

CHOICE HOTELS INTERNATIONAL INC /DE
Form 10-Q
August 09, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED JUNE 30, 2011

OR

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

COMMISSION FILE NO. 001-13393

CHOICE HOTELS INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

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DELAWARE
(State or other jurisdiction of
incorporation or organization)

52-1209792
(I.R.S. Employer

Identification No.)

10750 COLUMBIA PIKE

SILVER SPRING, MD. 20901

(Address of principal executive offices)

(Zip Code)

(301) 592-5000

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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, and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months. Yes ☒ No ☐

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

Large accelerated filer ☒

Accelerated filer ☐

Non-accelerated filer ☐

Smaller reporting company ☐

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

CLASS
Common Stock, Par Value \$0.01 per share

SHARES OUTSTANDING AT JUNE 30, 2011
59,842,272

CHOICE HOTELS INTERNATIONAL, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION**ITEM 1. FINANCIAL STATEMENTS****CHOICE HOTELS INTERNATIONAL, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF INCOME****(UNAUDITED, IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
REVENUES:				
Royalty fees	\$ 62,301	\$ 57,443	\$ 106,541	\$ 98,464
Initial franchise and relicensing fees	2,585	2,655	5,199	4,567
Procurement services	6,557	6,611	9,722	9,856
Marketing and reservation	90,832	80,389	153,799	139,229
Hotel operations	1,073	1,109	1,937	1,976
Other	1,953	1,641	3,384	3,177
Total revenues	165,301	149,848	280,582	257,269
OPERATING EXPENSES:				
Selling, general and administrative	26,539	22,824	50,386	44,640
Depreciation and amortization	1,948	2,220	3,903	4,392
Marketing and reservation	90,832	80,389	153,799	139,229
Hotel operations	860	808	1,693	1,564
Total operating expenses	120,179	106,241	209,781	189,825
Operating income	45,122	43,607	70,801	67,444
OTHER INCOME AND EXPENSES, NET:				
Interest expense	3,267	675	6,491	1,296
Interest income	(221)	(135)	(431)	(195)
Other (gains) and losses	(38)	1,238	1,005	221
Equity in net income of affiliates	0	(195)	(301)	(548)
Total other income and expenses, net	3,008	1,583	6,764	774
Income before income taxes	42,114	42,024	64,037	66,670
Income taxes	14,536	15,013	20,729	23,866
Net income	27,578	\$ 27,011	43,308	\$ 42,804
Basic earnings per share	\$ 0.46	\$ 0.45	\$ 0.72	\$ 0.72
Diluted earnings per share	\$ 0.46	\$ 0.45	\$ 0.72	\$ 0.72
Cash dividends declared per share	\$ 0.185	\$ 0.185	\$ 0.37	\$ 0.37

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

CHOICE HOTELS INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(UNAUDITED, IN THOUANDS, EXCEPT SHARE AMOUNTS)

	June 30, 2011	December 31, 2010
ASSETS		
Current assets		
Cash and cash equivalents	\$ 90,961	\$ 91,259
Receivables (net of allowance for doubtful accounts of \$9,258 and \$9,159, respectively)	58,044	47,638
Deferred income taxes	429	429
Other current assets	22,030	24,256
Total current assets	171,464	163,582
Property and equipment, at cost, net	53,872	55,662
Goodwill	66,041	66,041
Franchise rights and other identifiable intangibles, net	19,153	20,825
Receivable marketing and reservation fees	60,475	42,507
Investments, employee benefit plans, at fair value	24,972	23,365
Deferred income taxes	24,435	24,435
Other assets	20,893	15,305
Total assets	\$ 441,305	\$ 411,722
LIABILITIES AND SHAREHOLDERS' DEFICIT		
Current liabilities		
Accounts payable	\$ 46,833	\$ 41,168
Accrued expenses	36,919	47,818
Deferred revenue	60,898	67,322
Current portion of long-term debt	516	420
Deferred compensation and retirement plan obligations	2,693	2,552
Revolving credit facility	0	200
Income taxes payable	17,142	5,778
Total current liabilities	165,001	165,258
Long-term debt	251,981	251,554
Deferred compensation and retirement plan obligations	34,969	35,707
Other liabilities	17,296	17,274
Total liabilities	469,247	469,793
Commitments and Contingencies		
SHAREHOLDERS' DEFICIT		
Common stock, \$0.01 par value, 160,000,000 shares authorized; 95,345,362 shares issued at June 30, 2011 and December 31, 2010 and 59,842,272 and 59,583,770 shares outstanding at June 30, 2011 and December 31, 2010, respectively	598	596
Additional paid-in capital	95,083	92,774
Accumulated other comprehensive loss	(5,768)	(7,192)
Treasury stock (35,503,090 and 35,761,592 shares at June 30, 2010 and December 31, 2010, respectively), at cost	(867,249)	(872,306)
Retained earnings	749,394	728,057
Total shareholders' deficit	(27,942)	(58,071)

Total liabilities and shareholders' deficit	\$ 441,305	\$ 411,722
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The accompanying notes are an integral part of these consolidated financial statements.

CHOICE HOTELS INTERNATIONAL, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED, IN THOUSANDS)

	Six Months Ended June 30,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 43,308	\$ 42,804
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,903	4,392
Provision for bad debts	1,340	1,637
Non-cash stock compensation and other charges	7,436	5,297
Non-cash interest and other loss	22	307
Dividends received from equity method investments	159	148
Equity in net income of affiliates	(301)	(548)
Changes in assets and liabilities, net of acquisitions:		
Receivables	(11,058)	(10,061)
Receivable – marketing and reservation fees, net	(11,387)	(17,996)
Accounts payable	6,026	9,043
Accrued expenses	(11,004)	(6,601)
Income taxes payable/receivable	11,404	11,492
Deferred income taxes	40	(55)
Deferred revenue	(6,463)	5,475
Other assets	(750)	(4,307)
Other liabilities	(624)	577
Net cash provided by operating activities	32,051	41,604
CASH FLOWS FROM INVESTING ACTIVITIES:		
Investment in property and equipment	(5,110)	(12,249)
Equity method investments	(1,600)	0
Acquisitions, net of cash acquired	0	(466)
Issuance of notes receivable	(2,651)	(8,008)
Collections of notes receivable	13	37
Purchases of investments, employee benefit plans	(1,139)	(1,204)
Proceeds from sale of investments, employee benefit plans	347	836
Other items, net	(192)	(361)
Net cash used in investing activities	(10,332)	(21,415)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Net borrowings (repayments) pursuant to revolving credit facilities	(200)	13,400
Repayments of long-term debt	(13)	0
Proceeds from the issuance of long-term debt	75	0
Purchase of treasury stock	(2,527)	(9,242)
Dividends paid	(21,922)	(21,924)
Excess tax benefits from stock-based compensation	1,061	12
Debt issuance costs	(2,356)	0
Proceeds from exercise of stock options	3,132	1,315
Net cash used in financing activities	(22,750)	(16,439)

Net change in cash and cash equivalents	(1,031)	3,750
Effect of foreign exchange rate changes on cash and cash equivalents	733	(694)
Cash and cash equivalents at beginning of period	91,259	67,870
 Cash and cash equivalents at end of period	 \$ 90,961	 \$ 70,926
Supplemental disclosure of cash flow information:		
Cash payments during the period for:		
Income taxes, net of refunds	\$ 7,526	\$ 11,921
Interest	\$ 7,678	\$ 1,341
Non-cash investing and financing activities:		
Declaration of dividends	\$ 21,972	\$ 21,934
Capital lease obligation	\$ 430	\$ 0
Issuance of restricted shares of common stock	\$ 8,222	\$ 9,083
Issuance of performance vested restricted stock units	\$ 0	\$ 256
Issuance of treasury stock to employee stock purchase plan	\$ 380	\$ 314

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

CHOICE HOTELS INTERNATIONAL, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. Company Information and Significant Accounting Policies

The accompanying unaudited consolidated financial statements of Choice Hotels International, Inc. and subsidiaries (together the Company) have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). In the opinion of management, all adjustments (which include any normal recurring adjustments) considered necessary for a fair presentation have been included. Certain information and footnote disclosures normally included in financial statements presented in accordance with accounting principles generally accepted in the United States of America (GAAP) have been omitted. The year-end balance sheet information was derived from audited financial statements, but does not include all disclosures required by GAAP. The Company believes the disclosures made are adequate to make the information presented not misleading. The consolidated financial statements should be read in conjunction with the consolidated financial statements for the year ended December 31, 2010 and notes thereto included in the Company's Form 10-K, filed with the SEC on March 1, 2011 (the 10-K). Interim results are not necessarily indicative of the entire year results because of seasonal variations. All intercompany transactions and balances between Choice Hotels International, Inc. and its subsidiaries have been eliminated in consolidation.

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

Certain amounts in the prior year's financial statements have been reclassified to conform to the current year presentation with no effect on previously reported net income or shareholders' deficit.

Cash and Cash Equivalents

The Company considers all highly liquid investments purchased with a maturity of three months or less at the date of purchase to be cash equivalents. As of June 30, 2011 and December 31, 2010, \$3.6 million and \$2.8 million, respectively, of book overdrafts representing outstanding checks in excess of funds on deposit are included in accounts payable in the accompanying consolidated balance sheets.

The Company maintains cash balances in domestic banks, which at times, may exceed the limits of amounts insured by the Federal Deposit Insurance Corporation. In addition, the Company also maintains cash balances in international banks which do not provide deposit insurance.

Recently Adopted Accounting Guidance

In September 2009, the Financial Accounting Standards Board (FASB) ratified Emerging Issues Task Force (EITF) Issue No. 08-1, Revenue Arrangements with Multiple Deliverables (EITF 08-1). EITF 08-1 updates the current guidance pertaining to multiple-element revenue arrangements included in Accounting Standards Codification (ASC) Subtopic 605-25, which originated primarily from EITF 00-21, also titled Revenue Arrangements with Multiple Deliverables. EITF 08-1 was effective for annual reporting periods beginning January 1, 2011 for calendar year entities with earlier adoption permitted. The adoption of these provisions did not have a material impact on our consolidated financial statements.

In July 2010, the FASB issued Accounting Standards Update (ASU) No. 2010-20, which updates the guidance in ASC Topic 310, *Receivables*, related to disclosures about the credit quality of financing receivables and the allowance for credit losses. The new disclosures require disaggregated information related to financing receivables and will include for each class of financing receivables, among other things: a roll forward for the allowance for credit losses, credit quality information, impaired loan information, modification information, non-accrual and past-due information. The disclosures as of the end of a reporting period are effective for interim and annual reporting

periods ending on or after December 15, 2010. Disclosures of reporting period activity (i.e. allowance roll-forward) are required for interim and annual periods beginning after December 15, 2010. The Company has updated its disclosures as appropriate.

Future Adoption of Accounting Standards

In May 2011, the FASB issued ASU No. 2011-04 Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (ASU No. 2011-04). ASU No. 2011-04 generally provides a uniform framework for fair value measurements and related disclosures between GAAP and International Financial Reporting Standards (IFRS). Additional disclosure requirements in the update include: (1) for Level 3 fair value measurements, quantitative information about unobservable inputs used, a description of the valuation processes used by the entity, and a qualitative discussion about the sensitivity of the measurements to changes in the unobservable inputs; (2) for an entity's use of a non-financial asset that is different from the asset's highest and best use, the reason for the difference; (3) for financial instruments not measured at fair value but for which disclosure of fair value is required, the fair value hierarchy level in which the fair value measurements were determined; and (4) the disclosure of all transfers between Level 1 and Level 2 of the fair value hierarchy. ASU 2011-04 will be effective for interim and annual periods beginning on or after December 15, 2011. The Company will update its disclosures as appropriate upon adoption of this standard.

In June 2011, the FASB issued ASU No. 2011-05 Comprehensive Income (Topic 220): Presentation of Comprehensive Income (ASU No. 2011-05). ASU No. 2011-05 amends existing guidance by allowing only two options for presenting the components of net income and other comprehensive income: (1) in a single continuous financial statement, statement of comprehensive income or (2) in two separate but consecutive financial statements, consisting of an income statement followed by a separate statement of other comprehensive income. Also, items that are reclassified from other comprehensive income to net income must be presented on the face of the financial statements. ASU No. 2011-05 requires retrospective application, and it is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, with early adoption permitted. The Company is currently evaluating the financial statement presentation options required by ASU 2011-05.

2. Other Current Assets

Other current assets consist of the following:

	June 30, 2011	December 31, 2010
	(In thousands)	
Land held for sale	\$ 8,112	\$ 11,089
Prepaid expenses	8,420	8,070
Notes receivable (See Note 3)	3,740	3,966
Other current assets	1,758	1,131
Total	\$ 22,030	\$ 24,256

Land held for sale represents the Company's purchase of various parcels of real estate as part of its program to incent franchise development in top markets for certain brands. The Company has acquired this real estate with the intent to resell it to third-party developers for the construction of hotels operated under the Company's brands. During the first quarter of 2011, the Company determined that one parcel of land no longer met the criteria to be classified as a current asset held for sale since it was no longer probable that the parcel would be sold within one year. As a result, the Company reclassified this land to other long-term assets on the Company's consolidated balance sheets at the lower of its carrying amount or fair value. The Company determined that the carrying amount of the land exceeded its estimated fair value by approximately \$1.8 million based on comparable sales. As a result, in the first quarter of 2011, the Company reduced the carrying amount of the land to its estimated fair value and recognized a \$1.8 million loss in other gains and losses in the consolidated statements of income.

