merger or require changes to the terms of the dual-listed company merger, which in either case could have the effect of imposing additional costs on or limiting the revenues of the combined company. Carnival Corporation has commenced a competing pre-conditional offer to acquire all of the outstanding shares of P&O Princess. Subsequent to the making of this offer by Carnival, the shareholders of P&O Princess and Royal Caribbean voted to adjourn their respective shareholder meetings that had been convened to approve the dual-listed company merger. We do not know at this time the date on which the meetings will be reconvened.

Even if the dual-listed company merger is completed as contemplated, the implementation of the merger has certain risks associated with it that may have an adverse effect on the economic performance of the combined companies or their respective share prices. We would be faced with the challenges of combining the businesses of two major corporations that have previously operated independently and the attendant risks of not achieving the expected costs savings, other financial and operating benefits or improvement in earnings. Delays or difficulties that may be encountered in connection with the dual-listed company merger and the integration of the two companies operations could divert management s attention from other strategic opportunities and from operational matters. In turn, this could have an adverse effect on the business, results of operations, financial condition or prospects of the combined company after the dual-listed company merger.

Item 4. ***Information on the Company***

History and Development of the Company

Royal Caribbean International was founded in 1968. The current parent corporation, Royal Caribbean Cruises Ltd., was incorporated on July 23, 1985 in the Republic of Liberia under the Business Corporation Act of Liberia. The address of the principal executive offices is 1050 Caribbean Way, Miami, Florida 33132; the telephone number is (305) 539-6000. Our registered agent is Michael J. Smith, Vice President, General Counsel and Secretary, 1050 Caribbean Way, Miami, Florida 33132.

We are the world s second largest cruise company with 22 cruise ships that have 45,854 berths. We operate our cruise ships through two cruise brands, Royal Caribbean International and Celebrity Cruises.

See Item 5. *Operating and Financial Review and Prospects* and the *Business Overview* sections that follow for more information regarding our history and development, significant capital expenditures, vessels under construction and methods of financing.

Business Overview

General

We operate two brands, Celebrity Cruises, which was acquired in July 1997, and Royal Caribbean International. Our brands offer a wide array of shipboard activities, services and amenities, including swimming pools, sun decks, beauty salons, exercise and massage facilities, ice skating rinks, rock climbing walls, gaming facilities, lounges, bars, show-time entertainment, retail shopping and cinemas. Our ships operate on a selection of worldwide itineraries that call on approximately 200 destinations. We compete principally on the basis of quality of service, variety of itineraries and price.

The Royal Caribbean International Brand

Royal Caribbean International serves the volume cruise vacation sector which we categorize as the contemporary and premium segments. The brand operates 14 cruise ships with 31,534 berths, offering various cruise itineraries that range from two to 16 nights and call on destinations throughout the world.

Royal Caribbean International s strategy is to attract an array of vacationing consumers in the contemporary segment by providing a wide variety of itineraries and cruise lengths with multiple options for onboard dining, entertainment, and other onboard activities. Additionally, Royal Caribbean International offers a variety of shore excursions at each port of call. We believe that the variety and quality of Royal Caribbean International s product offering represent excellent value to consumers, especially to couples and families traveling with children. Because of the brand s extensive product offerings, we believe Royal Caribbean International is well positioned to attract new consumers to the cruise industry and continue to bring past guests back for their next vacation. While the brand is positioned at the upper end of the contemporary segment, we believe that Royal Caribbean International s quality enables it to attract consumers from the premium segment as well, thereby achieving one of the broadest market coverages of any of the major brands in the cruise industry.

The Celebrity Cruises Brand

Celebrity Cruises primarily serves the premium segment. Celebrity Cruises operates eight cruise ships with 14,320 berths and offers various cruise itineraries that range from two to 17 nights.

Celebrity Cruises strategy is to attract consumers who want an enhanced cruise vacation in terms of modern vessels, gourmet dining and service, extensive and luxurious spa facilities, large staterooms and a high staff-to-guest ratio. These are hallmarks of the premium cruise vacation segment, which is Celebrity Cruises primary target. Celebrity Cruises also attracts experienced cruisers from the contemporary and luxury cruise categories. Celebrity Cruises is expanding its fleet to provide an increasing variety of itineraries and cruise lengths and therefore has a higher proportion of its fleet deployment in seasonal markets (i.e. Alaska, Bermuda, Europe and South America) than does the Royal Caribbean International brand.

Proposed Dual-Listed Company Merger with P&O Princess

On November 19, 2001, we entered into an agreement with P&O Princess, providing for the combination of Royal Caribbean and P&O Princess as a merger of equals under a dual-listed company structure. The purpose of the combination is to create what we believe would be the world s largest cruise vacation company by combining two companies with a strong strategic fit and meaningful growth opportunities. Each company would bring well known brands operating in key cruise vacation markets to the combined company. Furthermore, we believe that the combined company would have a strong fleet profile and greater access to capital markets, and that the dual-listed company structure would create opportunities for significant cost savings and other financial and operating benefits through the planned integration of the two companies operations.

The dual-listed company merger would involve a combination of the two companies through a number of contracts and certain amendments to our Articles of Incorporation and By-Laws and to P&O Princess Articles and Memorandum of Association. The two companies would retain their separate legal identities and maintain their separate stock exchange listings. Royal Caribbean shareholders would continue to hold their shares of common stock in Royal Caribbean, and P&O Princess shareholders would continue to hold their ordinary shares in P&O Princess. However, the companies would operate and be managed as if they were a single unified economic entity.

Although each of Royal Caribbean and P&O Princess would have a separate board of directors, the boards and senior executive management of each company would comprise the same individuals. The contracts governing the dual-listed company merger would provide that, as far as possible, the shareholders of Royal Caribbean and P&O Princess would be placed in substantially the same economic position as if they held shares in a single enterprise which owned all of the assets of both companies. The net effect of the dual-listed company merger would be that the shareholders of Royal Caribbean would own an economic interest equal to 49.3% of the combined company and the shareholders of P&O Princess would own an economic interest equal to 50.7% of the combined company. Special voting arrangements would be implemented so that the shareholders of both companies would vote together as a single decision-making body in proportion to their respective economic interests on matters requiring the approval of shareholders of either company. Such matters would include the appointment, removal and re-election of directors of each company. In the case of certain matters in relation to which the two bodies of shareholders may have divergent interests, the matter would require the prior approval of the shareholders of both companies, each voting separately as a class.

After completion of the dual-listed company merger, dividends declared by Royal Caribbean would continue to be paid by Royal Caribbean to its shareholders and dividends declared by P&O Princess would continue to be paid by P&O Princess to its shareholders. However, dividends and other distributions to shareholders of the two companies would be effectively equalized on a per share basis based on the prevailing equalization ratio, as determined under the contractual arrangements governing the dual-listed company merger. The payment of dividends by Royal Caribbean would depend on, among other things, the financial and business conditions of the combined company.

The obligations of Royal Caribbean and P&O Princess to effect the dual-listed company merger are subject to the satisfaction of various conditions, including the receipt of certain regulatory approvals and consents and approval by the shareholders of each of Royal Caribbean and P&O Princess. No assurance can be given that all required approvals and consents will be obtained, and if such approvals and consents are obtained, no assurance can be given as to the terms, conditions and timing of the approvals and consents. If the dual-listed company merger is not completed by November 16, 2002, either party can terminate the agreement if it is not in material breach of its obligations thereunder.

In December 2001, Carnival Corporation announced a competing pre-conditional offer to acquire all of the outstanding shares of P&O Princess. In connection with its pre-conditional offer, Carnival solicited proxies from P&O Princess shareholders in favor of an adjournment of the P&O Princess special meeting prior to a shareholder vote to approve the dual-listed company merger. On February 14, 2002, Royal Caribbean and P&O Princess convened special meetings of their respective shareholders to approve the dual-listed company merger. Prior to voting to approve the merger, the shareholders of each company voted to adjourn their respective meetings until an unspecified future date. We do not know at this time the date on which the meetings will be reconvened.

We have undertaken with P&O Princess customary covenants that place restrictions on each of us and our subsidiaries until completion of the dual-listed company merger or earlier termination of the merger agreement. In general, we are each required to conduct our respective businesses in the usual, regular and ordinary course and to use our reasonable best efforts to preserve materially intact our business organizations and present lines of business, to maintain commercially reasonable insurance, to maintain our material rights and franchises and preserve our existing material relationships with third parties.

P&O Princess and we have also agreed that each will not initiate, solicit, encourage or otherwise facilitate any inquiries or any proposal or offer relating to a merger, acquisition or other transaction involving the acquisition of 15% or more of the assets or equity securities of either P&O Princess or us. Subject to certain stated exceptions, both parties have agreed not to have any discussions with or provide any confidential information to any person relating to an acquisition proposal or otherwise facilitate any effort or attempt to make an acquisition proposal.

If the merger agreement is terminated under certain circumstances, we will be obligated to pay P&O Princess a break fee of $62.5 million. These circumstances include, among other things, our board of directors withdrawing or adversely modifying its recommendation to shareholders to approve the dual-listed company merger, our board of directors recommending an alternative acquisition transaction to shareholders, and our shareholders failing to approve the dual-listed company merger if another acquisition proposal with respect to Royal Caribbean exists at that time. Similarly, P&O Princess would be obligated to pay us a break fee of $62.5 million upon the occurrence of reciprocal circumstances.

Joint Venture with P&O Princess

On November 19, 2001, we entered into a joint venture agreement with P&O Princess to jointly create and operate a cruise line company to target customers in southern Europe. The joint venture company is owned 50% by P&O Princess and 50% by us. Each party has committed up to $500.0 million in shareholder equity, with approximately $5.0 million contributed by each party to date and the balance due and payable when called by the joint venture company. We have agreed to assign our ship-build contracts for *Serenade of the Seas* and *Jewel of the Seas* to the joint venture company, and P&O Princess has similarly agreed to assign two identified ship-build contracts to the joint venture company. The contracts will be held in trust for the joint venture company pending such assignments. Any payments the parties have made under these contracts prior to assignment will be credited against each party s respective shareholder equity commitment. Subject to the terms of the agreement, the joint venture agreement can be terminated by either party if certain commercial benchmarks have not been achieved by January 1, 2003 or April 1, 2003. The joint venture agreement does not require the approval of the shareholders of Royal Caribbean or P&O Princess.

The joint venture shareholders intend that the joint venture company be financed through third-party indebtedness and each joint venture shareholder has committed to provide necessary credit support in the form of guarantees on a pro rata basis, subject to legal or regulatory restrictions. To the extent that third-party financing cannot be obtained, and if approved in accordance with the terms of the joint venture agreement, the joint venture shareholders will provide financing on a pro rata basis on identical terms. We have obtained commitments for export financing for up to 80% of the contract price of each of the two vessels we have committed to the venture.

Under the joint venture agreement, if a change of control occurs with respect to a joint venture shareholder, the other shareholder has a right to acquire the interest of that shareholder at fair market value in exchange for preferred stock or a 15-year subordinated note (or a combination thereof) of the purchasing shareholder. Notwithstanding the foregoing, the joint venture shareholder subject to a change of control has the right, subject to certain conditions, to put its interest in the joint venture to the other joint venture shareholder at a discount to fair market value in exchange for preferred stock or a 20-year subordinated note (or a combination thereof) of the purchasing shareholder.

Industry

Since 1970, cruising has been one of the fastest growing sectors of the vacation market, as the number of North American guests has grown to an estimated 6.9 million in 2001 from 0.5 million in 1970, a compound annual growth rate of approximately 9%. We have capitalized on the increasing popularity of cruises through an extensive fleet expansion program.

According to our estimates, the North American market was served by an estimated 104 cruise ships with approximately 107,750 berths at the end of 1996. The number of berths in the industry is estimated to have increased to approximately 156,950 berths on 111 ships by the end of 2001. The net increase in capacity over the last five years is inclusive of approximately 36 ships with approximately 27,700 berths that have either been retired or moved out of the North American market. There are a number of cruise ships on order with an estimated 66,500 berths which will be placed in service between 2002 and 2005. Although we cannot predict the rate at which future retirements will occur, we believe ship retirements will continue due to competitive pressures and the age of the vessels.

The following table details the growth in the North American cruise market of both guests and weighted average berths over the past five years:

Year	North American Cruise Guests(1)	Weighted Average Supply of Berths Marketed in North America(2)
1997	5,051,000	109,257
1998	5,428,000	118,747
1999	5,894,000	130,152
2000	6,886,000	144,499
2001	6,906,000	151,690

(1) Source: Cruise Lines International Association based on guests carried for at least two consecutive nights.
(2) Source: Our estimates.

Cruise lines compete for consumers disposable leisure time spending with other vacation alternatives such as land-based resort hotels and sightseeing destinations, and public demand for such activities is influenced by general economic conditions. We believe that cruise guests currently represent only a small share of the vacation market and that a significant portion of cruise guests carried are first-time cruisers.

Our ships operate worldwide and call on destinations in Alaska, Australia/New Zealand, the Bahamas, Bermuda, Canada, the Caribbean, Europe, Hawaii, Mexico, New England, the Panama Canal, Scandinavia and South America.

Competition for cruise guests in all of these geographic areas is vigorous. In most of these areas, we compete with cruise ships owned by other international operators. We compete with a number of cruise lines; however, our principal competitors are Carnival Cruise Line, Holland America Line, Norwegian Cruise Line and Princess Cruises. We compete principally on the basis of quality of service, variety of itineraries and price.

Operating Strategies

Our principal operating strategies are to:

- improve the awareness and market penetration of both brands,
- continue to expand our fleet with state-of-the-art cruise ships,
- improve our competitive position with respect to the quality and innovation of our onboard product,
- expand into new markets and itineraries,
- further expand our international guest sourcing,
- utilize sophisticated yield management systems (revenue optimization per berth),
- further improve our technological capabilities, and
- maintain strong relationships with travel agencies, the principal industry distribution system.

Brand Awareness

Our strategy is to continue to broaden the recognition of both the Royal Caribbean International brand and the Celebrity Cruises brand in the cruise vacation sector. Each brand has a distinct identity and marketing focus but utilizes shared infrastructure resources.

We have positioned the Royal Caribbean International brand in the contemporary and premium segments of the cruise vacation sector. As such, Royal Caribbean International focuses on providing multiple choices to its guests through a variety of itineraries, accommodations, dining options, ship activities and shore excursions. Hallmarks of the brand include friendly and engaging service, modern ships, family programs, entertainment, health and fitness, and activities designed for guests of all ages.

We have positioned the Celebrity Cruises brand in the premium segment of the cruise vacation sector. The brand is recognized for its gourmet dining, impeccable service, large staterooms, a high staff-to-guest ratio and luxurious spa facilities. Among its many awards, Celebrity Cruises was voted the top one and two spots and received four of the top eight spots of 27 vessels honored in the Best Large Ships category of the 2001 Reader s Choice Awards poll by *Condé Nast Traveler*.

Fleet Expansion

Our current fleet expansion program encompasses three distinct vessel designs known as the Voyager-class, Millennium-class and Radiance-class. Since 1999, we have taken delivery of three Voyager, three Millennium, and one Radiance class vessels. We currently operate 22 ships with 45,854 berths.

Our increased average ship size and number of available berths have enabled us to achieve certain economies of scale. Larger ships allow us to transport more guests than smaller ships without a corresponding increase in certain operating expenses. This increase in fleet size also provides a larger revenue base to absorb our marketing, selling and administrative expenses.

Royal Caribbean International. Founded in 1968, Royal Caribbean International was the first cruise line to design ships especially for warm water year round cruising. Royal Caribbean International operated a modern fleet in the 1970s and early 1980s, establishing a reputation for high quality. Between 1988 and 1992, the brand tripled its capacity by embarking on its first major capital expansion program.

Royal Caribbean International committed to its second capital expansion program with orders for six Vision-class vessels, ranging in size from 1,804 to 2,000 berths, for delivery from 1995 through 1998. During this same period, Royal Caribbean International sold four of its original vessels because these ships were older in age and design and no longer consistent with its image and marketing strategy. Each Vision-class ship features a seven-deck atrium with glass elevators, skylights and glass walls, a pool and entertainment complex covered by a moveable glass roof, hundreds of cabins with verandahs, a two-deck main dining room, a state-of-the-art show theater, a glass-encased indoor/outdoor café and a shopping mall.

Royal Caribbean International is currently engaged in its third capital expansion program. It placed *Voyager of the Seas, Explorer of the Seas,* and *Adventure of the Sea*s, the first three Voyager-class vessels, in service in the fourth quarters of 1999, 2000, and 2001, respectively. Royal Caribbean International has two additional Voyager-class vessels on order. We believe these Voyager-class vessels are the largest and most innovative passenger cruise ships ever built. Each ship is approximately 140,000 gross tons with 3,114 berths. This new class of vessels is designed to provide more diverse vacation options for families and for those seeking active sports and entertainment alternatives during their vacation experience. Each Voyager-class ship has a variety of unique features: the cruise industry s first horizontal atrium (which is four decks tall, longer than a football field and provides entertainment, shopping and dining experiences), recreational activities such as ice skating, rock climbing, miniature golf and full court basketball, enhanced staterooms, expanded dining options and a variety of intimate spaces.

Royal Caribbean International took delivery of *Radiance of the Seas,* the first Radiance-class vessel, in March 2001. Royal Caribbean International has three additional Radiance-class vessels on order and options to purchase two more vessels. The Radiance-class vessels (approximately 90,000 gross tons each) are a progression from the brand s Vision-class series and have approximately 2,100 berths each. The Radiance-class ships incorporate many of the dining and entertainment options of the Voyager-class vessels, as well as offer a wide array of unique features. These features include panoramic glass elevators facing outward to the sea, floor to ceiling glass windows offering spectacular sea views, and a billiards club.

Celebrity Cruises. Celebrity Cruises was founded in 1990 and operated three ships between 1992 and 1995. Between 1995 and 1997, Celebrity Cruises undertook its first capital expansion program, adding three Century-class vessels which range in size from 1,750 to 1,850 berths and disposing of one of its original three vessels. Celebrity Cruises is currently engaged in its second capital expansion program and took delivery of *Millennium, Infinity* and *Summit,* the first three of the Millennium-class vessels, in June 2000, February 2001 and September 2001, respectively. Celebrity Cruises has one additional Millennium-class vessel, *Constellation,* on order with an expected delivery in the second quarter of 2002. Each Millennium-class ship has 2,034 berths and is approximately 90,000 gross tons.

The Millennium-class ships are a progression from the Century-class vessels, which have been widely accepted in the premium segment of the marketplace. This new class of vessels builds on the brand s primary strengths, including gourmet dining, spacious staterooms and suites complete with balconies, luxurious spa facilities and impeccable service. On the Millennium-class ships, an entire resort deck is dedicated to health, fitness and the rejuvenating powers of water. Celebrity Cruises spas are among the most luxurious spas afloat and offer a variety of features, including a large hydropool with neck massage and body jets. Guests can relax in *Notes,* the music library, smoke cigars at *Michael s Club* or stop by *The Platinum Club* for champagne and caviar.

Product Innovation

We recognize the need for new and innovative onboard products and experiences for our guests, which we develop based on guest feedback, crew suggestions and competitive product reviews. Accordingly, we continue to invest in design innovations on new ships and additional product offerings on our existing fleet. Expanded dining options, recreational activities such as ice skating and rock climbing and the latest technology such as our Internet Cafe and interactive television are among the services currently offered.

In 2001, we began the operation of Royal Celebrity Tours, a tour company offering fully-escorted, premium land tour programs in Alaska for guests traveling on our ships. We offer deluxe motorcoach and rail packages with glass-domed railcars that are among the largest in the world. We are adding a third and fourth railcar in 2002, thus doubling the number of guests we can accommodate on our Alaska rail tours. In an effort to further increase our tour presence in North America, we launched a Canadian Rockies tour program for the 2002 season and a Florida tour program for guests originating from Europe.