Description	June 30, 2011	Fair Value Measurements Using			Total Gains (Losses)
		Quoted Prices in Active Markets for Identical Assets (Level 1)	(\$ in millions) Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Land held for sale ⁽¹⁾	\$ 1.3	0	\$ 1.3	0	\$ (1.8)

(1) Included in Other Assets

3. Notes Receivable and Allowance for Losses

The Company segregates its notes receivable for the purposes of evaluating allowances for credit losses between two categories: *Mezzanine and Other Notes Receivable* and *Forgivable Notes Receivable*. The Company utilizes the level of security it has in the various notes receivable as its primary credit quality indicator (i.e. senior, subordinated or unsecured) when determining the appropriate allowances for uncollectible loans within these categories.

The following table shows the composition of our notes receivable balances:

Credit Quality Indicator	June 30, 2011 (\$ in thousands)			December 31, 2010 (\$ in thousands)		
	Forgivable Notes Receivable	Mezzanine & Other Notes Receivable	Total	Forgivable Notes Receivable	Mezzanine & Other Notes Receivable	Total
Senior	\$ 0	\$ 4,425	\$ 4,425	\$ 0	\$ 3,846	\$ 3,846
Subordinated	0	14,730	14,730	0	14,494	14,494
Unsecured	8,105	0	8,105	7,753	0	7,753
Total notes receivable	8,105	19,155	27,260	7,753	18,340	26,093
Allowance for losses on non-impaired loans	810	225	1,035	775	613	1,388
Allowance for losses on receivables specifically evaluated for impairment	0	9,364	9,364	0	8,638	8,638
Total loan reserves	810	9,589	10,399	775	9,251	10,026
Net carrying value	\$ 7,295	\$ 9,566	\$ 16,861	\$ 6,978	\$ 9,089	\$ 16,067
Current portion, net	\$ 160	\$ 3,580	\$ 3,740	\$ 114	\$ 3,852	\$ 3,966
Long-term portion, net	7,135	5,986	13,121	6,864	5,237	12,101
Total	\$ 7,295	\$ 9,566	\$ 16,861	\$ 6,978	\$ 9,089	\$ 16,067

The Company classifies notes receivable due within one year as other current assets and notes receivable with a maturity greater than one year as other assets in the Company's consolidated balance sheets.

The following table summarizes the activity related to the Company's Forgivable Notes Receivable and Mezzanine and & Other Notes Receivable allowance for losses from December 31, 2010 through June 30, 2011:

	Forgivable Notes Receivable	Mezzanine & Other Notes Receivable
	(In thousands)	
Balance, December 31, 2010	\$ 775	\$ 9,251
Provisions	134	338
Recoveries	2	0
Write-offs	(34)	0
Other ⁽¹⁾	(67)	0
Balance, June 30, 2011	\$ 810	\$ 9,589

(1) Consists of default rate assumption changes

Forgivable Notes Receivable

From time to time, the Company provides financing to franchisees for property improvements and other purposes in the form of forgivable promissory notes. The terms of the notes typically range from 3 to 10 years, bearing market interest rates, and are forgiven and amortized over that time period if the franchisee remains in the system in good standing. The notes are forgivable by the Company and therefore, franchisees are not required to repay the forgivable notes provided that the respective hotels remain in the system and in good standing throughout the term of their note. The Company fully reserves all defaulted notes in addition to recording a reserve on the estimated uncollectible portion of the remaining notes. For those notes not in default, the Company calculates an allowance for losses and determines the ultimate collectability on these forgivable notes based on the historical default rates for those unsecured notes that are not forgiven but are required to be repaid. The Company records bad debt expense in SG&A expenses in the accompanying consolidated statements of income in the quarter when the note is deemed uncollectible.

As of June 30, 2011 and December 31, 2010, the unamortized balance of these notes totaled \$8.1 million and \$7.8 million, respectively. The Company recorded an allowance for credit losses on these forgivable notes receivable of \$0.8 million at both June 30, 2011 and December 31, 2010, respectively. Amortization expense included in the accompanying consolidated statements of income related to the notes was \$0.6 million and \$1.1 million for the three and six months ended June 30, 2011, respectively. Amortization expense for the three and six months ended June 30, 2010 was \$0.5 million and \$1.0 million, respectively. At June 30, 2011, the Company had commitments to extend an additional \$5.7 million in forgivable notes receivable provided certain commitments are met by its franchisees, of which \$2.9 million is expected to be advanced in the next twelve months.

Mezzanine and Other Notes Receivable

The Company has provided financing to franchisees in support of the development of properties in key markets. These notes include non-interest bearing receivables as well as notes bearing market interest and are due upon maturity. Non-interest bearing notes are recorded net of their unamortized discounts. At June 30, 2011 and December 31, 2010, all discounts were fully amortized. Interest income associated with these note receivable is reflected in the accompanying consolidated statements of income under the caption of interest income.

The Company expects the owners to repay the loans in accordance with the loan agreements, or earlier as the hotels mature and capital markets permit. The Company estimates the collectability and records an allowance for loss on its mezzanine and other notes receivable when recording the receivables in the Company's financial statements. These estimates are updated quarterly based on available information.

The Company considers a loan to be impaired when, based on current information and events, it is probable that a creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement. All amounts due according to the contractual terms means that both the contractual interest payments and the contractual principal payments of a loan will be collected as scheduled in the loan agreement. The Company measures loan impairment based on the present value of expected future cash flows discounted at the loan's original effective interest rate or the estimated fair value of the collateral. For impaired loans, the Company establishes a specific impairment reserve for the difference between the recorded investment in the loan and the present value of the expected future cash flows or the estimated fair value of the collateral. The Company applies its loan impairment policy individually to all mezzanine and other notes receivable in the portfolio and does not aggregate loans for the purpose of applying such policy. For impaired loans, the Company recognizes interest income on a cash basis. If it is likely that a loan will not be collected based on financial or other business indicators it is the Company's policy to charge off these loans to SG&A expenses in the accompanying consolidated statements of income in the quarter when it is deemed uncollectible.

The Company assesses the collectability of its senior notes receivable by comparing the market value of the underlying assets to the carrying value of the outstanding notes. In addition, the Company evaluates the property's operating performance, the borrower's compliance with the terms of the loan and franchise agreements, and all related personal guarantees that have been provided by the borrower. For subordinated or unsecured receivables, the Company assesses the property's operating performance, the subordinated equity available to the Company, the borrower's compliance with the terms of loan and franchise agreements, and the related personal guarantees that have been provided by the borrower.

The Company considers loans to be past due and in default when payments are not made when due. Although the Company considers loans to be in default if payments are not received on the due date, the Company does not suspend the accrual of interest until those payments are more than 30 days past due. The Company applies payments received for loans on non-accrual status first to interest and then principal. The Company does not resume interest accrual until all delinquent payments are received.

The Company has determined that approximately \$12.7 million and \$10.8 million of its mezzanine and other notes receivable were impaired at June 30, 2011 and December 31, 2010, respectively. The Company has recorded allowance for credit losses on these impaired loans at June 30, 2011 and December 31, 2010 totaling \$9.4 million and \$8.6 million resulting in a carrying value of impaired loans of \$3.3 million and \$2.2 million, respectively for which we had no related allowance for credit losses. The Company did not recognize interest income during the time that the loans were impaired on either the accrual or cash basis during the periods ended June 30, 2011 and 2010. The Company had provided loan reserves on non-impaired loans totaling \$0.2 million and \$0.6 million at June 30, 2011 and December 31, 2010, respectively. Past due balances of mezzanine and other notes receivable by credit quality indicators are as follows:

	30-89 days Past Due	> 90 days Past Due	Total Past Due (\$ in thousands)	Current	Total Receivables
As of June 30, 2011					
Senior	\$ 0	\$ 0	\$ 0	\$ 4,425	\$ 4,425
Subordinated	0	10,931	10,931	3,799 ⁽¹⁾	14,730
	\$ 0	\$ 10,931	\$ 10,931	\$ 8,224	\$ 19,155
As of December 31, 2010					
Senior	\$ 0	\$ 0	\$ 0	\$ 3,846	\$ 3,846
Subordinated	0	10,931	10,931	3,563	14,494
	\$ 0	\$ 10,931	\$ 10,931	\$ 7,409	\$ 18,340

⁽¹⁾ Amount includes a \$1.9 million note receivable with a maturity date of June 30, 2011. The Company is currently renegotiating the terms of this loan including an extension of the maturity date.

4. Receivable Marketing and Reservation Fees

The marketing fees receivable from cumulative marketing expenses incurred in excess of cumulative marketing fees earned at June 30, 2011 and December 31, 2010 was \$24.5 million and \$17.0 million, respectively. As of June 30, 2011 and December 31, 2010, the reservation fees receivable related to cumulative reservation expenses incurred in excess of cumulative reservation fees earned was \$36.0 million and \$25.5 million, respectively. Depreciation and amortization expense attributable to marketing and reservation activities for the three months ended June 30, 2011 and 2010 was \$3.3 million and \$3.4 million, respectively. Depreciation and amortization expense attributable to marketing and reservation activities for the six months ended June 30, 2011 and 2010 was \$6.5 million and \$6.1 million, respectively. Interest expense attributable to reservation activities was \$1.0 million and \$0.1 million for the three months ended June 30, 2011 and 2010, respectively. Interest expense attributable to reservation activities was \$2.0 million and \$0.2 million for the six months ended June 30, 2011 and 2010, respectively.

The Company evaluates the receivable for marketing and reservation costs in excess of cumulative marketing and reservation system fees earned on a periodic basis for collectability. The Company will record an allowance when, based on current information and events, it is probable that we will be unable to collect all amounts due for marketing and reservation activities according to the contractual terms of the franchise agreements. The receivables are considered to be uncollectible if the expected net, undiscounted cash flows from marketing and reservation activities are less than the carrying amount of the asset.

5. Other Assets

Other assets consist of the following:

	June 30, 2011	December 31, 2010
	(In thousands)	
Notes receivable (see Note 3)	\$ 13,121	\$ 12,101
Deferred financing fees	3,708	2,102
Equity method investments	2,015	251
Other	2,049	851
Total	\$ 20,893	\$ 15,305

6. Deferred Revenue

Deferred revenue consists of the following:

	June 30, 2011	December 31, 2010
	(In thousands)	
Loyalty programs	\$ 55,691	\$ 61,604
Initial, relicensing and franchise fees	3,837	4,631
Procurement service fees	882	1,052
Other	488	35
Total	\$ 60,898	\$ 67,322

7. Debt

Debt consists of the following at:

	June 30, 2011	December 31, 2010
	(In thousands)	
\$250 million senior notes with an effective interest rate of 6.19% at June 30, 2011 and December 31, 2010	\$ 249,412	\$ 249,379
\$350 million senior unsecured revolving credit facility with an effective interest rate of 0.675% at December 31, 2010	0	200
Capital lease obligations due 2016 with an effective interest rate of 4.66% at June 30, 2011 and December 31, 2010	2,968	2,538
Other notes payable	117	57
Total debt	\$ 252,497	\$ 252,174
Less current portion	516	620
Total long-term debt	\$ 251,981	\$ 251,554

On February 24, 2011, the Company entered into a new \$300 million senior unsecured revolving credit agreement (the "Revolver") with Wells Fargo Bank, National Association, as administrative agent and a syndicate of lenders. Simultaneously with the closing of the Revolver, the \$350 million unsecured revolving credit agreement dated as of June 2006 (the "Old Revolver") was terminated. The Revolver provides for a \$300 million unsecured revolving credit facility with a final maturity date on February 24, 2016. Up to \$30 million of borrowings under the Revolver may be used for letters of credit and up to \$20 million of borrowings under the Revolver may be used for swing-line loans.

The Revolver is unconditionally guaranteed, jointly and severally, on a senior unsecured basis by all of the Company's subsidiaries that currently guaranty the obligations under the Company's Indenture governing the terms of its 5.70% senior notes due 2020.

The Company may at any time prior to the final maturity date increase the amount of the Revolver by up to an additional \$150 million to the extent that any one or more lenders commit to being a lender for the additional amount and certain other customary conditions are met.

The Company may elect to have borrowings under the Revolver bear interest at (i) a base rate plus a margin ranging from 5 to 80 basis points based on the Company's credit rating or (ii) LIBOR plus a margin ranging from 105 to 180 basis points based on the Company's credit rating. In addition, the Revolver requires the Company to pay a quarterly facility fee on the full amount of the commitments under the Revolver (regardless of usage) ranging from 20 to 45 basis points based upon the credit rating of the Company.

The Revolver requires that the Company and its restricted subsidiaries comply with various covenants, including with respect to restrictions on liens, incurring indebtedness, making investments and effecting mergers and/or asset sales. In addition, the Revolver imposes financial maintenance covenants requiring the Company to maintain a total leverage ratio of not more than 3.5 to 1.0 and an interest coverage ratio of at least 3.5 to 1.0. The Revolver includes customary events of default, the occurrence of which, following any applicable cure period, would permit the lenders to, among other things, declare the principal, accrued interest and other obligations of the Company under the Revolver to be immediately due and payable. At June 30, 2011, the Company was in compliance with all covenants under the Revolver.

The proceeds of the Revolver are used for general corporate purposes, including working capital, debt repayment, stock repurchases, dividends, investments and other permitted uses. At June 30, 2011, no amounts were outstanding under the Revolver.

Debt issuance costs incurred in connection with the Revolver totaled \$2.4 million and are being amortized, on a straight-line basis, which is not materially different than the effective interest method, through the maturity of the Revolver. Amortization of these costs is included in interest expense in the accompanying statements of income.

On August 25, 2010, the Company completed a \$250 million senior unsecured note offering (the "Senior Notes") at a discount of \$0.6 million, bearing a coupon of 5.7% with an effective rate of 6.19%. The Senior Notes will mature on August 28, 2020, with interest on the Senior Notes to be paid semi-annually on February 28th and August 28th.

The Company used the net proceeds from the offering, after deducting underwriting discounts and other offering expenses, to repay outstanding borrowings under the Old Revolver and other general corporate purposes. The Company's Senior Notes are guaranteed jointly, severally, fully and unconditionally by eight 100%-owned domestic subsidiaries.

8. Pension Plan

The Company sponsors an unfunded non-qualified defined benefit plan (SERP) for certain senior executives. No assets are held with respect to the SERP; therefore benefits are funded as paid to participants. For each of the three months ended June 30, 2011 and 2010, the Company recorded \$0.1 million in expenses related to the SERP which are included in SG&A expense in the accompanying consolidated statements of income. The expenses related to the SERP for each of the six month periods ended June 30, 2011 and 2010 was \$0.3 million. Benefit payments totaling \$0.4 million are currently scheduled to be remitted within the next twelve months.

The following table presents the components of net periodic benefit costs for the three and six months ended June 30, 2011 and 2010:

(In thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Components of net periodic pension cost:				
Interest cost	\$ 136	\$ 134	\$ 271	\$ 269
Net periodic pension cost	\$ 136	\$ 134	\$ 271	\$ 269

The 2011 monthly net periodic pension costs are approximately \$0.5 million. The components of projected pension costs for the year ended December 31, 2011 are as follows:

(in thousands)	
Components of net periodic pension cost:	
Interest cost	\$ 541
Net periodic pension cost	\$ 541

The following is a reconciliation of the changes in the projected benefit obligation for the six months ended June 30, 2011:

(in thousands)	
Projected benefit obligation, December 31, 2010	\$ 10,034
Interest cost	271
Actuarial loss	16
Benefit payments	(207)
Projected benefit obligation, June 30, 2011	\$ 10,114

The amounts in accumulated other comprehensive income (loss) that have not yet been recognized as components of net periodic benefit costs at June 30, 2011 are as follows:

(in thousands)	
Transition asset (obligation)	\$ 0
Prior service cost	0
Accumulated loss	(657)
Total	\$ (657)

9. Non-Qualified Retirement, Savings and Investment Plans

The Company sponsors two non-qualified retirement savings and investment plans for certain employees and senior executives. Employee and Company contributions are maintained in separate irrevocable trusts. Legally, the assets of the trusts remain those of the Company; however, access to the trusts' assets is severely restricted. The trusts cannot be revoked by the Company or an acquirer, but the assets are subject to the claims of the Company's general creditors. The participants do not have the right to assign or transfer contractual rights in the trusts.

In 2002, the Company adopted the Choice Hotels International, Inc. Executive Deferred Compensation Plan (EDCP) which became effective January 1, 2003. Under the EDCP, certain executive officers may defer a portion of their salary into an irrevocable trust. Prior to January 1, 2010, participants could elect an investment return of either the annual yield of the Moody's Average Corporate Bond Rate Yield Index plus 300 basis points, or a return based on a selection of available diversified investment options. Effective January 1, 2010, the Moody's Average Corporate Bond Rate Yield Index plus 300 basis points is no longer an investment option for salary deferrals made on compensation earned after December 31, 2010. As of June 30, 2011 and December 31, 2010, the Company recorded a deferred compensation liability of \$16.5 million and \$17.6 million, respectively related to these deferrals and credited investment returns. Compensation expense is recorded in SG&A expense on the Company's consolidated statements of income based on the change in the deferred compensation obligation related to earnings credited to participants as well as changes in the fair value of diversified investments. Compensation expense recorded in SG&A for the three months ended June 30, 2011 and 2010 were \$0.2 million and \$0.1 million respectively. Compensation expense recorded in SG&A for the six months ended June 30, 2011 and 2010 was \$0.5 million and \$0.3 million, respectively.

The Company has invested the employee salary deferrals in diversified long-term investments which are intended to provide investment returns that partially offset the earnings credited to the participants. The diversified investments held in the trusts totaled \$14.7 million and \$13.6 million as of June 30, 2011 and December 31, 2010, respectively, and are recorded at their fair value, based on quoted market prices. These investments are considered trading securities and therefore the changes in the fair value of the diversified assets is included in other gains and losses in the accompanying statements of income. The Company recorded investment gains (losses) during the three months ended June 30, 2011 and 2010 of approximately \$48 thousand and (\$0.7 million), respectively. The Company recorded investments gains (losses) during the six month ended June 30, 2011 and 2010 totaling \$0.5 million and (\$0.2 million), respectively.

In 1997, the Company adopted the Choice Hotels International, Inc. Non-Qualified Retirement Savings and Investment Plan (Non-Qualified Plan). The Non-Qualified Plan allows certain employees who do not participate in the EDCP to defer a portion of their salary and invest these amounts in a selection of available diversified investment options. As of June 30, 2011 and December 31, 2010, the Company had recorded a deferred compensation liability of \$11.0 million and \$10.6 million, respectively related to these deferrals. Compensation expense is recorded in SG&A expense on the Company's consolidated statements of income based on the change in the deferred compensation obligation related to earnings credited to participants as well as changes in the fair value of diversified investments. The net decrease in compensation expense recorded in SG&A for the three months ended June 30, 2011 and 2010 was \$0.1 million and \$0.7 million, respectively. The net increase in compensation expense recorded in SG&A for the six months ended June 30, 2011 was \$0.2 million while the net decrease in compensation expense for the six months ended June 30, 2010 was \$0.3 million.

The diversified investments held in the trusts were \$10.2 million and \$9.7 million as of June 30, 2011 and December 31, 2010, respectively, and are recorded at their fair value, based on quoted market prices. These investments are considered trading securities and therefore the changes in the fair value of the diversified assets is included in other gains and losses in the accompanying statements of income. The Company recorded investment losses during the three months ended June 30, 2011 and 2010 of approximately \$9 thousand and \$0.6 million, respectively. The Company recorded investment gains during the six months ended June 30, 2011 of \$0.3 million and investment losses of \$0.2 million for the six months ended June 30, 2010. In addition, the Non-Qualified Plan held shares of the Company's common stock with a market value of \$0.8 million and \$0.9 million at June 30, 2011 and December 31, 2010, respectively, which are recorded as a component of shareholders deficit.

10. Fair Value Measurements

The Company estimates the fair value of its financial instruments utilizing a three-tier fair value hierarchy, which prioritizes the inputs used in measuring fair value. There have been no significant transfers into or out of Level 1 or Level 2 inputs during the three and six months ended June 30, 2011. The following summarizes the three levels of inputs, as well as the assets that the Company values using those levels of inputs.

Level 1: Quoted prices in active markets for identical assets and liabilities. The Company's Level 1 assets consist of marketable securities (primarily mutual funds) held in the Company's EDCP and Non-Qualified Plan deferred compensation plans.

Level 2: Observable inputs, other than quoted prices in active markets for identical assets and liabilities, such as quoted prices for similar assets and liabilities; quoted prices in markets that are not active; or other inputs that are observable. The Company's Level 2 assets consist of money market funds held in the Company's EDCP and Non-Qualified Plan deferred compensation plans and those recorded in cash and cash equivalents.

Level 3: Unobservable inputs, supported by little or no market data available, where the reporting entity is required to develop its own assumptions to determine the fair value of the instrument. The Company does not currently have any assets whose fair value was determined using Level 3 inputs.

		Fair Value Measurements at Reporting Date Using		
	Total	Level 1	Level 2	Level 3
Assets (in thousands)				
As of June 30, 2011				
Money market funds, included in cash and cash equivalents	\$ 10,001	\$ 0	\$ 10,001	\$ 0
Mutual funds ⁽¹⁾	22,711	22,711	0	0
Money market funds ⁽¹⁾	2,260	0	2,260	0
	\$ 34,972	\$ 22,711	\$ 12,261	\$ 0
As of December 31, 2010				
Money market funds, included in cash and cash equivalents	\$ 10,001	\$ 0	\$ 10,001	\$ 0
Mutual funds ⁽¹⁾	20,917	20,917	0	0
Money market funds ⁽¹⁾	2,448	0	2,448	0
	\$ 33,366	\$ 20,917	\$ 12,449	\$ 0

(1) Included in Investments, employee benefit plans, fair value on the consolidated balance sheets.

The Company believes that the fair values of its current assets and current liabilities approximate their reported carrying amounts due to the short-term nature of these items. In addition, the interest rates of the Company's Revolver adjust frequently based on current market rates; accordingly its carrying amount approximates fair value.

The Company estimates the fair value of its senior notes, using quoted market prices. At June 30, 2011 and December 31, 2010, the senior notes had an approximate fair value of \$253.2 million and \$244.0 million, respectively.

11. Income Taxes

The effective income tax rate was 34.5% for the three months ended June 30, 2011, compared to an effective income tax rate of 35.7% for the three months ended June 30, 2010. The effective income tax rate was 32.4% for the six months ended June 30, 2011, compared to an effective tax rate of 35.8% for the six months ended June 30, 2010.

The effective income tax rate for the six months ended June 30, 2011 differed from the U.S. federal statutory rate of 35% primarily due to a \$1.4 million adjustment that reduced current federal taxes payable. The Company believes that this adjustment is not material to its financial statements for prior annual or interim periods, the six months ended June 30, 2011 or the Company's expected annual results for the year ended December 31, 2011. The effective income tax rates for the three and six months ended June 30, 2011 were impacted by the effect of foreign operations, partially offset by state income taxes. The effective income tax rates for the three and six months ended June 30, 2010 differed from the U.S. federal statutory rate of 35% primarily due to the effect of foreign operations, partially offset by state income taxes.

12. Share-Based Compensation and Capital Stock

Stock Options

No stock options were granted during the three month period ended June 30, 2011. The Company granted 12,649 options to certain employees of the Company at a fair value of \$0.2 million for the three month period ended June 30, 2010. The Company granted 0.2 million and 0.3 million options to certain employees of the Company at fair value of \$2.1 million and \$2.6 million during the six months ended June 30, 2011 and 2010, respectively. The stock options granted by the Company had an exercise price equal to the market price of the Company's common stock on the date of grant. The fair value of the options granted was estimated on the grant date using the Black-Scholes option-pricing model with the following weighted average assumptions:

	2011 Grants	2010 Grants
Risk-free interest rate	2.10%	2.19%
Expected volatility	39.51%	41.92%
Expected life of stock option	4.4 years	4.4 years
Dividend yield	1.79%	2.26%
Requisite service period	4 years	4 years
Contractual life	7 years	7 years
Weighted average fair value of options granted	\$ 12.42	\$ 10.07

The expected life of the options and volatility are based on historical data and are not necessarily indicative of exercise patterns or actual volatility that may occur. Historical volatility is calculated based on a period that corresponds to the expected life of the stock option. The dividend yield and the risk-free rate of return are calculated on the grant date based on the then current dividend rate and the risk-free rate of return for the period corresponding to the expected life of the stock option. Compensation expense related to the fair value of these awards is recognized straight-line over the requisite service period based on those awards that ultimately vest.

The aggregate intrinsic value of the stock options outstanding and exercisable at June 30, 2011 was \$4.6 million and \$3.2 million, respectively. The total intrinsic value of options exercised during the three months ended June 30, 2011 and 2010 was approximately \$0.6 million and \$0.2 million, respectively. The total intrinsic value of options exercised during the six months ended June 30, 2011 and 2010 was \$2.3 million and \$0.9 million, respectively.

The Company received approximately \$0.9 million and \$0.7 million in proceeds from the exercise of 38,600 and 23,992 employee stock options during the three month periods ended June 30, 2011 and 2010, respectively. The Company received \$3.1 million and \$1.3 million in proceeds from the exercise of approximately 0.1 million of employee stock options during both of the six month periods ended June 30, 2011 and 2010, respectively.