Worldwide Itineraries

Our ships operate worldwide with a selection of itineraries that call on approximately 200 destinations. New ships allow us to expand into new destinations, itineraries and markets. Royal Caribbean International offers the *Exotic Destinations* program which provides global cruise itineraries including Australia/New Zealand, Hawaii, and the South Pacific. Celebrity Cruises continues to deploy vessels in the European market, as a strategic initiative. Celebrity Cruises offers *Celebrity Voyages*SM with 10 to 17-night itineraries throughout the Caribbean and South America. We continue to dedicate additional capacity to shorter itineraries with the implementation of four and five-night cruises out of Ft. Lauderdale and San Juan and by establishing a Royal Caribbean International vessel year-round in Port Canaveral to provide three and four-night Bahamas cruises. In addition, both Royal Caribbean International and Celebrity Cruises are expanding their home ports to include Baltimore, Charleston, New Orleans, Galveston and Tampa.

International Guests

In connection with our global expansion, international guests have provided an increasing share of our growth. International guests have grown from approximately 7% of total guests in 1991 to approximately 20% of total guests in 2001. One of our strategies is to use fleet deployment and expanded itineraries to increase our guest sourcing outside North America. Over the past few years, we have increased our investment in information technology spending and increased our international advertising to enhance brand awareness worldwide. We carry out our international sales effort through our sales offices located in London, Frankfurt, Oslo and Genoa, and a network of 40 independent international representatives located throughout the world. We also are able to accept bookings in various currencies. See Note 2 of the Consolidated Financial Statements for additional information on revenues by geographic area for each of the last three financial years.

In connection with our international strategy, in July 2000 we entered into a multi-faceted strategic alliance with First Choice Holidays PLC, one of the United Kingdom s largest integrated tour operators. First Choice Holidays PLC now provides both brands with a significantly larger distribution base in the United Kingdom and access to First Choice Holidays PLC s significant retail outlets, operated under several well-known brand names, as well as use of its new distribution technology, including its unique interactive digital sales technology and online e-retail outlets. We have provided First Choice Holidays PLC with special training and promotional material geared at increasing distribution. This marketing alliance was solidified by our investment of approximately $300 million in convertible preferred stock issued by First Choice Holidays PLC. If fully converted, our holding would represent approximately a 17% interest in First Choice Holidays PLC.

Separately, we entered into a joint venture with First Choice Holidays PLC to launch a new cruise brand, Island Cruises. *Viking Serenade,* a 1,512-passenger ship which operated under the Royal Caribbean International brand until February 14, 2002, is the first ship operated by Island Cruises. As part of the transaction, *Viking Serenade* was renamed *Island Escape* and it offers Mediterranean itineraries in summer and Mexican Baja itineraries in winter.

In November 2001, we entered into a new joint venture agreement with P&O Princess to jointly create and operate a cruise line company to target customers in southern Europe. The joint venture company is owned 50% by P&O Princess and 50% by us. Each party has committed up to $500.0 million in shareholder equity, with approximately $5.0 million contributed by each party to date and the balance due and payable when called by the joint venture company. We have agreed to assign our ship-build contracts for *Serenade of the Seas* and *Jewel of the Seas* to the joint venture company, and P&O Princess has similarly agreed to assign two identified ship-build contracts to the joint venture company. Subject to the terms of the agreement, the joint venture agreement can be terminated by either party if certain commercial benchmarks have not been achieved by January 1, 2003 or April 1, 2003.

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Revenue Management

We believe we have the most advanced revenue management capabilities in the industry, which enables us to make optimal decisions about pricing, inventory and marketing actions. We are continuously working to refine these systems and tools through increased forecasting capabilities, ongoing improvements to our understanding of price/demand relationships, and greater automation of the decision process.

Technological Development

We have invested heavily in information technology to support our corporate infrastructure and guest and travel trade relations. We now have fully automated our pierside embarkation process, and have developed a corporate shoreside intranet to improve our internal productivity. Both Royal Caribbean International and Celebrity Cruises have extensive websites that are world class marketing portals with consumer booking engines, providing access to millions of Internet users throughout the world. To further enhance our customer service, we have provided on-line access so guests can book shore excursions via our websites up to ten days before sailing. We also have begun installing interactive televisions in guests staterooms, enabling them to shop for shore excursions, select a dinner wine and monitor their onboard accounts. Other innovations include royalcaribbean online and online@celebritycruises, which allow guests access to the Internet. For the trade, we have cruisingpower.com, a website dedicated to Internet communications with the travel community, which enables fast access to online tools. These online tools include *Cruise Match 2000® Online,* an internet browser-based booking system, *CruisePay,* an on-line payment service and *Cruise Writer,* which provides the capability to customize brochures and flyers. We have also launched *CruiseManager,* an independent browser-based booking tool through *CruisePath Network.*

Travel Agency Support

Almost all of the bookings for our ships are made by independent travel agencies and we are committed to supporting the travel agency community. For key accounts, we have moved from a single sales force representing both Royal Caribbean International and Celebrity Cruises to separate sales personnel dedicated to each brand to build service quality and to improve outreach to travel agents. We were the first cruise company to develop an automated booking system for the trade, *CruiseMatch®2000.* This automated reservations system allows travel agents direct access to our computer reservation system to improve ease of bookings. More than 30,000 independent travel agencies worldwide can book cruises for both brands using *CruiseMatch®2000.* Our customer service center uses state-of-the-art technology to help travel agents resolve guest service issues prior to sailing. We operate two reservation call centers, one in Miami, Florida and the other in Wichita, Kansas, thereby offering flexibility and extended hours of operations.

Sales, Marketing and Guest Services

Royal Caribbean International has a comprehensive marketing program through which it positions itself as a provider of high quality, excellent value, all-inclusive cruise vacations. Royal Caribbean International s marketing strategies focus on active adults and families who are vacation enthusiasts seeking new experiences, different places, and have a real lust for life.

Celebrity Cruises has recently initiated an integrated targeted marketing strategy. The strategy calls for building relationships with customers by delivering the brand s message to the target customer using direct, one-to-one marketing channels, and measuring results. Celebrity s target customer is the experienced cruiser who appreciates quality and value.

We offer to handle travel aspects related to guest reservations and transportation, particularly arranging guest air transportation, which is one of our important areas of operation. We have developed Custom Air service where guests can now view their flight itineraries 60 days prior to cruise departure and decide to lock-in those flights or choose others. By providing guests their air itineraries earlier, agents and guests can decide if it makes sense for them to take advantage of our Custom Air program. We maintain a comprehensive relationship with many of the major airlines ranging from fare negotiation and space handling to baggage transfer.

Operations

Cruise Ships and Itineraries

We operate 22 ships, under two brands, on a selection of worldwide itineraries ranging from two to 17 nights that call on approximately 200 destinations. The following table represents summary information concerning our ships and their areas of operation based on 2002 itineraries (subject to change):

Vessel	Year Vessel Entered Service	Berths	Primary Areas of Operation
Royal Caribbean International			
Brilliance of the Seas[1]	2002	2,100	Europe, Canada/New England, Southern Caribbean
Adventure of the Seas	2001	3,114	Southern Caribbean
Radiance of the Seas	2001	2,100	Pacific Northwest, Alaska, Southern Caribbean
Explorer of the Seas	2000	3,114	Eastern & Western Caribbean
Voyager of the Seas	1999	3,114	Western Caribbean
Vision of the Seas	1998	2,000	Panama Canal, Hawaii, Alaska, Mexican Riviera
Enchantment of the Seas	1997	1,950	Eastern & Western Caribbean
Rhapsody of the Seas	1997	2,000	Western Caribbean
Grandeur of the Seas	1996	1,950	Western Caribbean, Mexican Riviera, Panama Canal
Splendour of the Seas			

1996 1,804
Europe, South America
Legend of the Seas
1995 1,804
Alaska, Hawaii, Mexican Riviera, Australia/New Zealand
Majesty of the Seas
1992 2,354
Bahamas
Monarch of the Seas
1991 2,354
Western Caribbean
Nordic Empress
1990 1,600
Caribbean, Bermuda
Sovereign of the Seas
1988 2,276
Bahamas
Celebrity Cruises

Constellation(1)
2002 2,034
Europe, Caribbean
Summit
2001 2,034
Caribbean, Alaska, Hawaii
Infinity
2001 2,034
Alaska, Southern Caribbean, Panama Canal, Hawaii
Millennium
2000 2,034
Caribbean
Mercury
1997 1,870
Alaska, South America, Caribbean
Galaxy
$
893,771

Expenses

Operating
expenses

Room expense
$
95,161

$
69,380

$
279,589

$
176,523

Food and
beverage expense
37,780

27,061

121,450

66,458

Management and
franchise fee
expense
34,838

29,571

107,766

86,110

Other operating expense
105,646

78,120

320,325

195,000

Total property operating expenses
273,425

204,132

829,130

524,091

Depreciation and amortization
60,373

45,231

183,429

122,136

Property tax, insurance and other
34,382

23,618

104,418

60,929

General and
administrative
11,622

9,506

38,059

28,757

Transaction costs
261

32,607

2,181

36,923

Total operating
expenses
380,063

315,094

1,157,217

772,836

Operating income
66,979

26,161

204,110

120,935

Other income
856

110

2,514

323

Interest income
1,149

1,157

3,339

2,306

Interest expense
(24,629
)

(19,650
)

(78,772
)

(48,527
)
Gain (loss) on
sale of hotel
properties, net
35,895

(19
)

32,957

(49
)
(Loss) gain on
extinguishment of
indebtedness, net
(1,656
)

—

6,010

—

Gain on
settlement of
investment in
loan
—

2,670

—

2,670

Income before
equity in income
from
unconsolidated
joint ventures
78,594

10,429

170,158

77,658

Equity in income
from

unconsolidated
joint ventures
219

57

637

57

Income before
income tax
expense
78,813

10,486

170,795

77,715

Income tax
expense
(4,156
)

(6,375
)

(7,852
)

(9,362
)
Net income
74,657

4,111

162,943

68,353

Net (income) loss attributable to noncontrolling interests:

Noncontrolling interest in consolidated joint ventures
(9
)

(32
)

170

5

Noncontrolling interest in the Operating Partnership
(299
)

(43
)

(626
)

(318
)
Preferred distributions - consolidated joint venture
(374
)

(122
)

(1,109
)

(122
)
Net income
attributable to
RLJ
73,975

3,914

161,378

67,918

Preferred
dividends
(6,279
)

(2,093
)

(18,836
)

(2,093
)
Net income
attributable to
common
shareholders
$
67,696

$
1,821

$
142,542

$
65,825

Basic per
common share
data:

Net income per
share attributable
to common
shareholders
$
0.39

$
0.01

$
0.81

$
0.50

Weighted-average
number of
common shares
174,326,198

140,249,961

174,253,393

129,317,120

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Diluted per common share data:				
Net income per share attributable to common shareholders	$ 0.39	$ 0.01	$ 0.81	$ 0.50
Weighted-average number of common shares	174,479,341	140,307,269	174,365,101	129,399,177
Comprehensive income:				
Net income	$ 74,657	$ 4,111	$ 162,943	$ 68,353
Unrealized gain on interest rate derivatives	4,675	1,746	29,469	5,579
Comprehensive income	79,332	5,857	192,412	73,932
Comprehensive (income) loss attributable to noncontrolling interests:				
Noncontrolling interest in consolidated joint ventures	(9)	(32)	170	5
Noncontrolling interest in the Operating Partnership	(299)	(43)	(626)	(318)
Preferred distributions - consolidated joint venture	(374)	(122)	(1,109)	(122)
Comprehensive income attributable to RLJ	$ 78,650	$ 5,660	$ 190,847	$ 73,497

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

RLJ Lodging Trust
Consolidated Statements of Changes in Equity
(Amounts in thousands, except share data)
(unaudited)

	Shareholders' Equity							Noncontrolling Interest			
	Preferred Stock		Common Stock								
	Shares	Amount	Shares	Par Value	Additional Paid-in Capital	Distributions in excess of net earnings	Accumulated Other Comprehensive Income	Operating Partnership	Consolidated Joint Ventures	Preferred Equity in a Consolidated Joint Venture	Total Equity
lance at cember 31, 17	12,879,475	$366,936	174,869,046	$1,749	$3,208,002	$(82,566)	$8,846	$11,181	$11,700	$44,430	$3,570,27
t income ss)	—	—	—	—	—	161,378	—	626	(170)	1,109	162,943
realized n on erest rate ivatives	—	—	—	—	—	—	29,469	—	—	—	29,469
ntributions m joint nture tners	—	—	—	—	—	—	—	—	110	—	110
uance of tricted ck	—	—	591,851	6	(6)	—	—	—	—	—	—
nortization share-based npensation	—	—	—	—	10,135	—	—	—	—	—	10,135
ares quired to isfy nimum uired eral and te tax hholding vesting tricted ck	—	—	(132,370)	(2)	(2,924)	—	—	—	—	—	(2,926
rfeiture of tricted ck	—	—	(113,325)	(1)	1	—	—	—	—	—	—
stributions preferred ares	—	—	—	—	—	(18,836)	—	—	—	—	(18,836

stributions common res and ts	—	—	—	—	—	(173,817)	—	(783)	—	—	(174,600
ferred tributions - nsolidated nt venture	—	—	—	—	—	—	—	—	—	(1,109)	(1,109
lance at ptember 30, 18	12,879,475	$366,936	175,215,202	$1,752	$3,215,208	$(113,841)	$38,315	$11,024	$11,640	$44,430	$3,575,46

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

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RLJ Lodging Trust
Consolidated Statements of Changes in Equity
(Amounts in thousands, except share data)
(unaudited)

	Shareholders' Equity Preferred Stock		Common Stock					Noncontrolling Interest			
	Shares	Amount	Shares	Par Value	Additional Paid-in Capital	Retained Earnings (Distributions in excess of net earnings)	Accumulated Other Comprehensive Income (Loss)	Operating Partnership	Consolidated Joint Ventures	Preferred Equity in a Consolidated Joint Venture	Total Equity
lance at cember 31, 16	—	$—	124,364,178	$1,244	$2,187,333	$38,249	$(4,902)	$7,380	$5,973	$—	$2,235,27
t income ss)	—	—	—	—	—	67,918	—	318	(5)	122	68,353
realized n on erest rate rivatives	—	—	—	—	—	—	5,579	—	—	—	5,579
uance of mmon ares	—	—	50,358,104	504	1,015,723	—	—	—	—	—	1,016,227
uance of erating rtnership ts	—	—	—	—	—	—	—	4,342	—	—	4,342
uance of ries A mulative nvertible eferred ares	12,879,475	366,936	—	—	—	—	—	—	—	—	366,936
ncontrolling erest orded in nnection h the ergers	—	—	—	—	—	—	—	—	5,157	—	5,157
eferred uity in a nsolidated nt venture	—	—	—	—	—	—	—	—	—	44,430	44,430
uance of tricted stock	—	—	425,076	4	(4)	—	—	—	—	—	—
nortization share-based	—	—	—	—	7,964	—	—	—	—	—	7,964

mpensation											
ares quired to isfy nimum quired eral and te tax hholding on sting tricted stock	—	—	(105,378)	(2)	(2,214)	—	—	—	—	—	(2,216
ares quired as t of a share urchase gram	—	—	(122,508)	(1)	(2,609)	—	—	—	—	—	(2,610
rfeiture of tricted stock	—	—	(5,866)	—	—	—	—	—	—	—	—
stributions preferred ares	—	—	—	—	—	(2,093)	—	—	—	—	(2,093
stributions common ares and ts	—	—	—	—	—	(129,400)	—	(577)	—	—	(129,977
eferred tributions - nsolidated nt venture	—	—	—	—	—	—	—	—	—	(122)	(122
lance at tember 30, 17	12,879,475	$366,936	174,913,606	$1,749	$3,206,193	$(25,326)	$677	$11,463	$11,125	$44,430	$3,617,24

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

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RLJ Lodging Trust
Consolidated Statements of Cash Flows
(Amounts in thousands)
(unaudited)

	For the nine months ended September 30, 2018	2017
Cash flows from operating activities		
Net income	$162,943	$68,353
Adjustments to reconcile net income to cash flow provided by operating activities:		
(Gain) loss on sale of hotel properties, net	(32,957)	49
Gain on extinguishment of indebtedness, net	(6,010)	—
Gain on settlement of investment in loan	—	(2,670)
Depreciation and amortization	183,429	122,136
Amortization of deferred financing costs	2,688	2,597
Other amortization	(2,450)	(104)
Equity in income from unconsolidated joint ventures	(637)	(57)
Distributions of income from unconsolidated joint ventures	2,050	750
Accretion of interest income on investment in loan	—	(664)
Amortization of share-based compensation	9,722	7,964
Deferred income taxes	6,145	7,972
Changes in assets and liabilities:		
Hotel and other receivables, net	(18,420)	(16,493)
Prepaid expense and other assets	12,871	74
Accounts payable and other liabilities	(6,916)	28,411
Advance deposits and deferred revenue	3,801	(1,238)
Accrued interest	(2,785)	(9,751)
Net cash flow provided by operating activities	313,474	207,329
Cash flows from investing activities		
Acquisition of FelCor, net of cash acquired	—	(24,883)
Proceeds from the sale of hotel properties, net	447,737	(49)
Improvements and additions to hotel properties	(144,195)	(58,853)
Additions to property and equipment	(116)	(152)
Proceeds from the settlement of an investment in loan	—	12,792
Net cash flow provided by (used in) investing activities	303,426	(71,145)
Cash flows from financing activities		
Borrowings under Revolver	300,000	—
Repayments under Revolver	(300,000)	—
Redemption of senior notes	(539,025)	—
Payments of mortgage loans principal	(32,942)	(3,168)
Repurchase of common shares under a share repurchase program	—	(2,610)
Repurchase of common shares to satisfy employee withholding requirements	(2,925)	(2,216)
Distributions on preferred shares	(18,836)	—
Distributions on common shares	(173,367)	(150,701)
Distributions on Operating Partnership units	(766)	(667)
Payments of deferred financing costs	(3,615)	(1,050)
Preferred distributions - consolidated joint venture	(1,113)	(126)
Contributions from joint venture partners	110	—
Net cash flow used in financing activities	(772,479)	(160,538)

Net change in cash, cash equivalents, and restricted cash reserves	(155,579)	(24,354)
Cash, cash equivalents, and restricted cash reserves, beginning of year	659,076	523,878
Cash, cash equivalents, and restricted cash reserves, end of period	$503,497	$499,524

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

RLJ Lodging Trust
Notes to the Consolidated Financial Statements
(unaudited)

1. Organization

RLJ Lodging Trust (the "Company") was formed as a Maryland real estate investment trust ("REIT") on January 31, 2011. The Company is a self-advised and self-administered REIT that owns primarily premium-branded, high-margin, focused-service and compact full-service hotels. The Company elected to be taxed as a REIT, for U.S. federal income tax purposes, commencing with its taxable year ended December 31, 2011.

Substantially all of the Company's assets and liabilities are held by, and all of its operations are conducted through, RLJ Lodging Trust, L.P. (the "Operating Partnership"). The Company is the sole general partner of the Operating Partnership. As of September 30, 2018, there were 175,989,104 units of limited partnership interest in the Operating Partnership ("OP units") outstanding and the Company owned, through a combination of direct and indirect interests, 99.6% of the outstanding OP units.

As of September 30, 2018, the Company owned 152 hotel properties with approximately 29,400 rooms, located in 25 states and the District of Columbia. The Company, through wholly-owned subsidiaries, owned a 100% interest in 148 of its hotel properties, a 98.3% controlling interest in the DoubleTree Metropolitan Hotel New York City, a 95% controlling interest in The Knickerbocker, and 50% interests in entities owning two hotel properties. The Company consolidates its real estate interests in the 150 hotel properties in which it holds a controlling financial interest, and the Company records the real estate interests in the two hotels in which it holds an indirect 50% interest using the equity method of accounting. The Company leases 151 of the 152 hotel properties to its taxable REIT subsidiaries ("TRS"), of which the Company owns a controlling financial interest.

2. Summary of Significant Accounting Policies

The Company's Annual Report on Form 10-K for the year ended December 31, 2017 contains a discussion of the Company's significant accounting policies. Other than noted below, there have been no other significant changes to the Company's significant accounting policies since December 31, 2017.