Restricted Stock

The following table is a summary of activity related to restricted stock grants:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Restricted share grants	20,979	24,564	201,624	274,954
Weighted average grant date fair value per share	\$ 36.71	\$ 37.46	\$ 40.78	\$ 33.03
Aggregate grant date fair value (\$000)	\$ 770	\$ 920	\$ 8,222	\$ 9,083
Restricted shares forfeited	21,562	635	27,368	8,829
Vesting service period of shares granted	1-3 years	3-4 years	1-4 years	3-4 years
Grant date fair value of shares vested (\$000)	\$ 1,526	\$ 1,574	\$ 6,357	\$ 5,748

Compensation expense related to the fair value of these awards is recognized straight-line over the requisite service period based on those restricted stock grants that ultimately vest. The fair value of grants is measured by the market price of the Company's stock on the date of grant. Restricted stock awards generally vest ratably over the service period beginning with the first anniversary of the grant date. Awards granted to retirement eligible board of directors are recognized over the shorter of the requisite service period or the length of time until retirement since the terms of the grant provide that the awards will vest upon retirement.

Performance Vested Restricted Stock Units

The Company has granted performance vested restricted stock units (PVRSU) to certain employees. The vesting of these stock awards is contingent upon the Company achieving performance targets at the end of specified performance periods and the employees' continued employment. The performance conditions affect the number of shares that will ultimately vest. The range of possible stock-based award vesting is between 0% and 200% of the initial target. If a minimum of 50% of the performance target is not attained then no awards will vest under the terms of the PVRSU agreements. Compensation expense related to these awards will be recognized over the requisite service period and will only be recognized on those PVRSUs that ultimately vest based on the Company's estimate of the achievement of the various performance targets. The Company has currently estimated that between 0% and 100% of the various award targets will be achieved. The fair value is measured by the market price of the Company's common stock on the date of grant. Compensation expense is recognized ratably over the requisite service period.

The following table is a summary of activity related to PVRSU grants:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Performance vested restricted stock units granted at target	0	0	25,036	33,517
Weighted average grant date fair value per share	\$ 0	\$ 0	\$ 41.25	\$ 32.60
Aggregate grant date fair value (\$000)	\$ 0	\$ 0	\$ 1,033	\$ 1,093
Stock units forfeited	2,442	0	41,512	9,650
Requisite service period	0	0	3 years	3 years

During the three and six months ended June 30, 2011, no PVRSU grants vested. PVRSU grants totaling 39,070 units were forfeited since the Company did not achieve the minimum performance conditions contained in the stock awards. The remaining 2,442 units were forfeited upon employee termination. During the six months ended June 30, 2010, PVRSU grants totaling 10,880 vested at a fair value of \$0.3 million. These PVRSU grants were initially granted at a target of 15,541 units; however, since the Company achieved only 70% of the targeted performance conditions contained in the stock awards granted in prior periods, 4,989 units were forfeited since the performance targets of the applicable PVRSU grant were not achieved.

A summary of stock-based award activity as of June 30, 2011 and changes during the six months ended are presented below:

	Six Months Ended June 30, 2011				Performance Vested	
	Stock Options			Restricted Stock		Restricted Stock Units
	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Shares	Weighted Average Grant Date Fair Value	Weighted Average Grant Date Fair Value
Outstanding at January 1, 2011	1,732,674	\$ 31.43		592,131	\$ 31.81	127,912
Granted	166,306	41.25		201,624	40.78	25,036
Exercised/Vested	(137,536)	22.77		(195,532)	32.51	0
Forfeited/Expired	(120,931)	33.08		(27,368)	33.28	(41,512)
Outstanding at June 30, 2011	1,640,513	\$ 33.03	4.7 years	570,855	\$ 34.67	111,436
Options exercisable at June 30, 2011	981,481	\$ 32.78	4.3 years			

The components of the Company's pretax stock-based compensation expense and associated income tax benefits are as follows for the three and six months ended June 30, 2011 and 2010:

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Stock options	\$ 0.7	\$ 0.6	\$ 1.3	\$ 1.2
Restricted stock	2.0	1.8	3.7	3.5
Performance vested restricted stock units	0.2	0.2	0.3	0.3
Total	\$ 2.9	\$ 2.6	\$ 5.3	\$ 5.0
Income tax benefits	\$ 1.1	\$ 1.0	\$ 2.0	\$ 1.9

Dividends

On May 5, 2011, the Company's board of directors declared a cash dividend of \$0.185 per share (or approximately \$11.0 million in the aggregate), which was paid on July 15, 2011 to shareholders of record as of July 1, 2011. On February 21, 2011, the Company's board of directors declared a cash dividend of \$0.185 per share (or approximately \$11.0 million in the aggregate), which was paid on April 15, 2011 to shareholders of record as of April 1, 2011.

On April 29, 2010, the Company's board of directors declared a cash dividend of \$0.185 per share (or approximately \$11.0 million in the aggregate), which was paid on July 16, 2010 to shareholders of record as of July 2, 2010. On February 16, 2010, the Company's board of directors declared a cash dividend of \$0.185 per share (or approximately \$11.0 million in the aggregate), which was paid on April 16, 2010 to shareholders of record as of April 5, 2010.

Stock Repurchase Program

No shares of common stock were purchased by the Company under the share repurchase program during the three and six month periods ended June 30, 2011. During the three months ended June 30, 2010, the Company did not purchase any shares of common stock under the share repurchase program. During the six months ended June 30, 2010, the Company purchased 0.2 million of shares of common stock under the share repurchase program at a total cost of \$6.9 million.

During the three and six months ended June 30, 2011, the Company redeemed 8,732 and 64,027 shares of common stock at a total cost of approximately \$0.3 million and \$2.5 million, respectively, from employees to satisfy statutory minimum tax requirements from the vesting of restricted stock grants.

During the three and six months ended June 30, 2010, the Company redeemed 8,563 and 73,696 shares of common stock at a total cost of approximately \$0.3 million and \$2.4 million, respectively, from employees to satisfy statutory minimum tax requirements from the vesting of restricted stock and PVRSU grants.

These redemptions were outside the share repurchase program initiated in June 1998.

13. Comprehensive Income

The components of accumulated other comprehensive income (loss) is as follows:

(In thousands)	June 30, 2011	December 31, 2010
Foreign currency translation adjustments	\$ 2,543	\$ 1,540
Deferred loss on cash flow hedge	(7,900)	(8,331)
Changes in pension benefit obligation recognized in other comprehensive income (loss)	(411)	(401)
Total accumulated other comprehensive income (loss)	\$ (5,768)	\$ (7,192)

The differences between net income and comprehensive income are described in the following table:

(In thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Net income	\$ 27,578	\$ 27,011	\$ 43,308	\$ 42,804
Other comprehensive income (loss), net of tax:				
Amortization of loss on cash flow hedge	216	0	431	0
Foreign currency translation adjustment, net	498	(1,189)	1,003	(1,183)
Actuarial pension loss, net of tax	0	0	(10)	0
Other comprehensive income (loss), net of tax	714	(1,189)	1,424	(1,183)
Comprehensive income	\$ 28,292	\$ 25,822	\$ 44,732	\$ 41,621

14. Earnings Per Share

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

(In thousands, except per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2011	2010	2011	2010
Computation of Basic Earnings Per Share:				
Net income	\$ 27,578	\$ 27,011	\$ 43,308	\$ 42,804
Income allocated to participating securities	(274)	(289)	(430)	(442)
Net income available to common shareholders	\$ 27,304	\$ 26,722	\$ 42,878	\$ 42,362
Weighted average common shares outstanding basic	59,243	58,954	59,162	58,939
Basic earnings per share	\$ 0.46	\$ 0.45	\$ 0.72	\$ 0.72
Computation of Diluted Earnings Per Share:				
Net income	\$ 27,578	\$ 27,011	\$ 43,308	\$ 42,804
Income allocated to participating securities	(274)	(289)	(430)	(441)
Net income available to common shareholders	\$ 27,304	\$ 26,722	\$ 42,878	\$ 42,363
Weighted average common shares outstanding basic	59,243	58,954	59,162	58,939
Diluted effect of stock options and PVRsUs	81	84	98	86
Weighted average shares outstanding-diluted	59,324	59,038	59,260	59,025
Diluted earnings per share	\$ 0.46	\$ 0.45	\$ 0.72	\$ 0.72

The Company's unvested restricted shares contain rights to receive non-forfeitable dividends, and thus are participating securities requiring the two-class method of computing earnings per share (EPS). The calculation of EPS for common stock shown above excludes the income attributable to the unvested restricted share awards from the numerator and excludes the dilutive impact of those awards from the denominator.

At June 30, 2011 and 2010, the Company had 1.6 million and 1.8 million outstanding stock options, respectively. Stock options are included in the diluted earnings per share calculation using the treasury stock method and average market prices during the period, unless the stock options would be anti-dilutive. For both the three and six month periods ended June 30, 2011, the Company excluded 0.4 million of anti-dilutive stock options from the diluted earnings per share calculation, respectively. For both the three and six months ended June 30, 2010, the Company excluded 0.6 million of anti-dilutive stock options from the diluted earnings per share calculation.

PVRsUs are also included in the diluted earnings per share calculation assuming the performance conditions have been met at the reporting date. However, at June 30, 2011 and 2010, PVRsUs totaling 111,436 and 131,372, respectively were excluded from the computation since the performance conditions had not been met.

15. Condensed Consolidating Financial Statements

Effective August 2010, the Company's Senior Notes are guaranteed jointly, severally, fully and unconditionally by eight 100%-owned domestic subsidiaries. There are no legal or regulatory restrictions on the payment of dividends to Choice Hotels International, Inc. from subsidiaries that do not guarantee the Senior Notes. As a result of the guarantee arrangements, the following condensed consolidating financial statements are presented. Investments in subsidiaries are accounted for under the equity method of accounting.

Choice Hotels International, Inc.
Condensed Consolidating Statement of Income
For the Three Months Ended June 30, 2011
(Unaudited, in Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES:					
Royalty fees	\$ 55,170	\$ 26,711	\$ 9,206	\$ (28,786)	\$ 62,301
Initial franchise and relicensing fees	2,573	0	12	0	2,585
Procurement services	6,557	0	0	0	6,557
Marketing and reservation	78,514	87,289	4,588	(79,559)	90,832
Other items, net	1,793	1,073	160	0	3,026
Total revenues	144,607	115,073	13,966	(108,345)	165,301
OPERATING EXPENSES:					
Selling, general and administrative	28,476	22,915	3,934	(28,786)	26,539
Marketing and reservation	81,244	84,675	4,472	(79,559)	90,832
Other items, net	706	1,879	223	0	2,808
Total operating expenses	110,426	109,469	8,629	(108,345)	120,179
Operating income	34,181	5,604	5,337	0	45,122
OTHER INCOME AND EXPENSES, NET:					
Interest expense	4,230	(965)	2	0	3,267
Equity in earnings of consolidated subsidiaries	(8,797)	0	0	8,797	0
Other items, net	(207)	(39)	(13)	0	(259)
Total other income and expenses, net	(4,774)	(1,004)	(11)	8,797	3,008
Income before income taxes	38,955	6,608	5,348	(8,797)	42,114
Income taxes	11,377	2,759	400	0	14,536
Net income	\$ 27,578	\$ 3,849	\$ 4,948	\$ (8,797)	\$ 27,578

Choice Hotels International, Inc.
Condensed Consolidating Statement of Income
For the Three Months Ended June 30, 2010
(Unaudited, in Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES:					
Royalty fees	\$ 51,486	\$ 22,571	\$ 7,231	\$ (23,845)	\$ 57,443
Initial franchise and relicensing fees	2,655	0	0	0	2,655
Procurement services	6,611	0	0	0	6,611
Marketing and reservation	71,045	82,216	3,721	(76,593)	80,389
Other items, net	1,614	1,109	27	0	2,750
Total revenues	133,411	105,896	10,979	(100,438)	149,848
OPERATING EXPENSES:					
Selling, general and administrative	23,473	19,642	3,554	(23,845)	22,824
Marketing and reservation	74,387	79,347	3,248	(76,593)	80,389
Other items, net	984	1,846	198	0	3,028
Total operating expenses	98,844	100,835	7,000	(100,438)	106,241
Operating income	34,567	5,061	3,979	0	43,607
OTHER INCOME AND EXPENSES, NET:					
Interest expense	759	(85)	1	0	675
Equity in earnings of consolidated subsidiaries	(5,573)	0	0	5,573	0
Other items, net	(120)	1,238	(210)	0	908
Total other income and expenses, net	(4,934)	1,153	(209)	5,573	1,583
Income before income taxes	39,501	3,908	4,188	(5,573)	42,024
Income taxes	12,490	2,054	469	0	15,013
Net income	\$ 27,011	\$ 1,854	\$ 3,719	\$ (5,573)	\$ 27,011

Choice Hotels International, Inc.

Condensed Consolidating Statement of Income

For the Six Months Ended June 30, 2011

(Unaudited, in Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES:					
Royalty fees	\$ 93,671	\$ 53,818	\$ 15,873	\$ (56,821)	\$ 106,541
Initial franchise and relicensing fees	5,187	0	12	0	5,199
Procurement services	9,722	0	0	0	9,722
Marketing and reservation	128,685	156,083	8,489	(139,458)	153,799
Other items, net	3,040	1,937	344	0	5,321
Total revenues	240,305	211,838	24,718	(196,279)	280,582
OPERATING EXPENSES:					
Selling, general and administrative	52,079	46,786	8,342	(56,821)	50,386
Marketing and reservation	134,016	150,730	8,511	(139,458)	153,799
Other items, net	1,414	3,743	439	0	5,596
Total operating expenses	187,509	201,259	17,292	(196,279)	209,781
Operating income	52,796	10,579	7,426	0	70,801
OTHER INCOME AND EXPENSES, NET:					
Interest expense	8,403	(1,916)	4	0	6,491
Equity in earnings of consolidated subsidiaries	(13,870)	0	0	13,870	0
Other items, net	(405)	(762)	1,440	0	273
Total other income and expenses, net	(5,872)	(2,678)	1,444	13,870	6,764
Income before income taxes	58,668	13,257	5,982	(13,870)	64,037
Income taxes	15,360	5,293	76	0	20,729
Net income	\$ 43,308	\$ 7,964	\$ 5,906	\$ (13,870)	\$ 43,308

Choice Hotels International, Inc.

Condensed Consolidating Statement of Income

For the Six Months Ended June 30, 2010

(Unaudited, in Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
REVENUES:					
Royalty fees	\$ 87,338	\$ 46,869	\$ 13,630	\$ (49,373)	\$ 98,464
Initial franchise and relicensing fees	4,567	0	0	0	4,567
Procurement services	9,856	0	0	0	9,856
Marketing and reservation	119,025	147,339	7,168	(134,303)	139,229
Other items, net	3,038	1,976	139	0	5,153
Total revenues	223,824	196,184	20,937	(183,676)	257,269
OPERATING EXPENSES:					
Selling, general and administrative	45,207	41,497	7,309	(49,373)	44,640
Marketing and reservation	124,590	142,053	6,889	(134,303)	139,229
Other items, net	1,968	3,591	397	0	5,956
Total operating expenses	171,765	187,141	14,595	(183,676)	189,825
Operating income	52,059	9,043	6,342	0	67,444
OTHER INCOME AND EXPENSES, NET:					
Interest expense	1,463	(169)	2	0	1,296
Equity earnings of consolidated subsidiaries	(10,962)	0	0	10,962	0
Other items, net	(181)	449	(790)	0	(522)
Total other income and expenses, net	(9,680)	280	(788)	10,962	774
Income before income taxes	61,739	8,763	7,130	(10,962)	66,670
Income taxes	18,935	4,105	826	0	23,866
Net income	\$ 42,804	\$ 4,658	\$ 6,304	\$ (10,962)	\$ 42,804

Choice Hotels International, Inc.

Condensed Consolidating Balance Sheet

As of June 30, 2011

(Unaudited, in thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Cash and cash equivalents	\$ 10,243	\$ 372	\$ 80,346	0	\$ 90,961
Receivables	50,176	1,720	6,148	0	58,044
Other current assets	5,623	15,627	3,587	(2,378)	22,459
Total current assets	66,042	17,719	90,081	(2,378)	171,464
Property and equipment, at cost, net	10,430	42,070	1,372	0	53,872
Goodwill	60,620	5,193	228	0	66,041
Franchise rights and other identifiable intangibles, net	12,118	3,643	3,392	0	19,153
Receivable marketing and reservation fees	60,475	0	0	0	60,475
Investment in and advances to affiliates	273,975	212,140	6,217	(492,332)	0
Investments, employee benefit plans, at fair value	0	24,972	0	0	24,972
Deferred income taxes	4,617	19,751	67	0	24,435
Other assets	9,694	7,556	3,643	0	20,893
Total assets	\$ 497,971	\$ 333,044	\$ 105,000	\$ (494,710)	\$ 441,305
LIABILITIES AND SHAREHOLDERS DEFICIT					
Accounts payable	\$ 7,080	\$ 34,946	\$ 4,807	\$ 0	\$ 46,833
Accrued expenses	17,889	17,347	1,683	0	36,919
Deferred revenue	5,565	54,329	1,004	0	60,898
Current portion of long-term debt	0	494	22	0	516
Income taxes payable	17,758	0	1,108	(1,724)	17,142
Other current liabilities	0	3,347	0	(654)	2,693
Total current liabilities	48,292	110,463	8,624	(2,378)	165,001
Long-term debt	249,411	2,476	94	0	251,981
Deferred compensation & retirement plan obligations	0	34,963	6	0	34,969
Advances from affiliates	218,902	483	13,951	(233,336)	0
Other liabilities	9,308	7,943	45	0	17,296
Total liabilities	525,913	156,328	22,720	(235,714)	469,247
Total shareholders (deficit) equity	(27,942)	176,716	82,280	(258,996)	(27,942)
Total liabilities and shareholders deficit	\$ 497,971	\$ 333,044	\$ 105,000	\$ (494,710)	\$ 441,305

Choice Hotels International, Inc.

Condensed Consolidating Balance Sheet

As of December 31, 2010

(In Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Cash and cash equivalents	\$ 4,849	\$ 18,659	\$ 67,751	\$ 0	\$ 91,259
Receivables	40,160	2,055	5,423	0	47,638
Other current assets	5,193	19,616	6,444	(6,568)	24,685
Total current assets	50,202	40,330	79,618	(6,568)	163,582
Property and equipment, at cost, net	11,586	42,678	1,398	0	55,662
Goodwill	60,620	5,193	228	0	66,041
Franchise rights and other identifiable intangibles, net	13,315	3,953	3,557	0	20,825
Receivable, marketing and reservation fees	42,507	0	0	0	42,507
Investments, employee benefit plans, at fair value	0	23,365	0	0	23,365
Investment in and advances to affiliates	251,245	186,045	7,338	(444,628)	0
Deferred income taxes	4,560	19,745	130	0	24,435
Other assets	7,339	7,366	600	0	15,305
Total assets	\$ 441,374	\$ 328,675	\$ 92,869	\$ (451,196)	\$ 411,722
LIABILITIES AND SHAREHOLDERS DEFICIT					
Accounts payable	\$ 5,700	\$ 31,475	\$ 3,993	0	\$ 41,168
Accrued expenses	19,257	26,890	1,671	0	47,818
Deferred revenue	14,070	52,256	996	0	67,322
Current portion of long-term debt	0	403	17	0	420
Other current liabilities	0	3,206	0	(654)	2,552
Revolving credit facility	200	0	0	0	200
Income taxes payable	9,395	0	2,297	(5,914)	5,778
Total current liabilities	48,622	114,230	8,974	(6,568)	165,258
Long-term debt	249,379	2,137	38	0	251,554
Deferred compensation & retirement plan obligations	0	35,707	0	0	35,707
Advances from affiliates	192,077	1,097	10,137	(203,311)	0
Other liabilities	9,367	7,880	27	0	17,274
Total liabilities	499,445	161,051	19,176	(209,879)	469,793
Total shareholders (deficit) equity	(58,071)	167,624	73,693	(241,317)	(58,071)
Total liabilities and shareholders deficit	\$ 441,374	\$ 328,675	\$ 92,869	\$ (451,196)	\$ 411,722

Choice Hotels International, Inc.
Condensed Consolidating Statement of Cash Flows
For the Six Months ended June 30, 2011
(Unaudited, in thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net cash provided (used) from operating activities	\$ 31,484	\$ (12,986)	\$ 13,553	0	\$ 32,051
CASH FLOWS FROM INVESTING ACTIVITIES:					
Investment in property and equipment	(1,407)	(3,520)	(183)	0	(5,110)
Equity method investments	0	0	(1,600)	0	(1,600)
Issuance of notes receivable	(631)	(2,020)	0	0	(2,651)
Collection of notes receivable	0	13	0	0	13
Purchases of investments, employee benefit plans	0	(1,139)	0	0	(1,139)
Proceeds from the sales of investments, employee benefit plans	0	347	0	0	347
Other items, net	(217)	(5)	30	0	(192)
Net cash used in investing activities	(2,255)	(6,324)	(1,753)	0	(10,332)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Net repayments pursuant to revolving credit facilities	(200)	0	0	0	(200)
Repayments of long-term debt	0	0	(13)	0	(13)
Proceeds from the issuance of long-term debt	0	0	75	0	75
Purchase of treasury stock	(2,527)	0	0	0	(2,527)
Debt issuance costs	(2,356)	0	0	0	(2,356)
Excess tax benefits from stock-based compensation	38	1,023	0	0	1,061
Dividends paid	(21,922)	0	0	0	(21,922)
Proceeds from exercise of stock options	3,132	0	0	0	3,132
Net cash provided (used) in financing activities	(23,835)	1,023	62	0	(22,750)
Net change in cash and cash equivalents	5,394	(18,287)	11,862	0	(1,031)
Effect of foreign exchange rate changes on cash and cash equivalents	0	0	733	0	733
Cash and cash equivalents at beginning of period	4,849	18,659	67,751	0	91,259
Cash and cash equivalents at end of period	\$ 10,243	\$ 372	\$ 80,346	\$ 0	\$ 90,961

Choice Hotels International, Inc.
Condensed Consolidating Statement of Cash Flows
For the Six Months Ended June 30, 2010
(Unaudited, in Thousands)

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Net cash provided from operating activities	\$ 26,531	\$ 10,466	\$ 4,607	0	\$ 41,604
CASH FLOWS FROM INVESTING ACTIVITIES:					
Investment in property and equipment	(2,867)	(9,195)	(187)	0	(12,249)
Acquisitions, net of cash acquired	0	0	(466)	0	(466)
Issuance of notes receivable	(7,228)	(780)	0	0	(8,008)
Collection of notes receivable	0	37	0	0	37
Purchases of investments, employee benefit plans	0	(1,204)	0	0	(1,204)
Proceeds from the sales of investments, employee benefit plans	0	836	0	0	836
Other items, net	(173)	(33)	(155)	0	(361)
Net cash used in investing activities	(10,268)	(10,339)	(808)	0	(21,415)
CASH FLOWS FROM FINANCING ACTIVITIES:					
Net borrowings pursuant to revolving credit facility	13,400	0	0	0	13,400
Purchase of treasury stock	(9,242)	0	0	0	(9,242)
Excess tax benefits from stock-based compensation	0	12	0	0	12
Dividends paid	(21,924)	0	0	0	(21,924)
Proceeds from exercise of stock options	1,315	0	0	0	1,315
Net cash (used in) provided by financing activities	(16,451)	12	0	0	(16,439)
Net change in cash and cash equivalents	(188)	139	3,799	0	3,750
Effect of foreign exchange rate changes on cash and cash equivalents	0	0	(694)	0	(694)
Cash and cash equivalents at beginning of period	4,281	303	63,286	0	67,870
Cash and cash equivalents at end of period	\$ 4,093	\$ 442	\$ 66,391	0	\$ 70,926

16. Reportable Segment Information

The Company has a single reportable segment encompassing its franchising business. Revenues from the franchising business include royalty fees, initial franchise and relicensing fees, marketing and reservation system fees, procurement services revenue and other revenue. The Company is obligated under its franchise agreements to provide marketing and reservation services appropriate for the operation of its systems. These services do not represent separate reportable segments as their operations are directly related to the Company's franchising business. The revenues received from franchisees that are used to pay for part of the Company's ongoing operations are included in franchising revenues and are offset by the related expenses paid for marketing and reservation activities to calculate franchising operating income. Corporate and other revenue consists of hotel operations. Except as described in Note 4, the Company does not allocate interest income, interest expense or income taxes to its franchising segment.

The following table presents the financial information for the Company's franchising segment:

(In thousands)	Three Months Ended June 30, 2011			Three Months Ended June 30, 2010		
	Corporate			Corporate		
	&			&		
	Franchising	Other	Consolidated	Franchising	Other	Consolidated
Revenues	\$ 164,228	\$ 1,073	\$ 165,301	\$ 148,739	\$ 1,109	\$ 149,848
Operating income (loss)	\$ 57,360	\$ (12,238)	\$ 45,122	\$ 52,564	\$ (8,957)	\$ 43,607
Income (loss) before income taxes	\$ 57,360	\$ (15,246)	\$ 42,114	\$ 52,759	\$ (10,735)	\$ 42,024

(In thousands)	Six Months Ended June 30, 2011			Six Months Ended June 30, 2010		
	Corporate			Corporate		
	&			&		
	Franchising	Other	Consolidated	Franchising	Other	Consolidated
Revenues	\$ 278,645	\$ 1,937	\$ 280,582	\$ 255,293	\$ 1,976	\$ 257,269
Operating income (loss)	\$ 93,437	\$ (22,636)	\$ 70,801	\$ 85,632	\$ (18,188)	\$ 67,444
Income (loss) before income taxes	\$ 91,971	\$ (27,934)	\$ 64,037	\$ 86,180	\$ (19,510)	\$ 66,670

17. Commitments and Contingencies

The Company is a defendant in a number of lawsuits arising in the ordinary course of business. In the opinion of management and the Company's legal counsel, the ultimate outcome of any such lawsuit individually will not have a material adverse effect on the Company's business, financial position, results of operations or cash flows.