Basis of Presentation and Principles of Consolidation

The unaudited consolidated financial statements and related notes have been prepared on the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America ("GAAP") and in conformity with the rules and regulations of the Securities and Exchange Commission ("SEC") applicable to financial information. The unaudited financial statements include all adjustments that are necessary, in the opinion of management, to fairly state the consolidated balance sheets, statements of operations and comprehensive income, statements of changes in equity and statements of cash flows.

The unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto as of and for the year ended December 31, 2017, included in the Company's Annual Report on Form 10-K filed with the SEC on February 28, 2018.

The consolidated financial statements include the accounts of the Company, the Operating Partnership and its wholly-owned subsidiaries, and joint ventures in which the Company has a majority voting interest and control. For the controlled subsidiaries that are not wholly-owned, the third-party ownership interest represents a noncontrolling interest, which is presented separately in the consolidated financial statements. The Company also records the real estate interests in two joint ventures in which it holds an indirect 50% interest using the equity method of accounting. All intercompany balances and transactions have been eliminated in consolidation.

Reclassifications

Certain prior year amounts in these financial statements have been reclassified to conform to the current year presentation with no impact to net income and comprehensive income, shareholders' equity or cash flows.

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Use of Estimates

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

Revenue

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") 2014-09, Revenue from Contracts with Customers, which supersedes or replaces nearly all GAAP revenue recognition guidance. The guidance establishes a new control-based revenue recognition model that changes the basis for deciding when revenue is recognized over time or at a point in time and expands the disclosures about revenue. The guidance also applies to sales of real estate and the new principles-based approach is largely based on the transfer of control of the real estate to the buyer. The Company adopted this standard on January 1, 2018 using the modified retrospective transition method. Accordingly, the Company's revenue beginning on January 1, 2018 is presented under ASC 606, while prior period revenue is reported under the accounting standards in effect for those historical periods. Based on the Company's assessment, the adoption of this standard did not have an impact to the Company's consolidated financial statements but it did result in additional disclosures in the notes to the consolidated financial statements. Refer to Note 7, Revenue, for the Company's disclosures about revenue.

Substantially all of the Company's revenues are derived from the operation of hotel properties. The Company generates room revenue by renting hotel rooms to customers at its hotel properties. The Company generates food and beverage revenue from the sale of food and beverage to customers at its hotel properties. The Company generates other revenue from parking fees, golf, pool and other resort fees, gift shop sales and other guest service fees at its hotel properties.

A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when the performance obligation is satisfied. The Company's contracts generally have a single performance obligation, such as renting a hotel room to a customer, or providing food and beverage to a customer, or providing a hotel property-related good or service to a customer. The Company's performance obligations are generally satisfied at a point in time.

The Company allocates revenue to each performance obligation based on its relative standalone selling price. The Company determines the standalone selling price based on the price it charges each customer for the use or consumption of the promised good or service.

The Company's revenue is recognized when control of the promised good or service is transferred to the customer, in an amount that reflects the consideration the Company expects to receive in exchange for the promised good or service. The revenue is recorded net of any sales and occupancy taxes collected from the customer. All rebates or discounts are recorded as a reduction to revenue, and there are no material contingent obligations with respect to rebates and discounts offered by the hotel properties.

The timing of revenue recognition, billings, and cash collections results in the Company recognizing hotel and other receivables and advance deposits and deferred revenue on the consolidated balance sheet. Hotel and other receivables are recognized when the Company has provided a good or service to the customer but is only waiting for the passage of time before the customer submits consideration to the Company. Advance deposits and deferred revenue are recognized on the consolidated balance sheets when cash payments are received in advance of the Company satisfying its performance obligation. Advance deposits and deferred revenue consist of amounts that are refundable and non-refundable to the customer. The advance deposits and deferred revenue are recognized as revenue in the consolidated statements of operations and comprehensive income when the Company satisfies its performance obligation to the customer.

For the majority of its goods or services and customers, the Company requires payment at the time the respective good or service is provided to the customer. The Company's payment terms vary by the type of customer and the goods or services offered to the customer. The Company applied a practical expedient to not disclose the value of unsatisfied performance obligations for contracts that have an original expected length of one year or less. Any contracts that have an original expected length of greater than one year are insignificant.

An allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the existing accounts receivable portfolio and increases to the allowance for doubtful accounts are recorded as bad debt expense. The allowance for doubtful accounts is calculated as a percentage of the aged accounts receivable.

Investment in Hotel Properties

The Company’s acquisitions generally consist of land, land improvements, buildings, building improvements, furniture, fixtures and equipment ("FF&E"), and inventory. The Company may also acquire intangible assets or liabilities related to in-place leases, management agreements, franchise agreements and advanced bookings. The Company allocates the purchase price among the assets acquired and the liabilities assumed based on their respective fair values at the date of acquisition. The Company determines the fair value by using market data and independent appraisals available to us and making numerous estimates and assumptions. Transaction costs are expensed for acquisitions that are considered business combinations and capitalized for asset acquisitions.

In January 2017, the FASB issued ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business. The guidance clarifies the definition of a business by adding guidance to assist companies and other reporting organizations with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. If substantially all of the fair value of the gross assets acquired (or disposed of) is concentrated in a single asset or a group of similar identifiable asset(s), then the transaction is considered to be an asset acquisition (or disposition). As a result of this standard, the Company anticipates the majority of its hotel purchases will be considered asset acquisitions as opposed to business combinations, although the determination will be made on a transaction-by-transaction basis. Transaction costs associated with asset acquisitions will be capitalized rather than expensed as incurred. The Company adopted this guidance on January 1, 2018 on a prospective basis. The Company does not believe the accounting for each future acquisition (or disposal) of assets or a business will be materially different, therefore, the adoption of this guidance is not expected to have a material impact on the Company's consolidated financial statements.

The Company’s investments in hotel properties are carried at cost and are depreciated using the straight-line method over the estimated useful lives of 15 years for land improvements, 15 years for building improvements, 40 years for buildings and three to five years for FF&E. Maintenance and repairs are expensed and major renewals or improvements to the hotel properties are capitalized. Indirect project costs, including interest, salaries and benefits, travel and other related costs that are directly attributable to the development, are also capitalized. Upon the sale or disposition of a hotel property, the asset and related accumulated depreciation accounts are removed and the related gain or loss is included in the gain or loss on sale of hotel properties in the consolidated statements of operations and comprehensive income. A sale or disposition of a hotel property that represents a strategic shift that has or will have a major effect on the Company's operations and financial results is presented as discontinued operations in the consolidated statements of operations and comprehensive income.

In accordance with the guidance on impairment or disposal of long-lived assets, the Company does not consider the "held for sale" classification on the consolidated balance sheet until it is probable that the sale will be completed within one year and the other requisite criteria for such classification have been met. The Company does not depreciate assets so long as they are classified as held for sale. Upon designation as held for sale and quarterly thereafter, the Company reviews the realizability of the carrying value, less costs to sell, in accordance with the guidance. Any such adjustment to the carrying value is recorded as an impairment loss.

The Company assesses the carrying value of its hotel properties whenever events or changes in circumstances indicate that the carrying amounts may not be recoverable. The recoverability is measured by comparing the carrying amount to the estimated future undiscounted cash flows which take into account current market conditions and the Company’s intent with respect to holding or disposing of the hotel properties. If the Company's analysis indicates that the carrying value is not recoverable on an undiscounted cash flow basis, the Company will recognize an impairment loss for the amount by which the carrying value exceeds the fair value. The fair value is determined through various valuation techniques, including internally developed discounted cash flow models, comparable market transactions or third-party appraisals.

Sale of Real Estate

ASU 2014-09 also applies to the sale of real estate and the new principles-based approach is largely based on the transfer of control of the real estate to the buyer. In February 2017, the FASB issued ASU 2017-05, Other Income - Gains and Losses from the Derecognition of Nonfinancial Assets (Subtopic 610-20): Clarifying the Scope of Asset Derecognition Guidance and Accounting for Partial Sales of Nonfinancial Assets. This guidance clarifies that ASC 610-20 applies to the derecognition of nonfinancial assets, including real estate, and in substance nonfinancial assets, which are defined as assets or a group of assets for which substantially all of the fair value consists of nonfinancial assets and the group or subsidiary is not a business. As a result of this guidance, sales and partial sales of real estate assets will be accounted for similar to all other sales of nonfinancial and in substance nonfinancial assets. The Company adopted this guidance on January 1, 2018 using the modified retrospective transition method. Based on the Company's assessment, the adoption of this guidance did not have an impact on the Company's consolidated financial statements.

Recently Issued Accounting Pronouncements

In February 2016, the FASB issued ASU 2016-02, Leases (Topic 842). The guidance will require lessees to recognize a right-of-use asset and a lease liability for most of their leases on the balance sheet, and an entity will need to classify its leases as either an operating or finance lease in order to determine the income statement presentation. Leases with a term of 12 months or less will be accounted for similar to the existing guidance today for operating leases. Lessors will classify their leases using an approach that is substantially equivalent to the existing guidance today for operating, direct financing, or sales-type leases. Lessors may only capitalize the incremental direct costs of leasing, so any indirect costs of leasing will be expensed as incurred. The guidance requires an entity to separate the lease components from the non-lease components in a contract, with the lease components being accounted for in accordance with ASC 842 and the non-lease components being accounted for in accordance with other applicable accounting guidance. The guidance is effective for annual reporting periods beginning after December 15, 2018, and the interim periods within those annual periods, with early adoption permitted. The Company will adopt this new standard on January 1, 2019. The Company has not yet completed its analysis on this standard, but it believes the application of the new standard will result in the recording of a right-of-use asset and a lease liability on the consolidated balance sheet for each of its ground leases, parking leases, and equipment leases, which represent the majority of the Company's current operating lease payments. The Company does not expect the adoption of this standard will materially affect its consolidated statements of operations and comprehensive income.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities. The guidance amends the hedge accounting recognition and presentation requirements in ASC 815. The guidance is meant to simplify the application of hedge accounting and better align the financial reporting for hedging activities with the entity's economic and risk management activities. Under the new guidance, all changes in the fair value of highly effective cash flow hedges will be recorded in other comprehensive income and they will be reclassified to earnings when the hedged item impacts earnings. The guidance is effective for annual reporting periods beginning after December 15, 2018, and the interim periods within those annual periods, with early adoption permitted. The Company will adopt this new standard on January 1, 2019. Based on the Company's assessment, the adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

In August 2018, the SEC issued SEC Final Rule 33-10532, Disclosure Update and Simplification. The amendments simplify or eliminate duplicative, overlapping, or outdated disclosure requirements. The amendments also add certain disclosure requirements, such as requiring entities to disclose the current and comparative quarter and year-to-date changes in shareholders' equity for interim periods. The amended rules are effective for reports filed on or after November 5, 2018. However, the SEC issued Compliance & Disclosure Interpretation 105.09 that allows entities to defer the adoption of the new disclosure requirement relating to changes in shareholders' equity for interim periods until the Form 10-Q for the quarterly period that begins after November 5, 2018. The Company will adopt the new disclosure requirement relating to changes in shareholders' equity for interim periods on January 1, 2019. Based on the Company's assessment, the adoption of the new disclosures will not have a material impact on the Company's consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, Fair Value Measurement (Topic 820): Disclosure Framework - Changes to the Disclosure Requirements for Fair Value Measurement. The guidance modifies the disclosure requirements for fair value measurements by removing or modifying some of the disclosures, while also adding new disclosures. The guidance is effective for annual reporting periods beginning after December 15, 2019, and the interim periods within those annual periods, with early adoption permitted. The Company will adopt this new standard on January 1, 2020. Based on the Company's assessment, the adoption of this standard is not expected to have a material impact on the Company's consolidated financial statements.

3. Merger with FelCor Lodging Trust Incorporated

On August 31, 2017 (the "Acquisition Date"), the Company, the Operating Partnership, Rangers Sub I, LLC, a wholly owned subsidiary of the Operating Partnership ("Rangers"), and Rangers Sub II, LP, a wholly owned subsidiary of the Operating Partnership ("Partnership Merger Sub"), consummated the transactions contemplated by the Agreement and Plan of Merger (the "Merger Agreement"), dated as of April 23, 2017, with FelCor Lodging Trust Incorporated ("FelCor") and FelCor Lodging Limited Partnership ("FelCor LP") pursuant to which Partnership Merger Sub merged with and into FelCor LP, with FelCor LP surviving as a wholly owned subsidiary of the Operating Partnership (the "Partnership Merger"), and, immediately thereafter, FelCor merged with and into Rangers, with Rangers surviving as a wholly owned subsidiary of the Operating Partnership (the "REIT Merger" and, together with the Partnership Merger, the "Mergers").

Upon completion of the REIT Merger and under the terms of the Merger Agreement, each issued and outstanding share of common stock, par value $0.01 per share, of FelCor (other than shares held by any wholly owned subsidiary of FelCor or by the Company or any of its subsidiaries) was converted into the right to receive 0.362 (the "Common Exchange Ratio") common shares of beneficial interest, par value $0.01 per share, of the Company (the "Common Shares"), and each issued and outstanding share of $1.95 Series A cumulative convertible preferred stock, par value $0.01 per share, of FelCor was converted into the right to receive one $1.95 Series A Cumulative Convertible Preferred Share, par value $0.01 per share, of the Company (a "Series A Preferred Share").

Upon completion of the Partnership Merger and under the terms of the Merger Agreement, each limited partner of FelCor LP was entitled to elect to exchange its outstanding common limited partnership units in FelCor LP (the "FelCor LP Common Units") for a number of newly issued Common Shares based on the Common Exchange Ratio. Upon completion of the Partnership Merger, each outstanding FelCor LP Common Unit of any holder who did not make the foregoing election was converted into the right to receive a number of common limited partnership units in the Operating Partnership (the "OP Units") based on the Common Exchange Ratio. No fractional shares of units of Common Shares or OP Units were issued in the Mergers, and the value of any fractional interests was paid in cash.

The Company accounted for the Mergers under the acquisition method of accounting in ASC 805, Business Combinations. As a result of the Mergers, the Company acquired an ownership interest in the following 37 hotel properties:

Hotel Property Name	Location	Ownership Interest	Management Company	Rooms
DoubleTree Suites by Hilton Austin	Austin, TX	100%	Hilton	188
DoubleTree Suites by Hilton Orlando - Lake Buena Vista	Orlando, FL	100%	Hilton	229
Embassy Suites Atlanta - Buckhead	Atlanta, GA	100%	Hilton	316
Embassy Suites Birmingham	Birmingham, AL	100%	Hilton	242
Embassy Suites Boston Marlborough (1)	Marlborough, MA	100%	Hilton	229
Embassy Suites Dallas - Love Field	Dallas, TX	100%	Aimbridge Hospitality	248
Embassy Suites Deerfield Beach - Resort & Spa	Deerfield Beach, FL	100%	Hilton	244
Embassy Suites Fort Lauderdale 17th Street	Fort Lauderdale, FL	100%	Hilton	361
Embassy Suites Los Angeles - International Airport South	El Segundo, CA	100%	Hilton	349
Embassy Suites Mandalay Beach - Hotel & Resort	Oxnard, CA	100%	Hilton	250
Embassy Suites Miami - International Airport	Miami, FL	100%	Hilton	318
Embassy Suites Milpitas Silicon Valley	Milpitas, CA	100%	Hilton	266
Embassy Suites Minneapolis - Airport	Bloomington, MN	100%	Hilton	310
Embassy Suites Myrtle Beach - Oceanfront Resort	Myrtle Beach, SC	100%	Hilton	255
Embassy Suites Napa Valley (2)	Napa, CA	100%	Hilton	205
Embassy Suites Orlando - International Drive South/Convention Center	Orlando, FL	100%	Hilton	244
Embassy Suites Phoenix - Biltmore	Phoenix, AZ	100%	Hilton	232
Embassy Suites San Francisco Airport - South San Francisco	San Francisco, CA	100%	Hilton	312
Embassy Suites San Francisco Airport - Waterfront	Burlingame, CA	100%	Hilton	340
Embassy Suites Secaucus - Meadowlands (3)	Secaucus, NJ	50%	Hilton	261
Hilton Myrtle Beach Resort	Myrtle Beach, SC	100%	Hilton	385
Holiday Inn San Francisco - Fisherman's Wharf (4)	San Francisco, CA	100%	InterContinental Hotels	585
San Francisco Marriott Union Square	San Francisco, CA	100%	Marriott	400
Sheraton Burlington Hotel & Conference Center (5) (6)	Burlington, VT	100%	Marriott	309
Sheraton Philadelphia Society Hill Hotel (7)	Philadelphia, PA	100%	Marriott	364
The Fairmont Copley Plaza (8)	Boston, MA	100%	FRHI Hotels & Resorts	383
The Knickerbocker New York	New York, NY	95%	Highgate Hotels	330
The Mills House Wyndham Grand Hotel	Charleston, SC	100%	Wyndham	216
The Vinoy Renaissance St. Petersburg Resort & Golf Club (9)	St. Petersburg, FL	100%	Marriott	361
Wyndham Boston Beacon Hill	Boston, MA	100%	Wyndham	304

Wyndham Houston - Medical Center Hotel & Suites	Houston, TX	100%	Wyndham	287
Wyndham New Orleans - French Quarter	New Orleans, LA	100%	Wyndham	374
Wyndham Philadelphia Historic District	Philadelphia, PA	100%	Wyndham	364
Wyndham Pittsburgh University Center	Pittsburgh, PA	100%	Wyndham	251
Wyndham San Diego Bayside	San Diego, CA	100%	Wyndham	600
Wyndham Santa Monica At The Pier	Santa Monica, CA	100%	Wyndham	132
Chateau LeMoyne - French Quarter, New Orleans (10)	New Orleans, LA	50%	InterContinental Hotels	171
				11,215

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(1) In February 2018, the Company sold this hotel property for a sale price of $23.7 million.

(2) In July 2018, the Company sold this hotel property for a sale price of $102.0 million.

(3) The Company owns an indirect 50% ownership interest in the real estate at this hotel property and records the real estate interests using the equity method of accounting. The Company leases the hotel property to its TRS, of which the Company owns a controlling financial interest in the operating lessee, so the Company consolidates its ownership interest in the leased hotel.

(4) In October 2018, the Company sold this hotel property for a sale price of $75.3 million.

(5) In December 2017, this hotel property was converted to the DoubleTree by Hilton Burlington Vermont.

(6) In September 2018, the Company sold this hotel property for a sale price of $35.0 million.

(7) In March 2018, the Company sold this hotel property for a sale price of $95.5 million.

(8) In December 2017, the Company sold this hotel property for a sale price of $170.0 million.

(9) In August 2018, the Company sold this hotel property for a sale price of $185.0 million.

(10) The Company owns an indirect 50% ownership interest in this hotel property and accounts for its ownership interest using the equity method of accounting. This hotel property is operated without a lease.

The total consideration for the Mergers was approximately $1.4 billion, which included the Company's issuance of approximately 50.4 million common shares at $20.18 per share to former FelCor common stockholders, the Company's issuance of approximately 12.9 million Series A Preferred Shares at $28.49 per share to former FelCor preferred stockholders, the Operating Partnership's issuance of approximately 0.2 million OP Units at $20.18 per unit to former FelCor LP limited partners, and cash. The total consideration consisted of the following (in thousands):

	Total Consideration
Common Shares	$ 1,016,227
Series A Preferred Shares	366,936
OP Units	4,342
Cash, net of cash, cash equivalents, and restricted cash reserves acquired	24,883
Total consideration	$ 1,412,388

The Company allocated the purchase price consideration as follows (in thousands):

	August 31, 2017
Investment in hotel properties	$2,661,114
Investment in unconsolidated joint ventures	25,651
Hotel and other receivables	28,308
Deferred income tax assets	58,170
Intangible assets	139,673
Prepaid expenses and other assets	23,811
Debt	(1,305,337)
Accounts payable and other liabilities	(118,360)
Advance deposits and deferred revenue	(23,795)
Accrued interest	(22,612)
Distributions payable	(4,312)
Noncontrolling interest in consolidated joint ventures	(5,493)
Preferred equity in a consolidated joint venture	(44,430)
Total consideration	$1,412,388

The Company used the following valuation methodologies, inputs, and assumptions to estimate the fair value of the assets acquired, the liabilities assumed, and the equity interests acquired:

- Investment in hotel properties — The Company estimated the fair values of the land and improvements, buildings and improvements, and furniture, fixtures, and equipment at the hotel properties by using a combination of the market, cost, and income approaches. These valuation methodologies are based on significant Level 3 inputs in the fair value hierarchy, such as estimates of future income growth, capitalization rates, discount rates, capital expenditures, and cash flow projections at the respective hotel properties.