In June 2008, the Company guaranteed \$1 million of a bank loan funding a franchisee's construction of a Cambria Suites in Columbus, Ohio. The guaranty will terminate on the earlier of (i) the repayment of all outstanding obligations under the bank loan that it supports (the current initial loan term runs through June 2013), or (ii) when the franchisee achieves certain debt service coverage ratios outlined in the underlying bank loan agreement. The Company has received a pledge of an equity interest in the entity constructing the property as well as personal guarantees from several of the franchisee's principal owners related to the repayment of any amounts the Company may be required to pay under this guaranty.

In July 2008, the Company guaranteed \$1 million of a bank loan funding a franchisee's construction of a Cambria Suites in Noblesville, Indiana. The guaranty will terminate on the earlier of (i) the repayment of all outstanding obligations under the bank loan that it supports (the current initial loan term runs through September 2011), or (ii) when the franchisee achieves certain debt service coverage ratios outlined in the underlying bank loan

agreement. The Company has received a pledge of an equity interest in the entity constructing the property as well as personal guarantees from several of the franchisee's principal owners related to the repayment of any amounts the Company may be required to pay under this guaranty.

The Company occasionally provides financing to franchisees for property improvements, hotel development efforts and other purposes. At June 30, 2011, the Company had commitments to extend an additional \$5.7 million for these purposes provided certain conditions are met by its franchisees, of which \$2.9 million is expected to be advanced in the next twelve months.

The Company has made commitments to purchase various parcels of real estate to support the development of its brands which include non-refundable deposits. Providing certain conditions are met by the seller, the Company expects to acquire these parcels of land for a total price of approximately \$3.5 million during the year ended December 31, 2011.

The Company has invested \$1.6 million in a joint venture and has a commitment to invest an additional \$3.4 million which is expected to be funded completely in 2011.

In the ordinary course of business, the Company enters into numerous agreements that contain standard indemnities whereby the Company indemnifies another party for breaches of representations and warranties. Such indemnifications are granted under various agreements, including those governing (i) purchases or sales of assets or businesses, (ii) leases of real estate, (iii) licensing of trademarks, (iv) access to credit facilities, (v) issuances of debt or equity securities, and (vi) certain operating agreements. The indemnifications issued are for the benefit of the (i) buyers in sale agreements and sellers in purchase agreements, (ii) landlords in lease contracts, (iii) franchisees in licensing agreements, (iv) financial institutions in credit facility arrangements, (v) underwriters in debt or equity security issuances and (vi) parties under certain operating agreements. In addition, these parties are also generally indemnified against any third party claim resulting from the transaction that is contemplated in the underlying agreement. While some of these indemnities extend only for the duration of the underlying agreement, many survive the expiration of the term of the agreement or extend into perpetuity (unless subject to a legal statute of limitations). There are no specific limitations on the maximum potential amount of future payments that the Company could be required to make under these indemnities, nor is the Company able to develop an estimate of the maximum potential amount of future payments to be made under these indemnifications as the triggering events are not subject to predictability. With respect to certain of the aforementioned indemnities, such as indemnifications of landlords against third party claims for the use of real estate property leased by the Company, the Company maintains insurance coverage that mitigates potential liability.

18. Termination Charges

During the six months ended June 30, 2011, the Company recorded one-time employee termination charges totaling \$0.9 million in SG&A and marketing and reservation expenses. These charges related to salary and benefits continuation payments for employees separating from service with the Company. At June 30, 2011, the Company had approximately \$0.6 million of these salary and benefits continuation payments remaining to be remitted. During the six months ended June 30, 2011, the Company remitted \$2.7 million of termination benefits related to employee termination charges recorded in prior periods and had approximately \$1.4 million of these benefits remaining to be paid.

At June 30, 2011 and December 31, 2010, approximately \$2.0 million and \$4.0 million of termination benefits remained and were included in current and non-current liabilities in the Company's consolidated financial statements. The Company expects \$1.7 million of benefits to be paid in the next twelve months.

19. Subsequent Events

On July 11, 2011, Choice Hotels International Services Corp., a wholly-owned subsidiary of the Company, as tenant, and F.P. Rockville II Limited Partnership (the "Landlord"), as landlord, executed an Office Lease (the "Lease") for office space to which the Company intends to relocate its corporate headquarters. The obligations of the tenant under the Lease have been guaranteed by the Company. The relocation is expected to occur upon construction of an office building, completion of other improvements to the property and building, and satisfaction of other conditions and contingencies set forth in the Lease, including significant conditions related to the scope and timing of the construction, development and permitting of the office building.

The target commencement date for the Lease, which is the date on which the Company will take occupancy of its leased premises for purposes of commencing an interior fit-out of the premises, is December 1, 2012. The target rent commencement date for the Lease, which is the date on which the Company will begin to make rental payments to the Landlord under the Lease, is June 1, 2013. The Lease runs for an initial term of 10 years from the rent commencement date. The leased premises will consist of approximately 138,000 square feet of office space in a to-be constructed office building located in Rockville, Maryland (the Building). The Company has an option to extend the Lease beyond the initial term for up to 15 years at then-current fair market rent.

No rent is due under the Lease until the rent commencement date, which is currently targeted to occur on or about June 1, 2013. Thereafter, the annual rent is established at a specific minimum amount and is re-set to a new minimum amount each year. Subject to one or more applicable adjustments set forth in the Lease, the Company's minimum annual rent amount, without set-off, deduction for improvement allowances or abatement of any kind, during the initial term ranges from approximately \$5.5 million during the initial year to approximately \$7.6 million during the final year. During the initial 10-year term of the Lease, the minimum expected rent payments by the Company are expected to be approximately \$67 million. In addition, beginning on or about the first anniversary of the rent commencement date, the Company is obligated to pay its proportionate share of increases in the cost of operating, managing and maintaining the Building.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis (MD&A) is intended to help the reader understand Choice Hotels International, Inc. and subsidiaries (together the Company). MD&A is provided as a supplement to-and should be read in conjunction with-our consolidated financial statements and the accompanying notes.

Overview

We are a hotel franchisor with franchise agreements representing 6,117 hotels open and 554 hotels under construction, awaiting conversion or approved for development as of June 30, 2011, with 491,366 rooms and 46,612 rooms, respectively, in 49 states, the District of Columbia and over 40 countries and territories outside the United States. Our brand names include Comfort Inn®, Comfort Suites®, Quality®, Clarion®, Ascend Collection®, Sleep Inn®, Econo Lodge®, Rodeway Inn®, MainStay Suites®, Suburban Extended Stay Hotel®, and Cambria Suites® (collectively, the Choice brands).

The Company conducts its international franchise operations through a combination of direct franchising and master franchising relationships. Master franchising relationships allow the use of our brands by third parties in foreign countries. These relationships are governed by master franchising agreements which generally provide the master franchise with the right to use our brands in a specific geographic region, usually for a fee. As a result of our use of master franchising relationships and international market conditions, total revenues from international franchising operations comprised only 8% and 9% of our total revenues for the three and six months ended June 30, 2011, respectively, while representing approximately 19% of hotels open at June 30, 2011.

Our Company generates revenues and cash flows primarily from initial, relicensing and continuing royalty fees attributable to our franchise agreements. Revenues are also generated from qualified vendor arrangements, hotel operations and other sources. The hotel industry is seasonal in nature. For most hotels, demand is lower in December through March than during the remainder of the year. Our principal source of revenues is franchise fees based on the gross room revenues of our franchised properties. The Company's franchise fee revenues and operating income reflect the industry's seasonality and historically have been lower in the first quarter than in the second, third or fourth quarters.

With a focus on hotel franchising instead of ownership, we benefit from the economies of scale inherent in the franchising business. The fee and cost structure of our business provides opportunities to improve operating results by increasing the number of franchised hotel rooms and effective royalty rates of our franchise contracts resulting in increased initial fee and relicensing revenue, ongoing royalty fees and procurement services revenues. In addition,

our operating results can also be improved through our company-wide efforts related to improving property level performance. The Company currently estimates that based on its current domestic portfolio of hotels under franchise that a 1% change in revenue per available room (RevPAR) or rooms under franchise would increase or decrease annual domestic royalty revenues by approximately \$2.2 million and a 1 basis point change in the Company's effective royalty rate would increase or decrease annual domestic royalties by approximately \$0.5 million. In addition to these revenues, we also collect marketing and reservation system fees to support centralized marketing and reservation activities for the franchise system. As a lodging franchisor, the Company currently has relatively low capital expenditure requirements.

The principal factors that affect the Company's results are: the number and relative mix of franchised hotel rooms; growth in the number of hotel rooms under franchise; occupancy and room rates achieved by the hotels under franchise; the effective royalty rate achieved; the level of franchise sales and relicensing activity; and our ability to manage costs. The number of rooms at franchised properties and occupancy and room rates at those properties significantly affect the Company's results because our fees are based upon room revenues at franchised hotels. The key industry standard for measuring hotel-operating performance is RevPAR, which is calculated by multiplying the percentage of occupied rooms by the average daily room rate realized. Our variable overhead costs associated with franchise system growth have historically been less than incremental royalty fees generated from new franchises. Accordingly, continued growth of our franchise business should enable us to realize benefits from the operating leverage in place and improve operating results.

We are contractually required by our franchise agreements to use the marketing and reservation system fees we collect for system-wide marketing and reservation activities. These expenditures, which include advertising costs and costs to maintain our central reservations system, help to enhance awareness and increase consumer preference for our brands. Greater awareness and preference promotes long-term growth in business delivery to our franchisees, which ultimately increases franchise fees earned by the Company.

Our Company articulates its mission as a commitment to our franchisees' profitability by providing them with hotel franchises that strive to generate the highest return on investment of any hotel franchise. We have developed an operating system dedicated to our franchisees' success that focuses on delivering guests to our franchised hotels and reducing costs for our hotel owners.

We believe that executing our strategic priorities creates value for our shareholders. Our Company focuses on two key value drivers:

Profitable Growth. We believe our success is dependent on improving the performance of our hotels, increasing our system size by selling additional hotel franchises, effective royalty rate improvement and maintaining a disciplined cost structure. We attempt to improve our franchisees' revenues and overall profitability by providing a variety of products and services designed to increase business delivery to and/or reduce operating and development costs for our franchisees. These products and services include national marketing campaigns, a central reservation system, property and yield management systems, quality assurance standards and qualified vendor relationships. We believe that healthy brands, which deliver a compelling return on investment for franchisees, will enable us to sell additional hotel franchises and raise royalty rates. We have established multiple brands that meet the needs of many types of guests, and can be developed at various price points and applied to both new and existing hotels. This ensures that we have brands suitable for creating growth in a variety of market conditions. Improving the performance of the hotels under franchise, growing the system through additional franchise sales and improving franchise agreement pricing while maintaining a disciplined cost structure are the keys to profitable growth.

Maximizing Financial Returns and Creating Value for Shareholders. Our capital allocation decisions, including capital structure and uses of capital, are intended to maximize our return on invested capital and create value for our shareholders. We believe our strong and predictable cash flows create a strong financial position that provides us a competitive advantage. Currently, our business does not require significant capital to operate and grow. Therefore, we can maintain a capital structure that generates high financial returns and use our excess cash flow to increase returns to our shareholders.

Historically, we have returned value to our shareholders in two primary ways: share repurchases and dividends. In 1998, we instituted a share repurchase program which has generated substantial value for our shareholders. During the six months ended June 30, 2011, the Company repurchased no shares of its common stock under the share repurchase program. Since the program's inception through June 30, 2011, we have repurchased 43.2 million shares (including 33.0 million prior to the two-for-one stock split effected in October 2005) of common stock at a total cost of \$1.0 billion. Considering the effect of the two-for-one stock split, the Company has repurchased 76.2 million shares at an average price of \$13.35 per share. We currently believe that our cash flows from operations will support our ability to complete the current board of directors repurchase authorization of approximately 3.6 million shares remaining as of June 30, 2011. Upon completion of the current authorization, our board of directors will evaluate the advisability of additional share repurchases.

During the six months ended June 30, 2011, we paid cash dividends totaling approximately \$21.9 million and we presently expect to continue to pay dividends in the future, subject to future business performance, economic conditions, changes in income tax regulations and other factors. Based on our present dividend rate and outstanding share count, aggregate annual dividends for 2011 would be approximately \$44.0 million.

Our board of directors previously authorized us to enter into programs which permit us to offer investment, financing and guaranty support to qualified franchisees as well as to acquire and resell real estate to incent franchise development for certain brands in top markets. Recent market conditions have resulted in an increase in opportunities to incentivize development under these programs.

Over the next several years, we expect to deploy capital opportunistically pursuant to these programs to promote growth of our emerging brands. The amount and timing of the investment in these programs will be dependent on market and other conditions. Our current expectation is that our annual investment in these programs will range from \$20 million to \$40 million. Notwithstanding these programs, the Company expects to continue to return value to its shareholders through a combination of share repurchases and dividends, subject to business performance, economic conditions, changes in income tax regulations and other factors.

We believe these value drivers, when properly implemented, will enhance our profitability, maximize our financial returns and continue to generate value for our shareholders. The ultimate measure of our success will be reflected in the items below.

Results of Operation: Royalty fees, operating income, net income and diluted earnings per share (EPS) represent key measurements of these value drivers. In the three months ended June 30, 2011, royalty fees revenue totaled \$62.3 million, an 8% increase from the same period in 2010. Operating income totaled \$45.1 million for the three months ended June 30, 2011, a \$1.5 million or 3% increase from the same period in 2010. Net income increased 2% from the same period of the prior year to \$27.6 million. Diluted earnings per share for the quarter ended June 30, 2011 were \$0.46 compared to \$0.45 for the three months ended June 30, 2010. These measurements will continue to be a key management focus in 2011 and beyond.

Refer to MD&A heading *Operations Review* for additional analysis of our results.

Liquidity and Capital Resources: Historically, the Company has generated significant cash flows from operations. Since our business does not currently require significant reinvestment of capital, we utilize cash in ways that management believes provide the greatest returns to our shareholders, which include share repurchases and dividends. We believe the Company's cash flow from operations and available financing capacity is sufficient to meet the expected future operating, investing, and financing needs of the business.

Refer to MD&A heading *Liquidity and Capital Resources* for additional analysis.

Operations Review***Comparison of Operating Results for the Three-Month Periods Ended June 30, 2011 and 2010***

The Company recorded net income of \$27.6 million for the three month period ended June 30, 2011, a \$0.6 million increase from the \$27.0 million for the quarter ended June 30, 2010. The increase in net income for the three months ended June 30, 2011, is primarily attributable to a \$1.5 million or 3% increase in operating income, partially offset by a \$1.4 million increase in other income and expenses, net. The increase in other income and expenses, net is primarily attributable to a \$2.6 million increase in interest expense due to higher effective borrowing rates on the fixed rate long-term debt issued in the third quarter of 2010 offset by a \$1.3 million increase in other gains and losses due to the appreciation in the fair value of investments held in the Company's non-qualified benefit plans compared to a decline in fair value of these investments in the prior year period.

Summarized financial results for the three months ended June 30, 2011 and 2010 are as follows:

(in thousands, except per share amounts)	2011	2010
REVENUES:		
Royalty fees	\$ 62,301	\$ 57,443
Initial franchise and relicensing fees	2,585	2,655
Procurement services	6,557	6,611
Marketing and reservation	90,832	80,389
Hotel operations	1,073	1,109
Other	1,953	1,641
Total revenues	165,301	149,848
OPERATING EXPENSES:		
Selling, general and administrative	26,539	22,824
Depreciation and amortization	1,948	2,220
Marketing and reservation	90,832	80,389
Hotel operations	860	808
Total operating expenses	120,179	106,241
Operating income	45,122	43,607
OTHER INCOME AND EXPENSES, NET:		
Interest expense	3,267	675
Interest income	(221)	(135)
Other (gains) and losses	(38)	1,238
Equity in net income of affiliates		(195)
Total other expenses, net	3,008	1,583
Income before income taxes	42,114	42,024
Income taxes	14,536	15,013
Net income	\$ 27,578	\$ 27,011
Diluted earnings per share	\$ 0.46	\$ 0.45

The Company utilizes certain measures such as adjusted net income, adjusted diluted EPS, adjusted selling, general and administrative (SG&A) expense, adjusted operating income and franchising revenues which do not conform to generally accepted accounting principles in the United States (GAAP) when analyzing and discussing its results with the investment community. This information should not be considered as an alternative to any measure of performance as promulgated under GAAP, such as net income, diluted EPS, SG&A, operating income and total

revenues. The Company's calculation of these measurements may be different from the calculations used by other companies and therefore comparability may be limited. We have included below a reconciliation of these measures to the comparable GAAP measurement as well as our reason for reporting these non-GAAP measures.

Franchising Revenues: The Company utilizes franchising revenues which exclude marketing and reservation system revenues and hotel operations rather than total revenues when analyzing the performance of the business. Marketing and reservation activities are excluded from revenues since the Company is contractually required by its franchise agreements to use these fees collected for marketing and reservation activities; as such, no income or loss to the Company is generated. Cumulative marketing and reservation system fees not expended are recorded as a payable on the Company's financial statements and are carried over to the next fiscal year and expended in accordance with the franchise agreements. Cumulative marketing and reservation expenditures in excess of fees collected for marketing and reservation activities are recorded as a receivable on the Company's financial statements. Hotel operations are excluded since they do not reflect the most accurate measure of the Company's core franchising business. This non-GAAP measure is a commonly used measure of performance in our industry and facilitates comparisons between the Company and its competitors.

Calculation of Franchising Revenues

	Three Months Ended June 30, (\$ amounts in thousands)	
	2011	2010
Franchising Revenues:		
Total Revenues	\$ 165,301	\$ 149,848
Adjustments:		
Marketing and reservation system revenues	(90,832)	(80,389)
Hotel operations	(1,073)	(1,109)
Franchising Revenues	\$ 73,396	\$ 68,350

Adjusted Net Income, Adjusted Diluted EPS, Adjusted SG&A and Adjusted Operating Income: We also use adjusted net income, adjusted diluted EPS, adjusted SG&A and adjusted operating income all of which exclude employee termination benefits for the three months ended June 30, 2011 and 2010. The Company utilizes these non-GAAP measures to enable investors to perform meaningful comparisons of past, present and future operating results.

Calculation of Adjusted Operating Income

	Three Months Ended June 30, (\$ amounts in thousands)	
	2011	2010
Operating Income	\$ 45,122	\$ 43,607
Adjustments:		
Employee termination benefits	347	(119)
Adjusted Operating Income	\$ 45,469	\$ 43,488

Calculation of Adjusted SG&A

	Three Months Ended June 30, (\$ amounts in thousands)	
	2011	2010
SG&A	\$ 26,539	\$ 22,824
Adjustments:		
Employee termination benefits	(347)	119
Adjusted SG&A	\$ 26,192	\$ 22,943

Calculation of Adjusted Net Income and Adjusted Diluted EPS

	Three Months Ended June 30, (In thousands, except per share amounts)	
	2011	2010
Net Income	\$ 27,578	\$ 27,011
Adjustments, net of tax:		
Employee termination benefits	218	(74)
Adjusted Net Income	\$ 27,796	\$ 26,937
Weighted average shares outstanding diluted	59,918	59,676
Diluted EPS	\$ 0.46	\$ 0.45
Adjustments:		
Employee termination benefits		
Adjusted Diluted EPS	\$ 0.46	\$ 0.45

The Company recorded adjusted net income of \$27.8 million for the three months ended June 30, 2011, a \$0.9 million increase compared to an adjusted net income of \$26.9 million for the three months ended June 30, 2010. The increase in adjusted net income for the three months ended June 30, 2011 is primarily due to a \$2.0 million increase in adjusted operating income and a \$1.3 million increase in other gains and losses due to the appreciation in the fair value of investments held in the Company's non-qualified benefit plans compared to a decline in fair value of these investments in the prior year period. These increases were partially offset by \$2.6 million increase in interest expense due to the issuance of \$250 million of senior notes in August 2010 which carry a higher effective interest rate than the Company's revolving credit facility. Adjusted operating income increased \$2.0 million as the Company's franchising revenues for the three months ended June 30, 2011 increased \$5.0 million or 7% from the same period of the prior year partially offset by a \$3.2 million increase in adjusted SG&A expenses.

Franchising Revenues: Franchising revenues were \$73.4 million for the three months ended June 30, 2011 compared to \$68.4 million for the three months ended June 30, 2010, an increase of 7%. The increase in franchising revenues is primarily due to an 8% increase in royalty revenues.

Domestic royalty fees for the three months ended June 30, 2011 increased \$3.7 million to \$55.4 million from \$51.7 million in the three months ended June 30, 2010, an increase of 7%. The increase in royalties is attributable to a 6.6% increase in RevPAR and a 4 basis point increase in the effective royalty rate of the domestic hotel system from 4.29% to 4.33%. System-wide RevPAR increased due to a combination of a 2.0% increase in average daily rates and a 230 bps increase in occupancy.

A summary of the Company's domestic franchised hotels operating information is as follows:

	For the Three Months Ended June 30, 2011*			For the Three Months Ended June 30, 2010*			Change		
	Average Daily Rate	Occupancy	RevPAR	Average Daily Rate	Occupancy	RevPAR	Average Daily Rate	Occupancy	RevPAR
Comfort Inn	\$ 77.54	57.7%	\$ 44.73	\$ 75.22	55.9%	\$ 42.04	3.1%	180 bps	6.4%
Comfort Suites	83.89	60.3%	50.55	82.40	56.9%	46.88	1.8%	340 bps	7.8%
Sleep	69.95	55.0%	38.45	68.54	53.3%	36.51	2.1%	170 bps	5.3%
Quality	66.58	50.4%	33.58	65.93	48.0%	31.62	1.0%	240 bps	6.2%
Clarion	73.14	47.9%	35.01	74.37	44.2%	32.85	(1.7)%	370 bps	6.6%
Econo Lodge	53.10	47.4%	25.14	52.44	45.7%	23.95	1.3%	170 bps	5.0%
Rodeway	49.34	47.7%	23.55	48.32	44.8%	21.63	2.1%	290 bps	8.9%
MainStay	66.31	69.2%	45.87	65.04	66.3%	43.09	2.0%	290 bps	6.5%
Suburban	41.13	69.7%	28.68	39.51	65.8%	25.98	4.1%	390 bps	10.4%
Ascend Collection	113.44	60.4%	68.50	108.34	57.0%	61.70	4.7%	340 bps	11.0%
Total	\$ 70.72	54.1%	\$ 38.22	\$ 69.31	51.8%	\$ 35.86	2.0%	230 bps	6.6%

Operating statistics represent hotel operations from March through May

The number of domestic rooms on-line declined by 345 rooms to 389,280 as of June 30, 2011 from 389,625 as of June 30, 2010. The total number of domestic hotels on-line increased by 0.5% to 4,961 as of June 30, 2011 from 4,936 as of June 30, 2010.

A summary of domestic hotels and rooms on-line at June 30, 2011 and 2010 by brand is as follows:

	June 30, 2011		June 30, 2010		Variance			
	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms	%	%
Comfort Inn	1,416	110,736	1,446	113,677	(30)	(2,941)	(2.1)%	(2.6)%
Comfort Suites	613	47,441	621	48,200	(8)	(759)	(1.3)%	(1.6)%
Sleep	394	28,625	392	28,586	2	39	0.5%	0.1%
Quality	1,027	89,571	984	88,453	43	1,118	4.4%	1.3%
Clarion	193	28,335	175	25,188	18	3,147	10.3%	12.5%
Econo Lodge	778	48,197	785	48,543	(7)	(346)	(0.9)%	(0.7)%
Rodeway	377	20,506	381	21,473	(4)	(967)	(1.0)%	(4.5)%
MainStay	39	3,007	36	2,798	3	209	8.3%	7.5%
Suburban	61	7,255	63	7,608	(2)	(353)	(3.2)%	(4.6)%
Ascend Collection	44	3,392	32	2,646	12	746	37.5%	28.2%
Cambria Suites	19	2,215	21	2,453	(2)	(238)	(9.5)%	(9.7)%
Total Domestic Franchises	4,961	389,280	4,936	389,625	25	(345)	0.5%	(0.1)%

International available rooms increased 1.2% to 102,086 as of June 30, 2011 from 100,858 as of June 30, 2010. The total number of international hotels increased 1.6% from 1,138 as of June 30, 2010 to 1,156 as of June 30, 2011.

As of June 30, 2011, the Company had 451 franchised hotels with 37,892 rooms under construction, awaiting conversion or approved for development in its domestic system as compared to 586 hotels and 47,056 rooms at June 30, 2010. The number of new construction franchised hotels in the Company's domestic pipeline declined 25% to 322 at June 30, 2011 from 431 at June 30, 2010. The number of conversion franchised hotels in the Company's domestic pipeline declined by 26 units or 17% from June 30, 2010 to 129 hotels at June 30, 2011. The Company had an additional 103 franchised hotels with 8,720 rooms under construction, awaiting conversion or approved for development in its international system as of June 30, 2011 compared to 97 hotels and 8,726 rooms at June 30, 2010. While the Company's hotel pipeline provides a strong platform for growth, a hotel in the pipeline does not always result in an open and operating hotel due to various factors.