- Investment in unconsolidated joint ventures — The Company estimated the fair value of its real estate interests in the unconsolidated joint ventures by using the same valuation methodologies for the investment in hotel properties noted above and for the debt noted below. The Company recognized the net assets acquired based on its respective ownership interest in the joint venture according to the joint venture agreement.

Deferred income tax assets — The Company estimated the future realizable value of the deferred income tax assets by estimating the amount of the net operating loss that will be utilized in future periods by the acquired taxable REIT subsidiaries. The Company then applied its applicable effective tax rate against the net operating losses to determine the appropriate deferred income tax assets to recognize. This valuation methodology is based on Level 3 inputs in the fair value hierarchy.

Intangible assets — The Company estimated the fair value of its below market ground lease intangible assets by calculating the present value of the difference between the contractual rental amounts paid according to the in-place lease agreements and the market rental rates for similar leased space, measured over a period equal to the remaining non-cancelable term of the lease. This valuation methodology is based on Level 3 inputs in the fair value hierarchy. The below market ground lease intangible assets are amortized over the remaining terms of the respective leases as adjustments to rental expense in property tax, insurance and other in the consolidated statements of operations and comprehensive income. The Company estimated the fair value of the advanced bookings intangible asset by using the income approach to determine the projected cash flows that a hotel property will receive as a result of future hotel room and guests events that have already been reserved and pre-booked at the hotel property as of the Acquisition Date. This valuation methodology is based on Level 3 inputs in the fair value hierarchy. The advanced bookings intangible asset is amortized over the duration of the hotel room and guest event reservations period at the hotel property to depreciation and amortization in the consolidated statements of operations and comprehensive income. The Company recognized the following intangible assets in the Mergers (dollars in thousands):

		Weighted Average Amortization Period (in Years)
Below market ground leases	$118,050	54
Advanced bookings	13,862	1
Other intangible assets	7,761	6
Total intangible assets	$139,673	46

Above market ground lease liabilities — The Company estimated the fair value of its above market ground lease liabilities by calculating the present value of the difference between the contractual rental amounts paid according to the in-place lease agreements and the market rental rates for similar leased space, measured over a period equal to the remaining non-cancelable term of the lease. This valuation methodology is based on Level 3 inputs in the fair value hierarchy. The Company recognized approximately $15.5 million of above market ground lease liabilities in the Mergers, which are included in accounts payable and other liabilities in the accompanying consolidated balance sheet. The above market ground lease liabilities are amortized over the remaining terms of the respective leases as adjustments to rental expense in property tax, insurance and other in the consolidated statements of operations and comprehensive income.

Debt — The Company estimated the fair value of the Senior Notes (as defined in Note 8) by using publicly available trading prices, market interest rates, and spreads for the Senior Notes, which are Level 3 inputs in the fair value hierarchy. The Company estimated the fair value of the mortgage loans using a discounted cash flow model and incorporated various inputs and assumptions for the effective borrowing rates for debt with similar terms and the loan to estimated fair value of the collateral, which are Level 3 inputs in the fair value hierarchy. The Company recognized approximately $71.7 million in above market debt fair value adjustments on the Senior Notes and the mortgage loans assumed in the Mergers, which is included in debt, net in the accompanying consolidated balance sheet. The above market debt fair value adjustments are amortized over the remaining terms of the respective debt instruments as adjustments to interest expense in the consolidated statements of operations and comprehensive income.

Noncontrolling interest in consolidated joint ventures — The Company estimated the fair value of the consolidated joint ventures by using the same valuation methodologies for the investment in hotel properties noted above. The Company then recognized the fair value of the noncontrolling interest in the consolidated joint ventures based on the joint venture partner's ownership interest in the consolidated joint venture. This valuation methodology is based on Level 3 inputs and assumptions in the fair value hierarchy.

- Preferred equity in a consolidated joint venture — The Company estimated the fair value of the preferred equity in a consolidated joint venture by comparing the contractual terms of the preferred equity agreement to market-based terms of a similar preferred equity agreement, which is based on Level 3 inputs in the fair value hierarchy.

- Hotel and other receivables, prepaid expenses and other assets, accounts payable and other liabilities, advance deposits and deferred revenue, accrued interest, and distributions payable — The carrying amounts of the assets acquired, the liabilities assumed, and the equity interests acquired approximate fair value because of their short term maturities.

For the hotel properties acquired during the nine months ended September 30, 2017, the total revenues and net income from the date of acquisition through September 30, 2017 are included in the accompanying consolidated statements of operations as follows (in thousands):

	For the one month ended September 30, 2017
Revenue	$ 66,457
Net income	$ 6,768

The following table presents the costs that were incurred in connection with the Mergers (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Transaction costs	$86	$30,270	$(527)	$34,517
Integration costs	156	2,193	1,881	2,193
	$242	$32,463	$1,354	$36,710

The transaction costs primarily related to transfer taxes, including any refund of transfer taxes, and financial advisory, legal, and other professional service fees in connection with the Mergers. The integration costs primarily related to professional fees and employee-related costs, including compensation for transition employees. The merger-related costs noted above were expensed to transaction costs in the accompanying consolidated statements of operations and comprehensive income.

The following unaudited condensed pro forma financial information presents the results of operations as if the Mergers had taken place on January 1, 2016. The unaudited condensed pro forma financial information is not necessarily indicative of what the actual results of operations of the Company would have been assuming the Mergers had taken place on January 1, 2016, nor is it indicative of the results of operations for future periods. The unaudited condensed pro forma financial information is as follows (in thousands):

	For the three months ended September 30, 2017	For the nine months ended September 30, 2017
	(unaudited)	
Revenue	$482,839	$ 1,431,409

Net income attributable to common shareholders	$35,275	$104,528
Net income per share attributable to common shareholders - basic	$0.20	$0.60
Net income per share attributable to common shareholders - diluted	$0.20	$0.60
Weighted-average number of shares outstanding - basic	174,186,944	174,141,367
Weighted-average number of shares outstanding - diluted	174,244,252	174,223,424

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4. Investment in Hotel Properties

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

	September 30, 2018	December 31, 2017
Land and improvements	$ 1,208,365	$ 1,275,030
Buildings and improvements	4,660,962	4,890,266
Furniture, fixtures and equipment	785,418	756,546
	6,654,745	6,921,842
Accumulated depreciation	(1,281,574)	(1,129,917)
Investment in hotel properties, net	$ 5,373,171	$ 5,791,925

For the three and nine months ended September 30, 2018, the Company recognized depreciation expense related to its investment in hotel properties of approximately $58.5 million and $176.4 million, respectively. For the three and nine months ended September 30, 2017, the Company recognized depreciation expense related to its investment in hotel properties of approximately $44.1 million and $120.8 million, respectively.

Held for Sale

In July 2018, the Company entered into a purchase and sale agreement to sell the Holiday Inn San Francisco - Fisherman's Wharf. At September 30, 2018, this hotel property has been included in assets of hotel properties held for sale, net in the accompanying consolidated balance sheet. The transaction closed on October 15, 2018.

The following table is a summary of the major classes of assets held for sale (in thousands):

	September 30, 2018
Land and improvements	$ 12,203
Buildings and improvements	10,900
Furniture, fixtures and equipment	2,074
Total investment in hotel properties, net	25,177
Intangible assets	272
Total assets of hotel properties held for sale, net	$ 25,449

5. Investment in Unconsolidated Joint Ventures

As of September 30, 2018 and December 31, 2017, the Company owned 50% interests in joint ventures that owned two hotel properties. The Company also owned 50% interests in joint ventures that owned real estate and a condominium management business that are associated with two of our resort hotel properties. The Company accounts for the investments in these unconsolidated joint ventures under the equity method of accounting. The Company makes adjustments to the equity in income (loss) from unconsolidated joint ventures related to the difference between the Company's basis in the investment in the unconsolidated joint ventures as compared to the historical basis of the assets and liabilities of the joint ventures. As of September 30, 2018 and December 31, 2017, the unconsolidated joint ventures' debt consisted entirely of non-recourse mortgage debt.

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The following table summarizes the components of the Company's investments in unconsolidated joint ventures (in thousands):

	September 30, 2018	December 31, 2017
Equity basis of the joint venture investments	$ (58)	$ 253
Cost of the joint venture investments in excess of the joint venture book value	22,530	23,632
Investment in unconsolidated joint ventures	$ 22,472	$ 23,885

The following table summarizes the components of the Company's equity in income from unconsolidated joint ventures (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Unconsolidated joint ventures net income attributable to the Company	$587	$150	$1,739	$150
Depreciation of cost in excess of book value	(368)	(93)	(1,102)	(93)
Equity in income from unconsolidated joint ventures	$219	$57	$637	$57

6. Sale of Hotel Properties

During the nine months ended September 30, 2018, the Company sold six hotel properties for a total sale price of approximately $454.1 million. In connection with these transactions, the Company recorded an aggregate $30.9 million net gain on sales, which is included in gain (loss) on sale of hotel properties, net in the accompanying consolidated statement of operations and comprehensive income. The gain on sale includes a gain on extinguishment of indebtedness of $5.1 million associated with two of the hotel properties that were sold.

The following table discloses the hotel properties that were sold during the nine months ended September 30, 2018:

Hotel Property Name	Location	Sale Date	Rooms
Embassy Suites Boston Marlborough	Marlborough, MA	February 21, 2018	229
Sheraton Philadelphia Society Hill Hotel	Philadelphia, PA	March 27, 2018	364
Embassy Suites Napa Valley	Napa, CA	July 13, 2018	205
DoubleTree Hotel Columbia	Columbia, MD	August 7, 2018	152
The Vinoy Renaissance St. Petersburg Resort & Golf Club	St. Petersburg, FL	August 28, 2018	362
DoubleTree by Hilton Burlington Vermont	Burlington, VT	September 27, 2018	309
		Total	1,621

During the nine months ended September 30, 2018, the Company also sold a parcel of land for a sale price of $1.5 million. In connection with this transaction, the Company recorded a $1.4 million gain on sale, which is included in gain on sale of hotel properties, net in the accompanying consolidated statement of operations and comprehensive income.

During the year ended December 31, 2016, the Company sold two hotel properties and deferred a gain of $15.0 million related to the Company's maximum exposure to loss with respect to certain post-closing obligations. During the nine months ended September 30, 2018, the Company satisfied certain post-closing obligations and recognized an additional $0.7 million gain on sale, which is included in gain on sale of hotel properties, net in the accompanying consolidated statement of operations and comprehensive income. The Company has satisfied all post-closing obligations with respect to the sale of the two hotel properties.

On October 15, 2018, the Company sold the Holiday Inn San Francisco - Fisherman's Wharf for $75.3 million. In connection with the sale, the Company transferred its purchase option on the land underlying the ground lease to the buyer. The proceeds to the Company as a result of the sale was approximately $30.4 million.

During the nine months ended September 30, 2017, the Company did not sell any hotel properties.

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7. Revenue

The Company recognized revenue from the following geographic markets (in thousands):

	For the three months ended September 30, 2018				For the three months ended September 30, 2017			
	Room Revenue	Food and Beverage Revenue	Other Revenue	Total Revenue	Room Revenue	Food and Beverage Revenue	Other Revenue	Total Revenue
Northern California	$67,161	$ 4,705	$ 2,238	$74,104	$39,998	$ 2,808	$ 1,064	$43,870
Southern California	36,820	4,189	2,612	43,621	21,268	2,293	1,130	24,691
New York City	34,935	4,093	1,164	40,192	26,987	2,158	800	29,945
South Florida	24,678	4,426	1,773	30,877	18,186	2,966	992	22,144
Chicago	21,935	3,457	577	25,969	20,553	3,648	473	24,674
Denver	21,503	3,186	372	25,061	22,432	3,330	428	26,190
Austin	17,399	2,058	865	20,322	17,356	2,103	688	20,147
Houston	14,041	853	1,150	16,044	13,549	617	741	14,907
Washington, DC	15,570	487	614	16,671	16,511	814	675	18,000
Louisville	8,233	3,361	468	12,062	9,935	2,215	566	12,716
Other	114,962	16,396	10,761	142,119	85,271	12,628	6,072	103,971
Total	$377,237	$ 47,211	$ 22,594	$447,042	$292,046	$ 35,580	$ 13,629	$341,255

	For the nine months ended September 30, 2018				For the nine months ended September 30, 2017			
	Room Revenue	Food and Beverage Revenue	Other Revenue	Total Revenue	Room Revenue	Food and Beverage Revenue	Other Revenue	Total Revenue
Northern California	$184,087	$15,586	$ 6,120	$205,793	$86,288	$ 5,126	$ 2,168	$93,582
South Florida	102,940	15,413	5,470	123,823	64,933	9,871	3,297	78,101
Southern California	100,838	12,545	6,688	120,071	48,326	4,654	2,039	55,019
New York City	93,612	11,722	3,106	108,440	62,678	4,353	1,995	69,026
Austin	63,968	7,035	2,696	73,699	59,469	6,723	1,941	68,133
Chicago	56,451	9,895	1,470	67,816	53,451	10,343	1,282	65,076
Denver	55,292	9,423	976	65,691	57,038	9,745	1,109	67,892
Washington, DC	51,577	2,047	1,785	55,409	52,664	2,410	1,831	56,905
Houston	47,469	2,803	3,199	53,471	41,339	2,080	2,197	45,616
Louisville	28,830	10,461	1,525	40,816	33,303	9,977	1,856	45,136
Other	353,051	60,920	32,327	446,298	211,262	26,110	11,913	249,285
Total	$1,138,115	$157,850	$65,362	$1,361,327	$770,751	$ 91,392	$ 31,628	$893,771

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8. Debt

The Company's debt consisted of the following (in thousands):

	September 30, 2018	December 31, 2017
Senior Notes	$506,503	$ 1,062,716
Revolver and Term Loans, net	1,168,736	1,170,954
Mortgage loans, net	614,925	646,818
Debt, net	$2,290,164	$ 2,880,488

Senior Notes

The Company's senior secured notes and the senior unsecured notes are collectively the "Senior Notes". The Company's Senior Notes consisted of the following (in thousands):

	Number of Assets Encumbered	Interest Rate	Maturity Date	Outstanding Borrowings at September 30, 2018	Outstanding Borrowings at December 31, 2017
Senior secured notes (1) (2) (3)	9	5.63%	—	$—	$ 552,669
Senior unsecured notes (1) (2) (4)	—	6.00%	June 2025	506,503	510,047
Total Senior Notes				$506,503	$ 1,062,716

(1) Requires payments of interest only through maturity.

(2) The senior secured notes include $28.7 million at December 31, 2017, and the senior unsecured notes include $31.5 million and $35.1 million at September 30, 2018 and December 31, 2017, respectively, related to fair value adjustments on the Senior Notes that were assumed in the Mergers.

(3) On March 9, 2018 (the "Redemption Date"), the Company completed the early redemption of the senior secured notes in full for an aggregate amount of approximately $539.0 million, which included the redemption price of 102.813% for the outstanding principal amount. The Company recognized a gain of approximately $7.7 million on the early redemption, which is included in gain (loss) on extinguishment of indebtedness, net in the accompanying consolidated statements of operations and comprehensive income. The gain on extinguishment of indebtedness excludes $5.1 million related to two hotel properties that were sold during the nine months ended September 30, 2018 that is included in gain (loss) on sale of hotel properties, net in the accompanying consolidated statement of operations and comprehensive income.

(4) The Company has the option to redeem the senior unsecured notes beginning June 1, 2020 at a premium of 103.0%.

The Senior Notes are subject to customary financial covenants. As of September 30, 2018 and December 31, 2017, the Company was in compliance with all financial covenants.

Revolver and Term Loans

The Company has the following unsecured credit agreements in place:

- $600.0 million revolving credit facility with a scheduled maturity date of April 22, 2020 with a one-year extension option if certain conditions are satisfied (the "Revolver");
- $400.0 million term loan with a scheduled maturity date of April 22, 2021 (the "$400 Million Term Loan Maturing 2021");

- $150.0 million term loan with a scheduled maturity date of January 22, 2022 (the "$150 Million Term Loan Maturing 2022");
- $400.0 million term loan with a scheduled maturity date of January 25, 2023 (the "$400 Million Term Loan Maturing 2023"). This term loan was referred to as the $400 Million Term Loan Maturing 2019 in previous periodic filings; and
- $225.0 million term loan with a scheduled maturity date of January 25, 2023 (the "$225 Million Term Loan Maturing 2023"). This term loan was referred to as the $225 Million Term Loan Maturing 2019 in previous periodic filings.

The $400 Million Term Loan Maturing 2021, the $150 Million Term Loan Maturing 2022, the $400 Million Term Loan Maturing 2023, and the $225 Million Term Loan Maturing 2023 are collectively the "Term Loans". The Revolver and Term

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Loans are subject to customary financial covenants. As of September 30, 2018 and December 31, 2017, the Company was in compliance with all financial covenants.

The Company's unsecured credit agreements consisted of the following (in thousands):

	Interest Rate at September 30, 2018 (1)	Maturity Date	Outstanding Borrowings at September 30, 2018	December 31, 2017
Revolver (2)	3.76%	April 2020	$—	$—
$400 Million Term Loan Maturing 2021	3.08%	April 2021	400,000	400,000
$150 Million Term Loan Maturing 2022	3.08%	January 2022	150,000	150,000
$400 Million Term Loan Maturing 2023	3.19%	January 2023	400,000	400,000
$225 Million Term Loan Maturing 2023	3.44%	January 2023	225,000	225,000
			1,175,000	1,175,000
Deferred financing costs, net (3)			(6,264)	(4,046)
Total Revolver and Term Loans, net			$1,168,736	$1,170,954

(1) Interest rate at September 30, 2018 gives effect to interest rate hedges.

(2) At both September 30, 2018 and December 31, 2017, there was $600.0 million of borrowing capacity on the Revolver. The Company has the ability to further increase the borrowing capacity to $750.0 million, subject to certain lender requirements.

(3) Excludes $1.7 million and $2.6 million as of September 30, 2018 and December 31, 2017, respectively, related to deferred financing costs on the Revolver, which are included in prepaid expense and other assets in the accompanying consolidated balance sheets.

Mortgage Loans

The Company's mortgage loans consisted of the following (in thousands):

Lender	Number of Assets Encumbered	Interest Rate at September 30, 2018 (1)	Maturity Date		Principal balance at September 30, 2018	December 31, 2017
Wells Fargo (5)	4	4.05%	March 2019	(3)	$141,000	$ 143,250
Wells Fargo (2)	4	4.08%	October 2019	(4)	150,000	150,000
PNC Bank (2) (6)	5	4.36%	March 2021	(7)	85,000	85,000
Wells Fargo (8)	1	5.25%	June 2022		32,269	32,882
PNC Bank/Wells Fargo (9)	3	4.95%	October 2022		92,322	120,893
Prudential (10)	1	4.94%	October 2022		29,758	30,323
Scotiabank (2) (11)	1	LIBOR + 3.00%	November 2018	(12)	85,073	85,404
	19				615,422	647,752
Deferred financing costs, net					(497)	(934)
Total mortgage loans, net					$614,925	$ 646,818

(1) Interest rate at September 30, 2018 gives effect to interest rate hedges.

(2) Requires payments of interest only through maturity.

(3) In March 2018, the Company extended the maturity date for a one-year term. The maturity date may be extended for three additional one-year terms at the Company’s option, subject to certain lender requirements.

(4) In October 2018, the Company extended the maturity date for a one-year term. The maturity date may be extended for two additional one-year terms at the Company's option, subject to certain lender requirements.

(5) Two of the four hotels encumbered by the Wells Fargo loan are cross-collateralized.

(6) The five hotels encumbered by the PNC Bank loan are cross-collateralized.

(7) The maturity date may be extended for two one-year terms at the Company’s option, subject to certain lender requirements.