A summary of the domestic franchised hotels under construction, awaiting conversion or approved for development at June 30, 2011 and 2010 by brand is as follows:

	June 30, 2011			June 30, 2010			Variance					
	Units			Units			Conversion		New Construction		Total	
	Conversion	New Construction	Total	Conversion	New Construction	Total	Units	%	Units	%	Units	%
Comfort Inn	27	50	77	33	69	102	(6)	(18)%	(19)	(28)%	(25)	(25)%
Comfort Suites	3	108	111	1	136	137	2	200%	(28)	(21)%	(26)	(19)%
Sleep Inn		62	62	1	101	102	(1)	(100)%	(39)	(39)%	(40)	(39)%
Quality	25	5	30	41	11	52	(16)	(39)%	(6)	(55)%	(22)	(42)%
Clarion	16	2	18	15	5	20	1	7%	(3)	(60)%	(2)	(10)%
Econo Lodge	34	1	35	35	2	37	(1)	(3)%	(1)	(50)%	(2)	(5)%
Rodeway	15	1	16	26	3	29	(11)	(42)%	(2)	(67)%	(13)	(45)%
MainStay	4	37	41		39	39	4	NM	(2)	(5)%	2	5%
Suburban		22	22		26	26		NM	(4)	(15)%	(4)	(15)%
Ascend Collection	5	3	8	3	4	7	2	67%	(1)	(25)%	1	14%
Cambria Suites		31	31		35	35		NM	(4)	(11)%	(4)	(11)%
Total	129	322	451	155	431	586	(26)	(17)%	(109)	(25)%	(135)	(23)%

Domestic hotels open and operating declined by 9 hotels during the three months ended June 30, 2011 compared to an increase of 31 domestic hotels open and operating during the three months ended June 30, 2010. Gross domestic franchise additions declined from 79 for the three months ended June 30, 2010 to 75 for the same period of 2011. New construction hotels represented 11 of the gross domestic additions during three months ended June 30, 2011 compared to 22 hotels in the same period of the prior year. The decline in new construction hotel openings is primarily due to a lack of new hotel construction financing which has resulted in a decline in new executed franchise agreements. Gross domestic additions for conversion hotels during the three months ended June 30, 2011 increased by 7 to 64 hotels from 57 hotels in the same period of the prior year.

Net domestic franchise terminations increased from 48 in the three months ended June 30, 2010 to 84 for the three months ended June 30, 2011 primarily due to an increased number of terminations related to the removal of hotels for non-payment of franchise fees and non-compliance with the Company's rules, regulations and standards.

International royalties increased by \$1.1 million or 20% from \$5.8 million in the second quarter of 2010 to \$6.9 million for the same period of 2011 primarily due to foreign currency fluctuations, global RevPAR increases and an increase in the number of rooms in the international system.

New domestic franchise agreements executed in the three months ended June 30, 2011 totaled 69 representing 6,569 rooms compared to 62 agreements representing 5,478 rooms executed in the second quarter of 2010. During the second quarter of 2011, 8 of the executed agreements were for new construction hotel franchises representing 647 rooms compared to 12 contracts representing 1,109 rooms for the same period a year ago. Conversion hotel executed franchise agreements totaled 61 representing 5,922 rooms for the three months ended June 30, 2011 compared to 50 agreements representing 4,369 rooms for the same period a year ago. Domestic initial fee revenue, included in the initial franchise and relicensing fees caption above, generated from executed franchise agreements increased 8% to \$1.8 million for the three months ended June 30, 2011 from \$1.6 million for the three months ended June 30, 2010. Initial fee revenue increased from the same period of the prior year primarily due to an 11% increase in the number of executed agreements

A summary of executed domestic franchise agreements by brand for the three months ended June 30, 2011 and 2010 is as follows:

	For the Three Months Ended June 30, 2011			For the Three Months Ended June 30, 2010			% Change		
	New	Conversion	Total	New	Conversion	Total	New	Conversion	Total
	Construction			Construction			Construction		
Comfort Inn	3	11	14	2	5	7	50%	120%	100%
Comfort Suites	1	2	3	6	1	7	(83)%	100%	(57)%
Sleep	1	1	2				NM	NM	NM
Quality		11	11		20	20	NM	(45)%	(45)%
Clarion		3	3		3	3	NM	%	%
Econo Lodge		12	12		12	12	NM	%	%
Rodeway		13	13		8	8	NM	63%	63%
MainStay		3	3	1		1	(100)%	NM	200%
Suburban	2	1	3				NM	NM	NM
Ascend Collection		4	4		1	1	NM	300%	300%
Cambria Suites	1		1	3		3	(67)%	NM	(67)%
Total Domestic System	8	61	69	12	50	62	(33)%	22%	11%

Relicensing fees include fees charged to the new owners of a franchised property whenever an ownership change occurs and the property remains in the franchise system as well as fees required to renew expiring franchise contracts. Relicensing and renewal contracts increased 19% from 31 in the second quarter of 2010 to 37 for the three months ended June 30, 2011. Relicensing revenues declined \$0.2 million from \$1.0 million for the three months ended June 30, 2010 to \$0.8 million for the three months ended June 30, 2011 due to a decrease in the average initial fee per agreement. The Company's relicensing activity in 2011 and beyond is dependent on the availability and cost of capital as well as the presence of an active real estate market for hotel transactions.

Selling, General and Administrative Expenses: The cost to operate the franchising business is reflected in SG&A on the consolidated statements of income. SG&A expenses were \$26.5 million for the three months ended June 30, 2011, a \$3.7 million or 16% increase from the three months ended June 30, 2010. Adjusted SG&A costs, which exclude certain items described above, increased \$3.2 million to \$26.2 million for the three months ended June 30, 2011 from \$22.9 million for the same period of 2010. Adjusted SG&A for the three months ended June 30, 2011 increased 14% over the same period of the prior year primarily due to increases in variable management incentive compensation, increased costs related to the Company's annual franchisee convention, foreign currency fluctuations and higher compensation expense recognized on deferred compensation arrangements as described in more detail in *Other Income and Expenses, Net*.

Marketing and Reservations: The Company's franchise agreements require the payment of franchise fees, which include marketing and reservation system fees. The fees, which are primarily based on a percentage of the franchisees' gross room revenues, are used exclusively by the Company for expenses associated with providing franchise services such as central reservation systems, national marketing and media advertising. The Company is contractually obligated to expend the marketing and reservation system fees it collects from franchisees in accordance with the franchise agreements; as such, no income or loss to the Company is generated.

Total marketing and reservation system fees were \$90.8 million and \$80.4 million for the three months ended June 30, 2011 and 2010, respectively. Depreciation and amortization attributable to marketing and reservation activities was \$3.3 million and \$3.4 million for the three month periods ended June 30, 2011 and 2010, respectively. Interest expense attributable to reservation activities was approximately \$1.0 million and \$0.1 million for the three month periods ended June 30, 2011 and 2010, respectively. The increase in the interest expense is primarily attributable to an increase in the Company's effective annual borrowing rates.

As of June 30, 2011 and December 30, 2010, the Company's balance sheet includes a receivable of \$60.5 million and \$42.5 million, respectively from cumulative marketing and reservation expenses incurred in excess of cumulative marketing and reservations system fee revenues earned. These receivables are recorded as an asset in the financial statements as the Company has the contractual authority to require that the franchisees in the system at any given point repay the Company for any deficits related to marketing and reservation activities. The Company's current franchisees are legally obligated to pay any assessment the Company imposes on its franchisees to obtain reimbursement of such deficit regardless of whether those constituents continue to generate gross room revenue and whether or not they joined the system following the deficit's occurrence. The Company has no present intention to accelerate repayment of the deficit from current franchisees. Conversely, cumulative marketing and reservation system fees not expended are recorded as a payable in the financial statements and are carried over to the next fiscal year and expended in accordance with the franchise agreements.

Our ability to recover these receivables may be adversely impacted by certain factors, including, among others, declines in the ability of our franchisees to generate revenues at properties they franchise from us, lower than expected franchise system growth of certain brands and/or lower than expected international franchise system growth. An extended period of occupancy or room rate declines or a decline in the number of hotel rooms in our franchise system could result in the generation of insufficient funds to recover marketing and reservation advances as well as meet the ongoing marketing and reservation needs of the overall system.

Other Income and Expenses, Net: Other income and expenses, net, increased \$1.4 million to an expense of \$3.0 million for the three months ended June 30, 2011 compared to an expense of \$1.6 million in the same period of the prior year primarily due to the following items:

Interest expense increased from \$0.7 million for the three months ended June 30, 2010 to \$3.3 million for the same period of 2011 due to the issuance of the Company's \$250 million senior notes with an effective rate of 6.19% on August 25, 2010. The proceeds were utilized to repay outstanding borrowings under the Company's \$350 million revolving line of credit which had an effective interest rate of approximately 0.7%.

Other gains and losses, net increased from a loss of \$1.2 million for the three months ended June 30, 2010 to a gain of \$38 thousand for the three months ended June 30, 2011 primarily due to fluctuations in the fair value of investments held in the Company's non-qualified employee benefit plans. As discussed in the accompanying critical accounting policies, the Company sponsors two non-qualified retirement and savings plans: the Non-Qualified Plan and the EDCP plan. The fair value of the Non-Qualified Plan investments declined by \$9 thousand during the three

months ended June 30, 2011 compared to a decline of \$0.6 million during the three months ended June 30, 2010. The fair value of the Company's investments held in the EDCP plan increased \$48 thousand during the three months ended June 30, 2011 compared to a decrease in fair value of \$0.7 million during the same period of the prior year.

The Company accounts for the Non-Qualified Plan in accordance with accounting for deferred compensation arrangements when investments are held in a rabbi trust and invested. As a result, the Company also recognizes compensation expense in SG&A related to changes in the fair value of investments held in the Non-Qualified Plan, excluding investments in the Company's stock. Therefore, during the three months ended June 30, 2011 and 2010, the Company's SG&A expense was reduced by \$0.1 million and \$0.7 million, respectively, due to the change in the fair value of these investments.

Income taxes. The effective income tax rate was 34.5% for the three months ended June 30, 2011, compared to an effective income tax rate of 35.7% for the three months ended June 30, 2010. The effective income tax rates for the three months ended June 30, 2011 and 2010 differed from the U.S. federal statutory rate of 35% primarily due to the effect of foreign operations, partially offset by state income taxes.

Net income: Net income for the three months ended June 30, 2011 increased by \$0.6 million to \$27.6 million from \$27.0 million in the same period of the prior year. Adjusted net income, as adjusted for certain items described above, increased by \$0.9 million to \$27.8 million for the three months ended June 30, 2011 from \$26.9 million for the same period of the prior year.

Diluted EPS: Diluted EPS were \$0.46 and \$0.45 for the three months ended June 30, 2011 and 2010, respectively.

Comparison of Operating Results for the Six-Month Periods Ended June 30, 2011 and 2010

The Company recorded net income of \$43.3 million for the six months ended June 30, 2011, a \$0.5 million, or 1% increase from the \$42.8 million for the six months ended June 30, 2010. The increase in net income for the six months ended June 30, 2011, is primarily attributable to a \$3.4 million or 5% increase in operating income partially offset by the Company's recordation of a \$1.8 million loss on assets held for sale as well as an increase in effective borrowing rates due to the issuance of fixed rate long-term debt in August 2010.

Summarized financial results for the six months ended June 30, 2011 and 2010 are as follows:

(in thousands, except per share amounts)	2011	2010
REVENUES:		
Royalty fees	\$ 106,541	\$ 98,464
Initial franchise and relicensing fees	5,199	4,567
Procurement services	9,722	9,856
Marketing and reservation	153,799	139,229
Hotel operations	1,937	1,976
Other	3,384	3,177
Total revenues	280,582	257,269
OPERATING EXPENSES:		
Selling, general and administrative	50,386	44,640
Depreciation and amortization	3,903	4,392
Marketing and reservation	153,799	139,229
Hotel operations	1,693	1,564
Total operating expenses	209,781	189,825
Operating income	70,801	67,444
OTHER INCOME AND EXPENSES, NET:		
Interest expense	6,491	1,296
Interest income	(431)	(195)
Other (gains) and losses	1,005	221
Equity in net income of affiliates	(301)	(548)
Total other income and expenses, net	6,764	774
Income before income taxes	64,037	66,670
Income taxes	20,729	23,866
Net income	\$ 43,308	\$ 42,804
Diluted earnings per share	\$ 0.72	\$ 0.72

The Company utilizes certain measures such as adjusted net income, adjusted diluted EPS, adjusted SG&A, adjusted operating income and franchising revenues which do not conform to GAAP when analyzing and discussing its results with the investment community. This information should not be considered as an alternative to any measure of performance as promulgated under GAAP, such as net income, diluted EPS, SG&A, operating income and total revenues. The Company's calculation of these measurements may be different from the calculations used by other companies and therefore comparability may be limited. We have included a reconciliation of these measures to the comparable GAAP measurement below as well as our reason for reporting these non-GAAP measures.