(8) Includes \$0.7 million and \$0.8 million at September 30, 2018 and December 31, 2017, respectively, related to a fair value adjustment on the mortgage loan that was assumed in conjunction with an acquisition.

(9) Includes \$2.0 million and \$3.0 million at September 30, 2018 and December 31, 2017, respectively, related to fair value adjustments on the mortgage loans that were assumed in the Mergers.

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(10) Includes $0.6 million and $0.7 million at September 30, 2018 and December 31, 2017, respectively, related to a fair value adjustment on the mortgage loan that was assumed in the Mergers.

(11) Includes $0.1 million and $0.4 million at September 30, 2018 and December 31, 2017, respectively, related to a fair value adjustment on the mortgage loan that was assumed in the Mergers.

(12) On November 5, 2018, the Company paid off the Scotiabank mortgage loan in full.

Certain mortgage agreements are subject to customary financial covenants. The Company was in compliance with all financial covenants at September 30, 2018 and December 31, 2017.

Interest Expense

The components of the Company's interest expense consisted of the following (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Senior Notes	$5,954	$3,980	$22,485	$3,980
Revolver and Term Loans	11,042	9,834	33,428	28,981
Mortgage loans	6,753	4,943	20,171	12,969
Amortization of deferred financing costs	880	893	2,688	2,597
Total interest expense	$24,629	$19,650	$78,772	$48,527

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9. Derivatives and Hedging

The Company's interest rate swaps consisted of the following (in thousands):

			Notional value at		Fair value at	
Hedge type	Interest rate	Maturity	September 30, 2018	December 31, 2017	September 30, 2018	December 31, 2017
Swap-cash flow	1.56%	March 2018	$—	$ 175,000	$—	$ (38)
Swap-cash flow	1.64%	March 2018	—	175,000	—	(71)
Swap-cash flow	1.83%	September 2018	—	15,758	—	(23)
Swap-cash flow	1.75%	September 2018	—	15,758	—	(14)
Swap-cash flow	1.83%	September 2018	—	38,678	—	(57)
Swap-cash flow	1.75%	September 2018	—	39,632	—	(35)
Swap-cash flow	1.83%	September 2018	—	17,190	—	(25)
Swap-cash flow	1.75%	September 2018	—	16,235	—	(14)
Swap-cash flow	2.02%	March 2019	125,000	125,000	212	(383)
Swap-cash flow	1.94%	March 2019	100,000	100,000	207	(213)
Swap-cash flow	1.27%	March 2019	125,000	125,000	750	836
Swap-cash flow	1.96%	March 2019	100,000	100,000	224	(230)
Swap-cash flow	1.85%	March 2019	50,000	50,000	142	(43)
Swap-cash flow	1.81%	March 2019	50,000	50,000	153	(19)
Swap-cash flow	1.74%	March 2019	25,000	25,000	86	13
Swap-cash flow	1.80%	September 2020	33,000	33,000	589	202
Swap-cash flow	1.80%	September 2020	82,000	82,000	1,463	502
Swap-cash flow	1.80%	September 2020	35,000	35,000	624	214
Swap-cash flow	1.81%	October 2020	143,000	143,000	2,958	803
Swap-cash flow	1.15%	April 2021	100,000	100,000	4,346	2,880
Swap-cash flow	1.20%	April 2021	100,000	100,000	4,217	2,726
Swap-cash flow	2.15%	April 2021	75,000	75,000	1,323	(144)
Swap-cash flow	1.91%	April 2021	75,000	75,000	1,793	415
Swap-cash flow	1.61%	June 2021	50,000	50,000	1,699	769
Swap-cash flow	1.56%	June 2021	50,000	50,000	1,778	869
Swap-cash flow	1.71%	June 2021	50,000	50,000	1,566	598
Swap-cash flow (1)	2.29%	December 2022	200,000	200,000	4,849	(413)
Swap-cash flow (1)	2.29%	December 2022	125,000	125,000	3,054	(259)
Swap-cash flow (1)	2.38%	December 2022	200,000	—	4,180	—
Swap-cash flow (1)	2.38%	December 2022	100,000	—	2,102	—
			$1,993,000	$ 2,186,251	$38,315	$ 8,846

(1) Effective between the maturity of the existing swaps in March 2019 and December 2022.

As of September 30, 2018 and December 31, 2017, the aggregate fair value of the interest rate swap assets of $38.3 million and $10.8 million, respectively, was included in prepaid expense and other assets in the accompanying consolidated balance sheets. As of December 31, 2017, the aggregate fair value of the interest rate swap liabilities of $2.0 million was included in accounts payable and other liabilities in the accompanying consolidated balance sheets.

As of September 30, 2018 and December 31, 2017, there was approximately $38.3 million and $8.8 million, respectively, of unrealized gains included in accumulated other comprehensive income related to interest rate hedges that are effective in offsetting the variable cash flows. There was no ineffectiveness recorded on the designated hedges during the three and nine month periods ended September 30, 2018 and 2017. For the three and nine months ended September 30, 2018, approximately $1.4 million and $1.7 million, respectively, of the amounts included in accumulated other comprehensive income were

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reclassified into interest expense. For the three and nine months ended September 30, 2017, approximately $1.3 million and $6.2 million, respectively, of the amounts included in accumulated other comprehensive loss were reclassified into interest expense. Approximately $10.1 million of the unrealized gains included in accumulated other comprehensive income at September 30, 2018 is expected to be reclassified into interest expense within the next 12 months.

10. Fair Value

Fair Value Measurement

Fair value is defined as the price that would be received upon the sale of an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or most advantageous market. The fair value hierarchy has three levels of inputs, both observable and unobservable:

- Level 1 — Inputs include quoted market prices in an active market for identical assets or liabilities.
- Level 2 — Inputs are market data, other than Level 1, that are observable either directly or indirectly. Level 2 inputs include quoted market prices for similar assets or liabilities, quoted market prices in an inactive market, and other observable information that can be corroborated by market data.
- Level 3 — Inputs are unobservable and corroborated by little or no market data.

Fair Value of Financial Instruments

The Company used the following market assumptions and/or estimation methods:

- Cash and cash equivalents, restricted cash reserves, hotel and other receivables, accounts payable and other liabilities — The carrying amounts reported in the consolidated balance sheets for these financial instruments approximate fair value because of their short term maturities.
- Debt — The Company estimated the fair value of the Senior Notes by using publicly available trading prices, market interest rates, and spreads for the Senior Notes, which are Level 2 and Level 3 inputs in the fair value hierarchy. The Company estimated the fair value of the Revolver and Term Loans by using a discounted cash flow model and incorporating various inputs and assumptions for the effective borrowing rates for debt with similar terms, which are Level 3 inputs in the fair value hierarchy. The Company estimated the fair value of the mortgage loans by using a discounted cash flow model and incorporating various inputs and assumptions for the effective borrowing rates for debt with similar terms and the loan to estimated fair value of the collateral, which are Level 3 inputs in the fair value hierarchy.

The fair value of the Company's debt was as follows (in thousands):

	September 30, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Senior Notes	$506,503	$503,969	$1,062,716	$1,038,892
Revolver and Term Loans, net	1,168,736	1,175,000	1,170,954	1,179,052
Mortgage loans, net	614,925	613,712	646,818	643,078
Debt, net	$2,290,164	$2,292,681	$2,880,488	$2,861,022

Recurring Fair Value Measurements

The following table presents the Company’s fair value hierarchy for those financial assets and liabilities measured at fair value on a recurring basis as of September 30, 2018 (in thousands):

	Fair Value at September 30, 2018			
	Level 1	Level 2	Level 3	Total
Interest rate swap asset	$ —	$ 38,315	$ —	$ 38,315
Interest rate swap liability	—	—	—	—
Total	$ —	$ 38,315	$ —	$ 38,315

The following table presents the Company’s fair value hierarchy for those financial assets and liabilities measured at fair value on a recurring basis as of December 31, 2017 (in thousands):

	Fair Value at December 31, 2017			
	Level 1	Level 2	Level 3	Total
Interest rate swap asset	$ —	$ 10,827	$ —	$ 10,827
Interest rate swap liability	—	(1,981)	—	(1,981)
Total	$ —	$ 8,846	$ —	$ 8,846

The fair values of the derivative financial instruments are determined using widely accepted valuation techniques including a discounted cash flow analysis on the expected cash flows for each derivative. The Company determined that the significant inputs, such as interest yield curves and discount rates, used to value its derivatives fall within Level 2 of the fair value hierarchy and that the credit valuation adjustments associated with the Company’s counterparties and its own credit risk utilize Level 3 inputs, such as estimates of current credit spreads to evaluate the likelihood of default by itself and its counterparties. As of September 30, 2018, the Company assessed the significance of the impact of the credit valuation adjustments on the overall valuation of its derivative positions and determined that the credit valuation adjustments were not significant to the overall valuation of its derivatives. As a result, the Company determined that its derivative valuations in their entirety are classified in Level 2 of the fair value hierarchy.

11. Income Taxes

The Company has elected to be taxed as a REIT under Sections 856 through 860 of the Internal Revenue Code of 1986, as amended (the "Code"). To qualify as a REIT, the Company must meet a number of organizational and operational requirements, including a requirement that it distribute at least 90% of its REIT taxable income, subject to certain adjustments and excluding any net capital gain, to shareholders. The Company’s intention is to adhere to the REIT qualification requirements and to maintain its qualification for taxation as a REIT. As a REIT, the Company is generally not subject to federal corporate income tax on the portion of taxable income that is distributed to shareholders. If the Company fails to qualify for taxation as a REIT in any taxable year, the Company will be subject to U.S. federal income taxes at regular corporate rates (including any applicable alternative minimum tax) and it may not be able to qualify as a REIT for four subsequent taxable years. As a REIT, the Company may be subject to certain state and local taxes on its income and property, and to federal income and excise taxes on undistributed taxable income. The Company’s TRSs will generally be subject to U.S. federal, state, and local income taxes at the applicable rates.

The Company accounts for income taxes using the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax bases, and for net operating loss, capital loss and tax credit carryforwards. The deferred tax assets and liabilities are measured using the enacted income tax rates in effect for the year in which those temporary differences are expected to be realized or settled. The effect on the deferred tax assets and liabilities from a change in tax rates is recognized in earnings in the period when the new rate is enacted. However, deferred tax assets are recognized only to the extent that it is more likely than not that they will be realized based on consideration of all available evidence, including the future reversals of existing taxable temporary differences, future projected taxable income and tax planning strategies. Valuation allowances are provided if, based upon the weight of the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized.

The Company had no accruals for tax uncertainties as of September 30, 2018 and December 31, 2017.

12. Commitments and Contingencies

Restricted Cash Reserves

The Company is obligated to maintain cash reserve funds for future capital expenditures at the hotels (including the periodic replacement or refurbishment of FF&E) as determined pursuant to the management agreements, franchise agreements and/or mortgage loan documents. The management agreements, franchise agreements and/or mortgage loan documents require the Company to reserve cash ranging typically from 3.0% to 5.0% of the individual hotel's revenues and maintain the reserves in restricted cash reserve escrows. Any unexpended amounts will remain the property of the Company upon termination of the management agreements, franchise agreements or mortgage loan documents. As of September 30, 2018 and December 31, 2017, approximately $78.1 million and $72.6 million, respectively, was available in the restricted cash reserves for future capital expenditures, real estate taxes and insurance.

Litigation

Other than the legal proceeding mentioned below, neither the Company nor any of its subsidiaries is currently involved in any regulatory or legal proceedings that management believes will have a material and adverse effect on the Company's financial position, results of operations or cash flows.

Prior to the Mergers, on March 24, 2016, an affiliate of InterContinental Hotels Group PLC ("IHG"), which was previously the hotel management company for three of FelCor's hotels (two of which were sold in 2006, and one of which was converted by FelCor into a Wyndham brand and operation in 2013), notified FelCor that the National Retirement Fund in which the employees at those hotels had participated had assessed a withdrawal liability of $8.3 million, with required quarterly payments including interest, in connection with the termination of IHG's operation of those hotels. FelCor's hotel management agreements with IHG stated that it may be obligated to indemnify and hold IHG harmless for some or all of any amount ultimately contributed to the pension trust fund with respect to those hotels.

Based on the current assessment of the claim, the resolution of this matter may not occur until 2022. As of September 30, 2018, the Company maintained an accrual of approximately $4.6 million for the future quarterly payments to the pension trust fund, which is included in accounts payable and other liabilities in the accompanying consolidated balance sheet.

The Company plans to vigorously defend the underlying claims and, if appropriate, IHG's demand for indemnification.

Management Agreements

As of September 30, 2018, 151 of the Company's hotel properties were operated pursuant to long-term management agreements with initial terms ranging from 3 to 25 years. This number includes 42 hotel properties that receive the benefits of a franchise agreement pursuant to management agreements with Hilton, Hyatt, Marriott, Wyndham, and other hotel brands. Each management company receives a base management fee generally between 3.0% and 3.5% of hotel revenues. Management agreements that include the benefits of a franchise agreement incur a base management fee generally between 2.0% and 7.0% of hotel revenues. The management companies are also eligible to receive an incentive management fee if hotel operating income, as defined in the management agreements, exceeds certain thresholds. The incentive management fee is generally calculated as a percentage of hotel operating income after the Company has received a priority return on its investment in the hotel.

Management fees are included in management and franchise fee expense in the accompanying consolidated statements of operations and comprehensive income. For the three and nine months ended September 30, 2018, the Company incurred management fee expense, including amortization of deferred management fees, of approximately $14.7 million and $45.7 million, respectively. For the three and nine months ended September 30, 2017, the Company incurred management fee expense, including amortization of deferred management fees, of approximately $10.9 million and $32.5 million, respectively.

The Wyndham management agreements guarantee minimum levels of annual net operating income at each of the Wyndham-managed hotels for each year of the initial 10-year term to 2023, subject to an aggregate $100.0 million limit over the term and an annual $21.5 million limit. The Company recognizes the pro-rata portion of the projected aggregate full-year guaranties as a reduction of Wyndham's contractual management and other fees.

Franchise Agreements

As of September 30, 2018, 108 of the Company’s hotel properties were operated under franchise agreements with initial terms ranging from 10 to 30 years. This number excludes 42 hotel properties that receive the benefits of a franchise agreement pursuant to management agreements with Hilton, Hyatt, Marriott, Wyndham, and other hotel brands. In addition, The Knickerbocker is not operated with a hotel brand so the hotel does not have a franchise agreement. Franchise agreements allow the hotel properties to operate under the respective brands. Pursuant to the franchise agreements, the Company pays a royalty fee, generally between 4.0% and 6.0% of room revenue, plus additional fees for marketing, central reservation systems and other franchisor costs generally between 1.0% and 4.3% of room revenue. Certain hotels are also charged a royalty fee of generally 3.0% of food and beverage revenues.

Franchise fees are included in management and franchise fee expense in the accompanying consolidated statements of operations and comprehensive income. For the three and nine months ended September 30, 2018, the Company incurred franchise fee expense of approximately $20.2 million and $62.1 million, respectively. For the three and nine months ended September 30, 2017, the Company incurred franchise fee expense of approximately $18.6 million and $53.6 million, respectively.

13. Equity

Common Shares of Beneficial Interest

In 2015, the Company's board of trustees authorized a share repurchase program to acquire up to $400.0 million of the Common Shares through December 31, 2016. On February 17, 2017, the Company's board of trustees increased the authorized amount that may be repurchased by $40.0 million to a total of $440.0 million. On February 16, 2018, the Company's board of trustees extended the duration of the share repurchase program to February 28, 2019.

During the nine months ended September 30, 2018, the Company did not repurchase and retire any of its Common Shares under the share repurchase program. As of September 30, 2018, the share repurchase program had a remaining capacity of $198.9 million. During the nine months ended September 30, 2017, the Company repurchased and retired 122,508 Common Shares for approximately $2.6 million.

As a result of the REIT Merger, on August 31, 2017, the Company issued 50.4 million Common Shares at a price of $20.18 per share to former FelCor common stockholders as consideration in the REIT Merger.

During the nine months ended September 30, 2018, the Company declared a cash dividend of $0.33 per Common Share in each of the first, second, and third quarters of 2018. During the nine months ended September 30, 2017, the Company declared a cash dividend of $0.33 per Common Share in each of the first, second, and third quarters of 2017.

Series A Preferred Shares

On August 31, 2017, the Company designated and authorized the issuance of up to 12,950,000 $1.95 Series A Preferred Shares. The Company issued 12,879,475 Series A Preferred Shares, at a price of $28.49 per share, to former FelCor preferred stockholders as consideration in the REIT Merger. The holders of the Series A Preferred Shares are entitled to receive dividends that are payable in cash in an amount equal to the greater of (i) $1.95 per annum or (ii) the cash distributions declared or paid for the corresponding period on the number of Common Shares into which a Series A Preferred Share is then convertible.

During the nine months ended September 30, 2018, the Company declared a cash dividend of $0.4875 on each Series A Preferred Share in each of the first, second, and third quarters of 2018. During the nine months ended September 30, 2017, the Company declared a cash dividend of $0.4875 on each Series A Preferred Share in the third quarter of 2017.

Noncontrolling Interest

The Company consolidates the Operating Partnership, which is a majority-owned limited partnership that has a noncontrolling interest. The outstanding OP Units held by the limited partners are redeemable for cash, or at the option of the Company, for a like number of Common Shares. As a result of the Partnership Merger, the Operating Partnership issued 215,152 OP units at a price of $20.18 per unit, to former FelCor LP limited partners as consideration in the Partnership Merger. As of September 30, 2018, 773,902 outstanding OP Units are held by the limited partners. The noncontrolling interest is included in the noncontrolling interest in the Operating Partnership on the consolidated balance sheets.

Consolidated Joint Venture Preferred Equity

The Company's joint venture that redeveloped The Knickerbocker raised $45.0 million ($44.4 million net of issuance costs) through the sale of redeemable preferred equity under the EB-5 Immigrant Investor Program. The purchasers receive a 3.25% current annual return (which increases to 8% if the Company does not redeem the equity interest before the fifth anniversary of the respective equity issuance), plus a 0.25% non-compounding annual return payable at redemption. The fifth anniversary for the majority of the equity issuance is in February 2019. The preferred equity raised by the joint venture is included in preferred equity in a consolidated joint venture on the consolidated balance sheets.

14. Equity Incentive Plan

The Company may issue share-based awards to officers, employees, non-employee trustees and other eligible persons under the RLJ Lodging Trust 2015 Equity Incentive Plan (the "2015 Plan"). The 2015 Plan provides for a maximum of 7,500,000 Common Shares to be issued in the form of share options, share appreciation rights, restricted share awards, unrestricted share awards, share units, dividend equivalent rights, long-term incentive units, other equity-based awards and cash bonus awards.

Share Awards

From time to time, the Company may award unvested restricted shares under the 2015 Plan as compensation to officers, employees and non-employee trustees. The issued shares vest over a period of time as determined by the board of trustees at the date of grant. The Company recognizes compensation expense for time-based unvested restricted shares on a straight-line basis over the vesting period based upon the fair market value of the shares on the date of issuance, adjusted for forfeitures.

Non-employee trustees may also elect to receive unrestricted shares under the 2015 Plan as compensation that would otherwise be paid in cash for their services. The shares issued to non-employee trustees in lieu of cash compensation are unrestricted and include no vesting conditions. The Company recognizes compensation expense for the unrestricted shares issued in lieu of cash compensation on the date of issuance based upon the fair market value of the shares on that date.

A summary of the unvested restricted shares as of September 30, 2018 is as follows:

	2018	
	Number of Shares	Weighted-Average Grant Date Fair Value
Unvested at January 1, 2018	700,325	$ 22.88
Granted	591,851	21.42
Vested	(348,580)	23.22
Forfeited	(113,325)	21.58
Unvested at September 30, 2018	830,271	$ 21.87

For the three and nine months ended September 30, 2018, the Company recognized approximately $3.8 million and $8.1 million, respectively, of share-based compensation expense related to restricted share awards, which includes the accelerated vesting of restricted share awards as a result of the Company's President and Chief Executive Officer retiring in August 2018. For the three and nine months ended September 30, 2017, the Company recognized approximately $2.0 million and $6.7 million, respectively, of share-based compensation expense related to restricted share awards. As of September 30, 2018, there was $15.9 million of total unrecognized compensation costs related to unvested restricted share awards and these costs are expected to be recognized over a weighted-average period of 2.5 years. The total fair value of the shares vested (calculated as the number of shares multiplied by the vesting date share price) during the nine months ended September 30, 2018 and 2017 was approximately $7.7 million and $5.7 million, respectively.

Performance Units

In February 2017, the Company awarded 259,000 performance units with a grant date fair value of $14.93 per unit to certain employees. The performance units vest over a four-year period, including three years of performance-based vesting plus an additional one year of time-based vesting.

In February 2018, the Company awarded 264,000 performance units with a grant date fair value of $13.99 per unit to certain employees. The performance units vest over a four-year period, including three years of performance-based vesting (the "2018 performance units measurement period") plus an additional one year of time-based vesting. These performance units may convert into restricted shares at a range of 25% to 150% of the number of performance units granted contingent upon the Company achieving an absolute total shareholder return and a relative total shareholder return over the measurement period at specified percentiles of the peer group, as defined by the award. If at the end of the 2018 performance units measurement period the target criterion is met, then 50% of the restricted shares will vest immediately. The remaining 50% will vest one year later. The award recipients will not be entitled to receive any dividends prior to the date of conversion. For any restricted shares issued upon conversion, the award recipient will be entitled to receive payment of an amount equal to all dividends that would have been paid if such restricted shares had been issued at the beginning of the 2018 performance units measurement period. The fair value of the performance units is determined using a Monte Carlo simulation with the following assumptions: a risk-free interest rate of 2.42%, volatility of 27.44%, and an expected term equal to the requisite service period for the awards. The Company estimated the compensation expense for the performance units on a straight-line basis using a calculation that recognizes 50% of the grant date fair value over three years and 50% of the grant date fair value over four years.

For the three and nine months ended September 30, 2018, the Company recognized approximately $0.2 million and $1.6 million, respectively, of share-based compensation expense related to the performance unit awards. For the three and nine months ended September 30, 2017, the Company recognized approximately $0.5 million and $1.3 million, respectively, of share-based compensation expense related to the performance unit awards. As of September 30, 2018, there was $3.8 million of total unrecognized compensation costs related to the performance unit awards and these costs are expected to be recognized over a weighted-average period of 2.3 years.

As of September 30, 2018, there were 2,981,978 Common Shares available for future grant under the 2015 Plan.

15. Earnings per Common Share

Basic earnings per Common Share is calculated by dividing net income attributable to common shareholders by the weighted-average number of Common Shares outstanding during the period excluding the weighted-average number of unvested restricted shares outstanding during the period. Diluted earnings per Common Share is calculated by dividing net income attributable to common shareholders by the weighted-average number of Common Shares outstanding during the period, plus any shares that could potentially be outstanding during the period. The potential shares consist of the unvested restricted share grants and unvested performance units, calculated using the treasury stock method. Any anti-dilutive shares have been excluded from the diluted earnings per share calculation.

Unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating shares and are considered in the computation of earnings per share pursuant to the two-class method. If there were any undistributed earnings allocable to the participating shares, they would be deducted from net income attributable to common shareholders used in the basic and diluted earnings per share calculations.

The limited partners’ outstanding OP Units (which may be redeemed for Common Shares under certain circumstances) have been excluded from the diluted earnings per share calculation as there was no effect on the amounts for the three and nine months ended September 30, 2018 and 2017, since the limited partners’ share of income would also be added back to net income attributable to common shareholders.

The computation of basic and diluted earnings per Common Share is as follows (in thousands, except share and per share data):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Numerator:				
Net income attributable to RLJ	$73,975	$ 3,914	$161,378	$ 67,918
Less: Preferred dividends	(6,279)	(2,093)	(18,836)	(2,093)
Less: Dividends paid on unvested restricted shares	(274)	(243)	(937)	(798)
Less: Undistributed earnings attributable to unvested restricted shares	(46)	—	—	—
Net income attributable to common shareholders excluding amounts attributable to unvested restricted shares	$67,376	$ 1,578	$141,605	$ 65,027
Denominator:				
Weighted-average number of Common Shares - basic	174,326,198	140,249,961	174,253,393	129,317,120
Unvested restricted shares	129,075	57,308	109,523	82,057
Unvested performance units	24,068	—	2,185	—
Weighted-average number of Common Shares - diluted	174,479,341	140,307,269	174,365,101	129,399,177
Net income per share attributable to common shareholders - basic	$0.39	$ 0.01	$0.81	$ 0.50
Net income per share attributable to common shareholders - diluted	$0.39	$ 0.01	$0.81	$ 0.50

16. Supplemental Information to Statements of Cash Flows (in thousands)

	For the nine months ended September 30,	
	2018	2017
Reconciliation of cash, cash equivalents, and restricted cash reserves		
Cash and cash equivalents	$425,384	$421,181
Restricted cash reserves	78,113	78,343
Cash, cash equivalents, and restricted cash reserves	$503,497	$499,524
Interest paid	$84,377	$34,170
Income taxes paid	$1,902	$1,107
Supplemental investing and financing transactions		
In conjunction with the sale of hotel properties, the Company recorded the following:		
Sale of hotel properties	$456,600	$—
Transaction costs	(8,432)	(49)
Operating prorations	(431)	—
Proceeds from the sale of hotel properties, net	$447,737	$(49)
Supplemental non-cash transactions (1)		
Accrued capital expenditures	$5,879	$5,465

(1) Refer to Note 3, Merger with FelCor Lodging Trust Incorporated, for information related to the non-cash investing and financing activities associated with the acquisition of FelCor.

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

The following discussion and analysis should be read in conjunction with our consolidated financial statements and related notes included elsewhere in this report, as well as the information contained in our Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on February 28, 2018 (the "Annual Report"), which is accessible on the SEC's website at www.sec.gov.

Statement Regarding Forward-Looking Information

The following information contains certain statements, other than purely historical information, including estimates, projections, statements relating to our business plans, objectives and expected operating results, and the assumptions upon which those statements are based, that are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements generally are identified by the use of the words "believe," "project," "expect," "anticipate," "estimate," "plan," "may," "will," "will continue," "intend," "should," or similar expressions. Although we believe that the expectations reflected in such forward-looking statements are based upon reasonable assumptions, beliefs and expectations, such forward-looking statements are not predictions of future events or guarantees of future performance and our actual results could differ materially from those set forth in the forward-looking statements. Some factors that might cause such a difference include the following: the current global economic uncertainty, increased direct competition, changes in government regulations or accounting rules, changes in local, national and global real estate conditions, declines in the lodging industry, seasonality of the lodging industry, risks related to natural disasters, such as earthquakes and hurricanes, hostilities, including future terrorist attacks or fear of hostilities that affect travel, our ability to obtain lines of credit or permanent financing on satisfactory terms, changes in interest rates, access to capital through offerings of our common and preferred shares of beneficial interest, or debt, our ability to identify suitable acquisitions, our ability to close on identified acquisitions and integrate those businesses and inaccuracies of our accounting estimates. Given these uncertainties, undue reliance should not be placed on such statements.

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Except as required by law, we undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise. We caution investors not to place undue reliance on these forward-looking statements and urge investors to carefully review the disclosures we make concerning risks and uncertainties in the sections entitled "Forward-Looking Statements," "Risk Factors," and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in our Annual Report, as well as the risks, uncertainties and other factors discussed in this Quarterly Report on Form 10-Q and identified in other documents filed by us with the SEC.

Overview

We are a self-advised and self-administered Maryland real estate investment trust ("REIT") that owns primarily premium-branded, high-margin, focused-service and compact full-service hotels. We are one of the largest U.S. publicly-traded lodging REITs in terms of both number of hotels and number of rooms. Our hotels are concentrated in markets that we believe exhibit multiple demand generators and attractive long-term growth prospects. We believe premium-branded, focused-service and compact full-service hotels with these characteristics generate high levels of Revenue per Available Room ("RevPAR"), strong operating margins and attractive returns.

Our strategy is to own primarily premium-branded, focused-service and compact full-service hotels. Focused-service and compact full-service hotels typically generate most of their revenue from room rentals, have limited food and beverage outlets and meeting space, and require fewer employees than traditional full-service hotels. We believe these types of hotels have the potential to generate attractive returns relative to other types of hotels due to their ability to achieve RevPAR levels at or close to those achieved by traditional full-service hotels while achieving higher profit margins due to their more efficient operating model and less volatile cash flows.

As we look at factors that could impact our business, we find that the consumer is generally in good financial health, job creation remains positive, and an increase in wages is adding to consumers' disposable income. While geopolitical and global economic uncertainty still exists and interest rates are rising, we remain cautiously optimistic that positive employment trends, high consumer confidence, and elevated corporate sentiment will continue to drive economic expansion in the U.S. and generate positive lodging demand and RevPAR growth for the industry. However, in light of accelerating supply, RevPAR growth is likely to be moderate.

We continue to follow a prudent and disciplined capital allocation strategy. We will continue to look for and weigh all possible investment decisions against the highest and best returns for our shareholders over the long term. We believe that our cash on hand and expected access to capital (including availability under our revolving credit facility ("Revolver")) along with our senior management team's experience, extensive industry relationships and asset management expertise, will enable us to pursue investment opportunities that generate additional internal and external growth.

As of September 30, 2018, we owned 152 hotel properties with approximately 29,400 rooms, located in 25 states and the District of Columbia. We owned, through wholly-owned subsidiaries, a 100% interest in 148 of our hotel properties, a 98.3% controlling interest in the DoubleTree Metropolitan Hotel New York City, a 95% controlling interest in The Knickerbocker, and 50% interests in entities owning two hotel properties. We consolidate our real estate interests in the 150 hotel properties in which we hold a controlling financial interest, and we record the real estate interests in the two hotels in which we hold an indirect 50% interest using the equity method of accounting. We lease 151 of the 152 hotel properties to our taxable REIT subsidiaries ("TRS"), of which we own a controlling financial interest.

For U.S. federal income tax purposes, we elected to be taxed as a REIT commencing with our taxable year ended December 31, 2011. Substantially all of our assets and liabilities are held by, and all of our operations are conducted through, our operating partnership RLJ Lodging Trust, L.P. (the "Operating Partnership"). We are the sole general partner of the Operating Partnership. As of September 30, 2018, we owned, through a combination of direct and indirect interests, 99.6% of the units of limited partnership interest in the Operating Partnership ("OP units").

Recent Significant Activities

Our significant activities reflect our commitment to creating long-term shareholder value through enhancing our hotel portfolio's quality, recycling capital and maintaining a prudent capital structure. During the nine months ended September 30, 2018, the following significant activities took place:

- In January 2018, we modified our $400.0 million term loan initially due in 2019, our $225.0 million term loan initially due in 2019, and our $150 million term loan due in 2022. We extended the maturity for both the $400.0 million term

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loan and the $225.0 million term loan to January 2023, and we improved the overall pricing for each of the modified term loans.

- In February 2018, we sold the Embassy Suites Boston Marlborough in Marlborough, Massachusetts for $23.7 million.
- In March 2018, we completed the early redemption of the senior secured notes in full for an aggregate principal amount of $524.0 million.
- In March 2018, we sold the Sheraton Philadelphia Society Hill Hotel in Philadelphia, Pennsylvania for $95.5 million.
- In July 2018, we sold the Embassy Suites Napa Valley in Napa, California for $102.0 million.
- In July 2018, we entered into a purchase and sale agreement to sell the Holiday Inn San Francisco - Fisherman's Wharf. At September 30, 2018, this hotel property has been included in assets of hotel properties held for sale, net on the consolidated balance sheet. The transaction closed on October 15, 2018.
- In August 2018, we sold the DoubleTree Hotel Columbia in Columbia, Maryland for $12.9 million.
- In August 2018, we sold The Vinoy Renaissance St. Petersburg Resort & Golf Club in St. Petersburg, Florida for $185.0 million.
- In September 2018, we sold the DoubleTree by Hilton Burlington Vermont in Burlington, Vermont for $35.0 million.
- We declared a cash dividend of $0.4875 on each Series A Preferred Share in each of the first, second, and third quarters of 2018.
- We declared a cash dividend of $0.33 per Common Share in each of the first, second, and third quarters of 2018.

Our Customers

The majority of our hotels consist of premium-branded, focused-service and compact full-service hotels. As a result of this property profile, the majority of our customers are transient in nature. Transient business typically represents individual business or leisure travelers. The majority of our hotels are located in business districts within major metropolitan areas. Accordingly, business travelers represent the majority of the transient demand at our hotels. As a result, macroeconomic factors impacting business travel have a greater effect on our business than factors impacting leisure travel.

Group business is typically defined as a minimum of 10 guestrooms booked together as part of the same piece of business. Group business may or may not use the meeting space at any given hotel. Given the limited meeting space at the majority of our hotels, group business that utilizes meeting space represents a small component of our customer base.

A number of our hotel properties are affiliated with brands marketed toward extended-stay customers. Extended-stay customers are generally defined as those staying five nights or longer.

Our Revenues and Expenses

Our revenues are primarily derived from the operation of hotels, including the sale of rooms, food and beverage revenue and other revenue, which consists of parking fees, golf, pool and other resort fees, gift shop sales and other guest service fees.

Our operating costs and expenses consist of the costs to provide hotel services, including room expense, food and beverage expense, management and franchise fees and other operating expenses. Room expense includes housekeeping and front office wages and payroll taxes, reservation systems, room supplies, laundry services and other costs. Food and beverage expense primarily includes the cost of food, the cost of beverages and associated labor costs. Other operating expenses include labor and other costs associated with the other operating department revenue, as well as labor and other costs associated with administrative departments, sales and marketing, repairs and maintenance and utility costs. Our hotels that are subject to franchise agreements are charged a royalty fee, plus additional fees for marketing, central reservation systems and other franchisor costs, in order for the hotel properties to operate under the respective brands. Franchise fees are based on a percentage of room revenue and for certain hotels additional franchise fees are charged for food and beverage revenue. Our hotels are managed by independent, third-party management companies under long-term agreements pursuant to which the management companies typically earn base and incentive management fees based on the levels of revenues and profitability of each individual hotel property. We generally receive a cash distribution from the hotel management companies on a monthly basis, which reflects hotel-level sales less hotel-level operating expenses.

Key Indicators of Financial Performance

We use a variety of operating, financial and other information to evaluate the operating performance of our business. These key indicators include financial information that is prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") as well as other financial measures that are non-GAAP measures. In addition, we use other information that may not be financial in nature, including industry standard statistical information and comparative data. We use this information to measure the operating performance of our individual hotels, groups of hotels and/or business as a whole. We also use these metrics to evaluate the hotels in our portfolio and potential acquisition opportunities to determine each hotel's contribution to cash flow and its potential to provide attractive long-term total returns. The key indicators include:

- Average Daily Rate ("ADR")
- Occupancy
- RevPAR

ADR, Occupancy and RevPAR are commonly used measures within the lodging industry to evaluate operating performance. RevPAR is an important statistic for monitoring the operating performance at the individual hotel property level and across our entire business. We evaluate the individual hotel RevPAR performance on an absolute basis with comparisons to budget and prior periods, as well as on a regional and company-wide basis. ADR and RevPAR include only room revenue.

We also use non-GAAP measures such as FFO, Adjusted FFO, EBITDA, EBITDAre, and Adjusted EBITDA to evaluate the operating performance of our business. For a more in depth discussion of the non-GAAP measures, please refer to the "Non-GAAP Financial Measures" section.

Critical Accounting Policies

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities at the date of our financial statements and the reported amounts of revenues and expenses during the reporting period. It is possible that the actual amounts may differ significantly from these estimates and assumptions. We evaluate our estimates, assumptions and judgments on an ongoing basis, based on information that is available to us, our business and industry experience, and various other matters that we believe are reasonable and appropriate for consideration under the circumstances. Our Annual Report on Form 10-K for the year ended December 31, 2017 contains a discussion of our critical accounting policies. As discussed in Note 2 to our accompanying consolidated financial statements, Summary of Significant Accounting Policies, we adopted ASU 2014-09 on January 1, 2018. Other than noted below, there have been no other significant changes to our critical accounting policies since December 31, 2017.

Revenue

Our revenue consists of room revenue, food and beverage revenue, and revenue from other hotel operating departments (such as parking fees, golf, pool and other resort fees, gift shop sales and other guest service fees). A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. The contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when the performance obligation is satisfied. Our contracts generally have a single performance obligation, such as renting a hotel room to a customer, or providing food and beverage to a customer, or providing a hotel property-related good or service to a customer. Our performance obligations are generally satisfied at a point in time. We recognize revenue when control of the promised good or service is transferred to the customer, in an amount that reflects the consideration we expect to receive in exchange for the promised good or service. The revenue is recorded net of any sales and occupancy taxes collected from the customer. All rebates or discounts are recorded as a reduction to revenue, and there are no material contingent obligations with respect to rebates and discounts offered by the hotel properties.

Advance deposits and deferred revenue are recognized on the consolidated balance sheets when cash payments are received prior to the satisfaction of a performance obligation. Advance deposits and deferred revenue consist of amounts that are refundable and non-refundable to the customer. The advance deposits and deferred revenue are recognized as revenue in the consolidated statements of operations and comprehensive income when we satisfy our performance obligation to the customer.

An allowance for doubtful accounts is our best estimate of the amount of probable credit losses in the existing accounts receivable portfolio and increases to the allowance for doubtful accounts are recorded as bad debt expense. The allowance for doubtful accounts is calculated as a percentage of the aged accounts receivable.

Results of Operations

At September 30, 2018 and 2017, we owned 152 and 159 hotel properties, respectively. Based on when a hotel property is acquired, sold or closed for renovation, the operating results for certain hotel properties are not comparable for the three and nine months ended September 30, 2018 and 2017. The non-comparable hotel properties include 37 hotel properties that were acquired in the Company's merger with FelCor Lodging Trust Incorporated ("FelCor") and seven dispositions that were completed between January 1, 2017 and September 30, 2018.

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Comparison of the three months ended September 30, 2018 to the three months ended September 30, 2017

	For the three months ended September 30,			
	2018	2017	$ Change	% Change
	(amounts in thousands)			
Revenues				
Operating revenues				
Room revenue	$377,237	$292,046	$85,191	29.2 %
Food and beverage revenue	47,211	35,580	11,631	32.7 %
Other revenue	22,594	13,629	8,965	65.8 %
Total revenues	$447,042	$341,255	$105,787	31.0 %
Expenses				
Operating expenses				
Room expense	$95,161	$69,380	$25,781	37.2 %
Food and beverage expense	37,780	27,061	10,719	39.6 %
Management and franchise fee expense	34,838	29,571	5,267	17.8 %
Other operating expense	105,646	78,120	27,526	35.2 %
Total property operating expenses	273,425	204,132	69,293	33.9 %
Depreciation and amortization	60,373	45,231	15,142	33.5 %
Property tax, insurance and other	34,382	23,618	10,764	45.6 %
General and administrative	11,622	9,506	2,116	22.3 %
Transaction costs	261	32,607	(32,346)	(99.2)%
Total operating expenses	380,063	315,094	64,969	20.6 %
Operating income	66,979	26,161	40,818	— %
Other income	856	110	746	— %
Interest income	1,149	1,157	(8)	(0.7)%
Interest expense	(24,629)	(19,650)	(4,979)	25.3 %
Gain (loss) on sale of hotel properties, net	35,895	(19)	35,914	— %
Loss on extinguishment of indebtedness	(1,656)	—	(1,656)	100.0 %
Gain on settlement of an investment in loan	—	2,670	(2,670)	(100.0)%
Income before equity in income from unconsolidated joint ventures	78,594	10,429	68,165	— %
Equity in income from unconsolidated joint ventures	219	57	162	— %
Income before income tax expense	78,813	10,486	68,327	— %
Income tax expense	(4,156)	(6,375)	2,219	(34.8)%
Net income	74,657	4,111	70,546	— %
Net income attributable to noncontrolling interests:				
Noncontrolling interest in consolidated joint ventures	(9)	(32)	23	(71.9)%
Noncontrolling interest in the Operating Partnership	(299)	(43)	(256)	— %
Preferred distributions - consolidated joint venture	(374)	(122)	(252)	— %
Net income attributable to RLJ	73,975	3,914	70,061	— %
Preferred dividends	(6,279)	(2,093)	(4,186)	— %
Net income attributable to common shareholders	$67,696	$1,821	$65,875	— %

Revenues

Total revenues increased $105.8 million, or 31.0%, to $447.0 million for the three months ended September 30, 2018 from $341.3 million for the three months ended September 30, 2017. The increase was a result of an $85.2 million increase in room revenue, an $11.6 million increase in food and beverage revenue, and a $9.0 million increase in other revenue.

Room Revenue

Room revenue increased $85.2 million, or 29.2%, to $377.2 million for the three months ended September 30, 2018 from $292.0 million for the three months ended September 30, 2017. The increase was a result of an $89.0 million increase in room revenue attributable to the non-comparable properties, partially offset by a $3.8 million decrease in room revenue attributable to the comparable properties. The decrease in room revenue from the comparable properties was attributable to a 1.6% decrease in RevPAR, led by RevPAR decreases in our Louisville and Austin markets of 17.1% and 9.0%, respectively, which were partially offset by RevPAR increases in our Northern California and Chicago markets of 7.3% and 6.7%, respectively.

The following are the quarter-to-date key hotel operating statistics for the comparable properties owned at September 30, 2018 and 2017, respectively:

	For the three months ended September 30,		
	2018	2017	% Change
Number of comparable properties (at end of period)	121	121	—
Occupancy	78.4 %	80.3 %	(2.3)%
ADR	$163.33	$162.15	0.7 %
RevPAR	$128.10	$130.18	(1.6)%

Food and Beverage Revenue

Food and beverage revenue increased $11.6 million to $47.2 million for the three months ended September 30, 2018 from $35.6 million for the three months ended September 30, 2017. The increase was a result of an $11.3 million increase in food and beverage revenue attributable to the non-comparable properties and a $0.3 million increase in food and beverage revenue attributable to the comparable properties.

Other Revenue

Other revenue, which includes revenue derived from ancillary sources such as parking fees, golf, pool and other resort fees, gift shop sales and other guest service fees, increased $9.0 million to $22.6 million for the three months ended September 30, 2018 from $13.6 million for the three months ended September 30, 2017. The increase was due to an $8.5 million increase in other revenue attributable to the non-comparable properties and a $0.4 million increase in other revenue attributable to the comparable properties.

Property Operating Expenses

Property operating expenses increased $69.3 million, or 33.9%, to $273.4 million for the three months ended September 30, 2018 from $204.1 million for the three months ended September 30, 2017. The increase was due to a $66.4 million increase in property operating expenses attributable to the non-comparable properties and a $2.9 million increase in property operating expenses attributable to the comparable properties.

The components of our property operating expenses for the comparable properties owned at September 30, 2018 and 2017, respectively, were as follows (in thousands):

	For the three months ended September 30,			
	2018	2017	$ Change	% Change
Room expense	$58,000	$55,765	$2,235	4.0 %
Food and beverage expense	19,022	18,539	483	2.6 %
Management and franchise fee expense	26,649	26,991	(342)	(1.3)%
Other operating expense	60,429	59,939	490	0.8 %
Total property operating expenses	$164,100	$161,234	$2,866	1.8 %

The increase in property operating expenses attributable to the comparable properties was due to higher room expense, food and beverage expense, and other operating expense. Room expense, food and beverage expense, and other operating expense fluctuate based on various factors, including changes in occupancy, labor costs, utilities and insurance costs. Management fees and franchise fees, which are computed as a percentage of gross revenue and room revenue, respectively, decreased as a result of lower revenues at the comparable properties.

Depreciation and Amortization

Depreciation and amortization expense increased $15.1 million, or 33.5%, to $60.4 million for the three months ended September 30, 2018 from $45.2 million for the three months ended September 30, 2017. The increase was a result of a $13.9 million increase in depreciation and amortization expense attributable to the non-comparable properties and a $1.2 million increase in depreciation and amortization expense attributable to the comparable properties.

Property Tax, Insurance and Other

Property tax, insurance and other expense increased $10.8 million, or 45.6%, to $34.4 million for the three months ended September 30, 2018 from $23.6 million for the three months ended September 30, 2017. The increase was attributable to a $10.3 million increase in property tax, insurance and other expense attributable to the non-comparable properties and a $0.4 million increase in property tax, insurance and other expense attributable to the comparable properties. The increase in property tax, insurance and other expense attributable to the non-comparable properties includes property tax reassessments in certain jurisdictions as a result of the merger with FelCor.

General and Administrative

General and administrative expense increased $2.1 million, or 22.3%, to $11.6 million for the three months ended September 30, 2018 from $9.5 million for the three months ended September 30, 2017. The increase in general and administrative expense was primarily due to the Company's larger operating platform as a result of the merger with FelCor, which included a $1.8 million increase in compensation expense and an increase of $1.2 million in professional fees and other general and administrative costs. The increase in compensation expense for the three months ended September 30, 2018 was due to an increase in salary, bonus, and other employee compensation costs, which includes the accelerated vesting of restricted share awards as a result of the Company's President and Chief Executive Officer retiring in August 2018. The increase in general and administrative expense was partially offset by a net decrease of $0.9 million related to expenses that were outside of the normal course of operations, including debt modification costs, executive transition costs, receipts of prior year employee tax credits, and professional fees incurred related to an activist shareholder defense.

Transaction Costs

Transaction costs decreased $32.3 million, or 99.2%, to $0.3 million for the three months ended September 30, 2018 from $32.6 million for the three months ended September 30, 2017. The decrease in transaction costs was attributable to a decrease of approximately $32.2 million in transaction and integration costs related to the merger with FelCor during the three months ended September 30, 2018.

Interest Expense

The components of our interest expense for the three months ended September 30, 2018 and 2017 were as follows (in thousands):

	For the three months ended September 30,			
	2018	2017	$ Change	% Change
Senior Notes	$5,954	$3,980	$1,974	49.6 %
Revolver and Term Loans	11,042	9,834	1,208	12.3 %
Mortgage loans	6,753	4,943	1,810	36.6 %
Amortization of deferred financing costs	880	893	(13)	(1.5)%
Total interest expense	$24,629	$19,650	$4,979	25.3 %

Interest expense increased $5.0 million, or 25.3%, to $24.6 million for the three months ended September 30, 2018 from $19.7 million for the three months ended September 30, 2017. The increase in interest expense was primarily due to assuming the senior secured notes and the senior unsecured notes (collectively the "Senior Notes") and mortgage loans in the merger with FelCor, along with the outstanding borrowings under the Revolver during the three months ended September 30, 2018. The increase in interest expense was partially offset by the redemption of the senior secured notes in March 2018 and the payoff of the Revolver in August 2018.

Loss on Extinguishment of Indebtedness

During the three months ended September 30, 2018, the Company recognized a loss on extinguishment of indebtedness of approximately $1.7 million, which was due to the early payoff of a mortgage loan that was encumbered by a hotel property that was sold during the three months ended September 30, 2018.

Gain on Settlement of Investment in Loan

During the three months ended September 30, 2017, the Company recognized a gain on settlement of investment in loan of approximately $2.7 million as a result of the investment in loan maturing in September 2017.

Income Taxes

As part of our structure, we own TRSs that are subject to federal and state income taxes. Income tax expense decreased $2.2 million, or 34.8%, to $4.2 million for the three months ended September 30, 2018 from $6.4 million for the three months ended September 30, 2017. The decrease in income tax expense was due to a decrease in the U.S. corporate income tax rate from 35% to 21% for the three months ended September 30, 2018 as compared to the three months ended September 30, 2017.

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Comparison of the nine months ended September 30, 2018 to the nine months ended September 30, 2017

	For the nine months ended September 30,			
	2018	2017	$ Change	% Change
	(amounts in thousands)			
Revenues				
Operating revenues				
Room revenue	$1,138,115	$770,751	$367,364	47.7 %
Food and beverage revenue	157,850	91,392	66,458	72.7 %
Other revenue	65,362	31,628	33,734	— %
Total revenues	$1,361,327	$893,771	$467,556	52.3 %
Expenses				
Operating expenses				
Room expense	$279,589	$176,523	$103,066	58.4 %
Food and beverage expense	121,450	66,458	54,992	82.7 %
Management and franchise fee expense	107,766	86,110	21,656	25.1 %
Other operating expense	320,325	195,000	125,325	64.3 %
Total property operating expenses	829,130	524,091	305,039	58.2 %
Depreciation and amortization	183,429	122,136	61,293	50.2 %
Property tax, insurance and other	104,418	60,929	43,489	71.4 %
General and administrative	38,059	28,757	9,302	32.3 %
Transaction costs	2,181	36,923	(34,742)	(94.1)%
Total operating expenses	1,157,217	772,836	384,381	49.7 %
Operating income	204,110	120,935	83,175	68.8 %
Other income	2,514	323	2,191	— %
Interest income	3,339	2,306	1,033	44.8 %
Interest expense	(78,772)	(48,527)	(30,245)	62.3 %
Gain (loss) on sale of hotel properties, net	32,957	(49)	33,006	— %
Gain on extinguishment of indebtedness, net	6,010	—	6,010	100.0 %
Gain on settlement of an investment in loan	—	2,670	(2,670)	(100.0)%
Income before equity in income from unconsolidated joint ventures	170,158	77,658	92,500	76.6 %
Equity in income from unconsolidated joint ventures	637	57	580	— %
Income before income tax expense	170,795	77,715	93,080	77.3 %
Income tax expense	(7,852)	(9,362)	1,510	(16.1)%
Net income	162,943	68,353	94,590	— %
Net loss (income) attributable to noncontrolling interests:				
Noncontrolling interest in consolidated joint ventures	170	5	165	— %
Noncontrolling interest in the Operating Partnership	(626)	(318)	(308)	96.9 %
Preferred distributions - consolidated joint venture	(1,109)	(122)	(987)	— %
Net income attributable to RLJ	161,378	67,918	93,460	— %
Preferred dividends	(18,836)	(2,093)	(16,743)	— %
Net income attributable to common shareholders	$142,542	$65,825	$76,717	— %

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Revenues

Total revenues increased $467.6 million, or 52.3%, to $1.36 billion for the nine months ended September 30, 2018 from $893.8 million for the nine months ended September 30, 2017. The increase was a result of a $367.4 million increase in room revenue, a $66.5 million increase in food and beverage revenue, and a $33.7 million increase in other revenue.

Room Revenue

Room revenue increased $367.4 million, or 47.7%, to $1.14 billion for the nine months ended September 30, 2018 from $770.8 million for the nine months ended September 30, 2017. The increase was a result of a $368.6 million increase in room revenue attributable to the non-comparable properties, partially offset by a $1.2 million decrease in room revenue attributable to the comparable properties. The decrease in room revenue from the comparable properties was attributable to a 0.2% decrease in RevPAR, led by RevPAR decreases in our Louisville and Austin markets of 13.4% and 5.2%, respectively, which were partially offset by RevPAR increases in our Northern California and Chicago markets of 7.7% and 5.6%, respectively.

The following are the year-to-date key hotel operating statistics for the comparable properties owned at September 30, 2018 and 2017, respectively:

	For the nine months ended September 30,		
	2018	2017	% Change
Number of comparable properties (at end of period)	121	121	—
Occupancy	78.5 %	78.6 %	(0.1)%
ADR	$166.71	$166.93	(0.1)%
RevPAR	$130.92	$131.16	(0.2)%

Food and Beverage Revenue

Food and beverage revenue increased $66.5 million, or 72.7%, to $157.9 million for the nine months ended September 30, 2018 from $91.4 million for the nine months ended September 30, 2017. The increase was a result of a $68.0 million increase in food and beverage revenue attributable to the non-comparable properties, partially offset by a $1.5 million decrease in food and beverage revenue attributable to the comparable properties.

Other Revenue

Other revenue, which includes revenue derived from ancillary sources such as parking fees, golf, pool and other resort fees, gift shop sales and other guest service fees, increased $33.7 million to $65.4 million for the nine months ended September 30, 2018 from $31.6 million for the nine months ended September 30, 2017. The increase was due to a $33.0 million increase in other revenue attributable to the non-comparable properties and a $0.7 million increase in other revenue attributable to the comparable properties.

Property Operating Expenses

Property operating expenses increased $305.0 million, or 58.2%, to $829.1 million for the nine months ended September 30, 2018 from $524.1 million for the nine months ended September 30, 2017. The increase was due to a $295.5 million increase in property operating expenses attributable to the non-comparable properties and a $9.6 million increase in property operating expenses attributable to the comparable properties.

The components of our property operating expenses for the comparable properties owned at September 30, 2018 and 2017, respectively, were as follows (in thousands):

	For the nine months ended September 30,			
	2018	2017	$ Change	% Change
Room expense	$167,782	$162,383	$5,399	3.3 %
Food and beverage expense	58,891	57,417	1,474	2.6 %
Management and franchise fee expense	83,190	83,211	(21)	— %
Other operating expense	178,504	175,797	2,707	1.5 %
Total property operating expenses	$488,367	$478,808	$9,559	2.0 %

The increase in property operating expense attributable to the comparable properties was due to higher room expense, food and beverage expense, and other operating expense. Room expense, food and beverage expense, and other operating expense fluctuate based on various factors, including changes in occupancy, labor costs, utilities and insurance costs. Management fees and franchise fees, which are computed as a percentage of gross revenue and room revenue, respectively, decreased as a result of lower revenues at the comparable properties.

Depreciation and Amortization

Depreciation and amortization expense increased $61.3 million, or 50.2%, to $183.4 million for the nine months ended September 30, 2018 from $122.1 million for the nine months ended September 30, 2017. The increase was a result of a $59.7 million increase in depreciation and amortization expense attributable to the non-comparable properties and a $1.6 million increase in depreciation and amortization expense attributable to the comparable properties.

Property Tax, Insurance and Other

Property tax, insurance and other expense increased $43.5 million, or 71.4%, to $104.4 million for the nine months ended September 30, 2018 from $60.9 million for the nine months ended September 30, 2017. The increase was primarily attributable to a $41.7 million increase in property tax, insurance and other expense attributable to the non-comparable properties and a $1.8 million increase in property tax, insurance and other expense attributable to the comparable properties. The increase in property tax, insurance and other expense attributable to the non-comparable properties includes property tax reassessments in certain jurisdictions as a result of the merger with FelCor.

General and Administrative

General and administrative expense increased $9.3 million, or 32.3%, to $38.1 million for the nine months ended September 30, 2018 from $28.8 million for the nine months ended September 30, 2017. The increase in general and administrative expense was primarily attributable to the Company's larger operating platform as a result of the merger with FelCor, which included an increase of $3.6 million in professional fees and other general and administrative costs and a $2.9 million increase in compensation expense. The increase in compensation expense for the nine months ended September 30, 2018 was due to an increase in salary, bonus, and other employee compensation costs, which includes the accelerated vesting of restricted share awards as a result of the Company's President and Chief Executive Officer retiring in August 2018. The remaining increase in general and administrative expense was due to an increase of $2.8 million related to expenses that were outside of the normal course of operations, including debt modification costs, executive transition costs, receipts of prior year employee tax credits, and professional fees incurred related to an activist shareholder defense.

Transaction Costs

Transaction costs decreased $34.7 million, or 94.1%, to $2.2 million for the nine months ended September 30, 2018 from $36.9 million for the nine months ended September 30, 2017. The decrease in transaction costs was attributable to a decrease of approximately $35.4 million in transaction and integration costs related to the merger with FelCor during the nine months ended September 30, 2018, partially offset by an increase of approximately $0.6 million in transaction costs that were incurred by the Company as a result of the higher volume of asset disposition transactions during the nine months ended September 30, 2018.

Interest Expense

The components of our interest expense for the nine months ended September 30, 2018 and 2017 were as follows (in thousands):

	For the nine months ended September 30,			
	2018	2017	$ Change	% Change
Senior Notes	$22,485	$3,980	$18,505	464.9 %
Revolver and Term Loans	33,428	28,981	4,447	15.3 %
Mortgage loans	20,171	12,969	7,202	55.5 %
Amortization of deferred financing costs	2,688	2,597	91	3.5 %
Total interest expense	$78,772	$48,527	$30,245	62.3 %

Interest expense increased $30.2 million to $78.8 million for the nine months ended September 30, 2018 from $48.5 million for the nine months ended September 30, 2017. The increase in interest expense was primarily due to assuming the Senior Notes and mortgage loans in the merger with FelCor, along with the outstanding borrowings under the Revolver during the nine months ended September 30, 2018. The increase in interest expense was partially offset by the redemption of the senior secured notes in March 2018 and the payoff of the Revolver in August 2018.

Gain on Extinguishment of Indebtedness, net

During the nine months ended September 30, 2018, the Company recognized a net gain on extinguishment of indebtedness of approximately $6.0 million. In March 2018, the Company recognized a $7.7 million gain on extinguishment of indebtedness, which was due to the early redemption of the senior secured notes. The gain on extinguishment of indebtedness related to the early redemption of the senior secured notes excludes $5.1 million related to two hotel properties that were sold during the nine months ended September 30, 2018, which is included in gain on sale of hotel properties in the accompanying consolidated statement of operations and comprehensive income. In July 2018, the Company recognized a $1.7 million loss on extinguishment of indebtedness, which was due to the early payoff of a mortgage loan that was encumbered by a hotel property that was sold during the nine months ended September 30, 2018.

Gain on Settlement of Investment in Loan

During the nine months ended September 30, 2017, the Company recognized a gain on settlement of investment in loan of approximately $2.7 million as a result of the investment in loan maturing in September 2017.

Income Taxes

As part of our structure, we own TRSs that are subject to federal and state income taxes. Income tax expense decreased $1.5 million, or 16.1%, to $7.9 million for the nine months ended September 30, 2018 from $9.4 million for the nine months ended September 30, 2017. The decrease in income tax expense was due to a decrease in the U.S. corporate income tax rate from 35% to 21% for the nine months ended September 30, 2018 as compared to the nine months ended September 30, 2017.

Non-GAAP Financial Measures

We consider the following non-GAAP financial measures useful to investors as key supplemental measures of our performance: (1) FFO, (2) Adjusted FFO, (3) EBITDA, (4) EBITDAre and (5) Adjusted EBITDA. These non-GAAP financial measures should be considered along with, but not as alternatives to, net income or loss as a measure of our operating performance. FFO, Adjusted FFO, EBITDA, EBITDAre, and Adjusted EBITDA, as calculated by us, may not be comparable to FFO, Adjusted FFO, EBITDA, EBITDAre and Adjusted EBITDA as reported by other companies that do not define such terms exactly as we define such terms.

Funds From Operations

We calculate funds from operations ("FFO") in accordance with standards established by the National Association of Real Estate Investment Trusts ("NAREIT"), which defines FFO as net income or loss, excluding gains or losses from sales of real estate, impairment, the cumulative effect of changes in accounting principles, plus depreciation and amortization, and adjustments for unconsolidated partnerships and joint ventures. Historical cost accounting for real estate assets implicitly assumes that the value of real estate assets diminishes predictably over time. Since real estate values instead have historically risen or fallen with market conditions, most real estate industry investors consider

FFO to be helpful in evaluating a real estate company's operations. We believe that the presentation of FFO provides useful information to investors regarding our operating performance and can facilitate comparisons of operating performance between periods and between REITs, even though FFO does not represent an amount that accrues directly to common shareholders. Our calculation of FFO may not be comparable to measures calculated by other companies who do not use the NAREIT definition of FFO or do not calculate FFO per diluted share in accordance with NAREIT guidance. Additionally, FFO may not be helpful when comparing us to non-REITs. We present FFO attributable to common shareholders, which includes our OP units, because our OP units may be redeemed for common shares. We believe it is meaningful for the investor to understand FFO attributable to all common shares and OP units.

We further adjust FFO for certain additional items that are not in NAREIT's definition of FFO, such as hotel transaction costs, non-cash income tax expense or benefit, the amortization of share-based compensation, and certain other expenses that we consider outside the normal course of operations. We believe that Adjusted FFO provides useful supplemental information to investors regarding our ongoing operating performance that, when considered with net income and FFO, is beneficial to an investor's understanding of our operating performance.

The following table is a reconciliation of our GAAP net income to FFO attributable to common shareholders and unitholders and Adjusted FFO attributable to common shareholders and unitholders for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Net income	$74,657	$4,111	$162,943	$68,353
Preferred dividends	(6,279)	(2,093)	(18,836)	(2,093)
Preferred distributions - consolidated joint venture	(374)	(122)	(1,109)	(122)
Depreciation and amortization	60,373	45,231	183,429	122,136
(Gain) loss on sale of hotel properties, net	(35,895)	19	(32,957)	49
Noncontrolling interest in consolidated joint ventures	(9)	(32)	170	5
Adjustments related to consolidated joint ventures (1)	(78)	(46)	(233)	(109)
Adjustments related to unconsolidated joint ventures (2)	661	193	1,998	193
FFO	93,056	47,261	295,405	188,412
Transaction costs	261	32,607	2,181	36,923
Loss (gain) on extinguishment of indebtedness, net	1,656	—	(6,010)	—
Gain on settlement of investment in loan	—	(2,670)	—	(2,670)
Amortization of share-based compensation	4,036	2,495	9,722	7,964
Non-cash income tax expense	3,217	5,711	6,171	7,972
Other (income) expenses (3)	(839)	1,116	3,330	1,116
Adjusted FFO	$101,387	$86,520	$310,799	$239,717

(1) Includes depreciation and amortization expense allocated to the noncontrolling interest in the consolidated joint ventures.
(2) Includes our ownership interest of the depreciation and amortization expense of the unconsolidated joint ventures.
(3) Represents income and expenses outside of the normal course of operations, including debt modification costs, hurricane-related costs that were not reimbursed by insurance, executive transition costs, receipts of prior year employee tax credits, and activist shareholder costs.

EBITDA and EBITDAre

Earnings before interest, taxes, depreciation and amortization ("EBITDA") is defined as net income or loss excluding: (1) interest expense; (2) provision for income taxes, including income taxes applicable to sales of assets; and (3) depreciation and amortization. We consider EBITDA useful to an investor in evaluating and facilitating comparisons of our operating performance between periods and between REITs by removing the impact of our capital structure (primarily interest expense) and asset base (primarily depreciation and amortization) from our operating results. In addition, EBITDA is used as one measure in determining the value of hotel acquisitions and disposals.

In addition to EBITDA, we present EBITDAre in accordance with NAREIT guidelines, which defines EBITDAre as net income or loss excluding interest expense, income tax expense, depreciation and amortization expense, gains or losses from sales of real estate, impairment, and adjustments for unconsolidated joint ventures. We believe that the presentation of EBITDAre provides useful information to investors regarding the Company's operating performance and can facilitate comparisons of operating performance between periods and between REITs.

We also present Adjusted EBITDA, which includes additional adjustments for items such as gains or losses on extinguishment of indebtedness, transaction costs, the amortization of share-based compensation, and certain other expenses that we consider outside the normal course of operations. We believe that Adjusted EBITDA provides useful supplemental information to investors regarding our ongoing operating performance that, when considered with net income, EBITDA, and EBITDAre, is beneficial to an investor's understanding of our operating performance. We previously presented Adjusted EBITDA in a similar manner, with the exception of the adjustments for noncontrolling interests in consolidated joint ventures, which totaled less than $0.1 million for both the three and nine months ended September 30, 2017. The rationale for including

100% of Adjusted EBITDA for the consolidated joint ventures with noncontrolling interests is that the full amount of any debt for the consolidated joint ventures is reported in our consolidated balance sheet and the metrics using debt to EBITDA provide a better understanding of the Company's leverage. This is also consistent with NAREIT's definition of EBITDAre.

The following table is a reconciliation of our GAAP net income to EBITDA, EBITDAre and Adjusted EBITDA for the three and nine months ended September 30, 2018 and 2017 (in thousands):

	For the three months ended September 30,		For the nine months ended September 30,	
	2018	2017	2018	2017
Net income	$74,657	$4,111	$162,943	$68,353
Depreciation and amortization	60,373	45,231	183,429	122,136
Interest expense, net (1)	23,479	18,873	75,433	47,589
Income tax expense	4,156	6,375	7,852	9,362
Adjustments related to unconsolidated joint ventures (2)	788	236	2,379	236
EBITDA	163,453	74,826	432,036	247,676
(Gain) loss on sale of hotel properties, net	(35,895)	19	(32,957)	49
EBITDAre	127,558	74,845	399,079	247,725
Transaction costs	261	32,607	2,181	36,923
Loss (gain) on extinguishment of indebtedness, net	1,656	—	(6,010)	—
Gain on settlement of investment in loan	—	(2,670)	—	(2,670)
Amortization of share-based compensation	4,036	2,495	9,722	7,964
Other (income) expenses (3)	(839)	1,116	3,330	1,116
Adjusted EBITDA	$132,672	$108,393	$408,302	$291,058

(1) Excludes amounts attributable to investment in loans of $0.4 million and $1.4 million for the three and nine months ended September 30, 2017, respectively.

(2) Includes our ownership interest of the interest, depreciation, and amortization expense of the unconsolidated joint ventures.

(3) Represents income and expenses outside of the normal course of operations, including debt modification costs, hurricane-related costs that were not reimbursed by insurance, executive transition costs, receipts of prior year employee tax credits, and activist shareholder costs.

Liquidity and Capital Resources

Our short-term liquidity requirements consist primarily of the funds necessary to pay for operating expenses and other expenditures directly associated with our hotel properties, including:

- recurring maintenance and capital expenditures necessary to maintain our hotel properties in accordance with brand standards;
- interest expense and scheduled principal payments on outstanding indebtedness; and
- distributions necessary to qualify for taxation as a REIT.

In addition, we expect to incur severance and termination payments to certain employees who were terminated in connection with the closure of one of the two buildings at the Holiday Inn San Francisco - Fisherman's Wharf hotel property. The building closed due to the underlying ground lease expiring on October 31, 2018, which resulted in the land and the building reverting to the ground lessor. The second building at the Holiday Inn San Francisco - Fisherman's Wharf hotel property was sold in connection with the sale of the hotel property, which is discussed in Note 6 to our accompanying consolidated financial statements, Sale of Hotel Properties.

We expect to meet our short-term liquidity requirements generally through the net cash provided by operations, existing cash balances, short-term borrowings under our Revolver, of which $600.0 million was available at September 30, 2018, proceeds from the sale of hotel properties, and proceeds from public offerings of common shares.

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Our long-term liquidity requirements consist primarily of the funds necessary to pay for the costs of acquiring additional hotel properties, the redevelopments, renovations, expansions and other capital expenditures that need to be made periodically with respect to our hotel properties, and scheduled debt payments, at maturity or otherwise. We expect to meet our long-term liquidity requirements through various sources of capital, including our Revolver and future equity (including OP units) or debt offerings, existing working capital, the net cash provided by operations, long-term mortgage loans and other secured and unsecured borrowings, and the proceeds from the sale of hotel properties.

Sources and Uses of Cash

As of September 30, 2018, we had $503.5 million of cash, cash equivalents, and restricted cash reserves as compared to $659.1 million at December 31, 2017.

Cash flows from Operating Activities

The net cash flow provided by operating activities totaled $313.5 million and $207.3 million for the nine months ended September 30, 2018 and 2017, respectively. Our cash flows provided by operating activities generally consist of the net cash generated by our hotel operations, partially offset by the cash paid for corporate expenses and other working capital changes. Refer to the "Results of Operations" section for further discussion of our operating results for the nine months ended September 30, 2018 and 2017.

Cash flows from Investing Activities

The net cash flow provided by investing activities totaled $303.4 million for the nine months ended September 30, 2018 primarily due to $447.7 million of net cash proceeds from the sale of hotel properties, partially offset by $144.2 million in routine capital improvements and additions to our hotel properties.

The net cash flow used in investing activities totaled $71.1 million for the nine months ended September 30, 2017 primarily due to $58.9 million in routine capital improvements and additions to our hotel properties and a net cash payment of $24.9 million for the acquisition of FelCor. The net cash flow used in investing activities was partially offset by $12.8 million in proceeds on the settlement of an investment in loan.

Cash flows from Financing Activities

The net cash flow used in financing activities totaled $772.5 million for the nine months ended September 30, 2018 primarily due to a payment of $539.0 million to redeem the senior secured notes, $193.0 million in distributions to shareholders and unitholders, $32.9 million in mortgage loans principal payments, $3.6 million in deferred financing cost payments, and $2.9 million paid to repurchase common shares.

The net cash flow used in financing activities totaled $160.5 million for the nine months ended September 30, 2017 primarily due to $151.4 million in distributions to shareholders and unitholders, $2.6 million paid to repurchase common shares under a share repurchase program, $2.2 million paid to repurchase common shares, and $3.2 million in mortgage loans principal payments.

Capital Expenditures and Reserve Funds

We maintain each of our hotel properties in good repair and condition and in conformity with applicable laws and regulations, franchise agreements and management agreements. The cost of all such routine improvements and alterations are paid out of furniture, fixtures and equipment ("FF&E") reserves, which are funded by a portion of each hotel property's gross revenues. Routine capital expenditures are administered by the property management companies. However, we have approval rights over the capital expenditures as part of the annual budget process for each of our hotel properties.

From time to time, certain of our hotel properties may undergo renovations as a result of our decision to upgrade portions of the hotels, such as guestrooms, public space, meeting space, and/or restaurants, in order to better compete with other hotels and alternative lodging options in our markets. In addition, upon acquisition of a hotel property we often are required to complete a property improvement plan in order to bring the hotel up to the respective franchisor's standards. If permitted by the terms of the management agreement, funding for a renovation will first come from the FF&E reserves. To the extent that the FF&E reserves are not available or sufficient to cover the cost of the renovation, we will fund all or the remaining portion of the renovation with cash and cash equivalents on hand, our Revolver and/or other sources of available liquidity.

With respect to some of our hotels that are operated under franchise agreements with major national hotel brands and for some of our hotels subject to first mortgage liens, we are obligated to maintain FF&E reserve accounts for future capital expenditures at these hotels. The amount funded into each of these reserve accounts is generally determined pursuant to the management agreements, franchise agreements and/or mortgage loan documents for each of the respective hotels, and typically ranges between 3.0% and 5.0% of the respective hotel's total gross revenue. As of September 30, 2018, approximately $73.2 million was held in FF&E reserve accounts for future capital expenditures.

Off-Balance Sheet Arrangements

As of September 30, 2018, we owned 50% interests in joint ventures that owned two hotel properties. We own more than 50% of the operating lessee for one of these hotels and the other hotel is operated without a lease. The Company also owned 50% interests in joint ventures that owned real estate and a condominium management business that are associated with two of our resort hotel properties. None of our trustees, officers or employees holds an ownership interest in any of these joint ventures or entities.

One of the 50% unconsolidated joint ventures that owns a hotel property has $21.1 million of non-recourse mortgage debt, of which our pro rata portion was $10.6 million, none of which is reflected as a liability on our consolidated balance sheet. Our liabilities with regard to the non-recourse debt and the liabilities of our subsidiaries that are members or partners in joint ventures are generally limited to guaranties of the borrowing entity's obligations to pay for the lender's losses caused by misconduct, fraud or misappropriation of funds by the venture and other typical exceptions from the non-recourse provisions in the mortgages, such as for environmental liabilities. In addition, this joint venture is subject to two ground leases with terms expiring in 2044.

The other 50% unconsolidated joint venture that owns a hotel property is subject to a ground lease with an initial term expiring in 2021. After the initial term, the joint venture may extend the ground lease for an additional term of 10 years to 2031.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk includes the risks that arise from changes in interest rates, equity prices and other market changes that affect market sensitive instruments. Our primary market risk exposure is to changes in interest rates on our variable rate debt. As of September 30, 2018, we had approximately $1.6 billion of total variable rate debt outstanding (or 72.3% of total indebtedness) with a weighted-average interest rate of 3.51% per annum. After taking into consideration the effect of interest rate swaps, $268.0 million (or 11.8% of total indebtedness) was subject to variable rates. As of September 30, 2018, if market interest rates on our variable rate debt not subject to interest rate swaps were to increase by 1.00%, or 100 basis points, interest expense would decrease future earnings and cash flows by approximately $2.7 million annually, taking into account our existing contractual hedging arrangements.

Our interest rate risk objectives are to limit the impact of interest rate fluctuations on earnings and cash flows and to lower our overall borrowing costs. To achieve these objectives, we manage our exposure to fluctuations in market interest rates through the use of fixed rate debt instruments to the extent that reasonably favorable rates are obtainable. We have entered into derivative financial instruments such as interest rate swaps to mitigate our interest rate risk or to effectively lock the interest rate on a portion of our variable rate debt. We do not enter into derivative or interest rate transactions for speculative purposes.

The following table provides information about our financial instruments that are sensitive to changes in interest rates. For debt obligations outstanding as of September 30, 2018, the following table presents the principal repayments and related weighted-average interest rates by contractual maturity dates (in thousands):

	2018	2019	2020	2021	2022	Thereafter	Total
Fixed rate debt (1)	$517	$3,215	$3,361	$3,558	$140,386	$475,000	$626,037
Weighted-average interest rate	5.01 %	5.01 %	5.01 %	5.01 %	5.01 %	6.00 %	5.76 %
Variable rate debt (1)	$85,750	$290,250	$—	$485,000	$150,000	$625,000	$1,636,000
Weighted-average interest rate (2)	5.25 %	4.07 %	— %	3.31 %	3.08 %	3.28 %	3.51 %
Total (3)	$86,267	$293,465	$3,361	$488,558	$290,386	$1,100,000	$2,262,037

(1) Excludes $6.3 million and $0.5 million of net deferred financing costs on the Term Loans and mortgage loans, respectively.
(2) The weighted-average interest rate gives effect to interest rate swaps, as applicable.
(3) Excludes a total of $34.9 million related to fair value adjustments on debt.

Our ultimate realized gain or loss with respect to interest rate fluctuations will depend on the exposures that arise during future periods, prevailing interest rates, and our hedging strategies at that time.

Changes in market interest rates on our fixed rate debt impact the fair value of our debt, but such changes have no impact to our consolidated financial statements. As of September 30, 2018, the estimated fair value of our fixed rate debt was $0.7 billion, which is based on having the same debt service requirements that could have been borrowed at the date presented, at prevailing current market interest rates. If interest rates were to rise by 1.00%, or 100 basis points, and our fixed rate debt balance remains constant, we expect the fair value of our debt to decrease by approximately $32.7 million.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

In accordance with Rule 13a-15(b) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), the Company’s management, under the supervision and participation of the Company's Chief Executive Officer and the Chief Financial Officer, has evaluated the effectiveness of the Company’s disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act) as of the end of the period covered by this report. Based on that evaluation, the Company’s Chief Executive Officer and Chief Financial Officer concluded that the Company’s disclosure controls and procedures were effective as of September 30, 2018.

Changes in Internal Control over Financial Reporting

There have been no changes in the Company’s internal control over financial reporting (as defined in Rule 13a-15 and 15d-15 of the Exchange Act) during the period ended September 30, 2018 that have materially affected, or are reasonably likely to materially affect, the Company’s internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The nature of the operations of our hotels exposes our hotel properties, the Company and the Operating Partnership to the risk of claims and litigation in the normal course of their business. Other than routine litigation arising out of the ordinary course of business, the Company is not presently subject to any material litigation nor, to the Company's knowledge, is any material litigation threatened against the Company.

Item 1A. Risk Factors

For a discussion of our potential risks and uncertainties, please refer to the "Risk Factors" section in the Annual Report which is accessible on the SEC's website at www.sec.gov. There have been no material changes to the risk factors previously disclosed in the Annual Report.

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

Unregistered Sales of Equity Securities

The Company did not sell any securities during the quarter ended September 30, 2018 that were not registered under the Securities Act of 1933, as amended (the "Securities Act").

Issuer Purchases of Equity Securities

During the nine months ended September 30, 2018, certain of the Company's employees surrendered common shares owned by them to satisfy their statutory minimum federal and state tax obligations associated with the vesting of restricted common shares of beneficial interest issued under the 2015 Plan.

The following table summarizes all of the share repurchases during the nine months ended September 30, 2018:

Period	Total number of shares purchased	Average price paid per share	Total number of shares purchased as part of publicly announced plans or programs	Maximum number of shares that may yet be purchased under the plans or programs (1)
January 1, 2018 through January 31, 2018	3,453	$ 23.20	—	8,604,348
February 1, 2018 through February 28, 2018	17,578	$ 21.75	—	10,042,025
March 1, 2018 through March 31, 2018	—	$ —	—	10,233,154
April 1, 2018 through April 30, 2018	1,605	$ 20.58	—	9,577,878
May 1, 2018 through May 31, 2018	22,836	$ 22.00	—	8,501,390
June 1, 2018 through June 30, 2018	—	$ —	—	9,021,883
July 1, 2018 through July 31, 2018	1,297	$ 22.57	—	8,806,220
August 1, 2018 through August 31, 2018	85,601	$ 22.17	—	9,079,531
September 1, 2018 through September 30, 2018	—	$ —	—	9,030,073
Total	132,370		—	

(1) The maximum number of shares that may yet be repurchased under the share repurchase program is calculated by dividing the total dollar amount available to repurchase shares by the closing price of our common shares on the last business day of the respective month.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

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Item 6. Exhibits

The exhibits required to be filed by Item 601 of Regulation S-K are noted below:

Exhibit Index

Exhibit Number	Description of Exhibit	
3.1	Articles of Amendment and Restatement of Declaration of Trust of RLJ Lodging Trust (incorporated by reference to Exhibit 3.1 to Amendment No. 4 to the Registrant's Registration Statement on Form S-11 (File. No. 333-172011) filed on May 5, 2011)	
3.2	Articles of Amendment to Articles of Amendment and Restatement of Declaration of Trust of RLJ Lodging Trust (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on May 7, 2015)	
3.3	Articles of Amendment to Articles of Amendment and Restatement of Declaration of Trust of RLJ Lodging Trust (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on May 5, 2016)	
3.4	Articles Supplementary to Articles of Amendment and Restatement of Declaration of Trust (incorporated by reference to Exhibit 3.1 to the Registrant's Current Report on Form 8-K filed on February 26, 2015)	
3.5	Articles Supplementary designating RLJ Lodging Trust's $1.95 Series A Cumulative Convertible Preferred Shares, par value $0.01 per share (incorporated by reference to Exhibit 3.5 to the Registrant's Form 8-A filed on August 30, 2017)	
3.6	Third Amended and Restated Bylaws of RLJ Lodging Trust (incorporated by reference to Exhibit 3.2 to the Registrant's Current Report on Form 8-K filed on May 5, 2016)	
10.1	Employment Agreement, dated as of July 16, 2018, by and among RLJ Lodging Trust, RLJ Lodging Trust, L.P., and Sean Mahoney (incorporated by reference to Exhibit 10.1 to the Registrant's Current Report on Form 8-K filed on July 20, 2018).	
31.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	
31.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	
101.INS	XBRL Instance Document	Submitted electronically with this report
101.SCH	XBRL Taxonomy Extension Schema Document	Submitted electronically with this report
101.CAL	XBRL Taxonomy Calculation Linkbase Document	Submitted electronically with this report
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document	Submitted electronically with this report
101.LAB	XBRL Taxonomy Label Linkbase Document	Submitted electronically with this report
101.PRE	XBRL Taxonomy Presentation Linkbase Document	Submitted electronically with this report

*Filed herewith

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

RLJ LODGING TRUST

Dated: November 7, 2018	/s/ LESLIE D. HALE Leslie D. Hale President and Chief Executive Officer
Dated: November 7, 2018	/s/ SEAN M. MAHONEY Sean M. Mahoney Executive Vice President, Chief Financial Officer and Treasurer (Principal Financial Officer)
Dated: November 7, 2018	/s/ CHRISTOPHER A. GORMSEN Christopher A. Gormsen Chief Accounting Officer (Principal Accounting Officer)