FOSSIL INC
Form 10-Q
May 09, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: March 30, 2013

OR

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

For the transition period from to

Commission file number: 000-19848

FOSSIL, INC.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**75-2018505** (I.R.S. Employer Identification No.)
901 S. Central Expressway, Richardson, Texas (Address of principal executive offices)	**75080** (Zip Code)

(972) 234-2525

(Registrant s telephone number, including area code)

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

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

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 (check one):

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

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

The number of shares of the registrant s common stock outstanding as of May 3, 2013: 58,672,408.

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

FOSSIL, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

UNAUDITED

IN THOUSANDS

	March 30, 2013	December 29, 2012
Assets		
Current assets:		
Cash and cash equivalents	$ 241,396	$ 177,236
Securities available for sale	56	127
Accounts receivable - net of allowances of $75,762 and $82,362, respectively	272,860	363,456
Inventories	520,306	506,314
Deferred income tax assets-net	31,442	34,238
Prepaid expenses and other current assets	81,598	62,741
Total current assets	1,147,658	1,144,112
Investments	0	6,965
Property, plant and equipment - net of accumulated depreciation of $269,411 and $262,041, respectively	329,223	335,446
Goodwill	201,356	184,793
Intangible and other assets-net	178,332	170,673
Total long-term assets	708,911	697,877
Total assets	$ 1,856,569	$ 1,841,989
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	$ 124,859	$ 149,561
Short-term debt	1,600	2,794
Accrued expenses:		
Compensation	50,044	55,563
Royalties	29,819	53,547
Co-op advertising	15,048	24,500
Transaction taxes	17,908	27,973
Other	56,733	61,575
Income taxes payable	18,307	31,265
Total current liabilities	314,318	406,778
Long-term income taxes payable	10,172	8,662
Deferred income tax liabilities	87,292	79,756
Long-term debt	151,129	75,140
Other long-term liabilities	48,304	31,189
Total long-term liabilities	296,897	194,747

Commitments and contingencies (Note 12)				
Stockholders equity:				
Common stock, 59,203 and 59,631 shares issued at March 30, 2013 and December 29, 2012, respectively		592		596
Additional paid-in capital		140,083		138,097
Retained earnings		1,083,717		1,066,082
Accumulated other comprehensive income		12,243		28,760
Total Fossil, Inc. stockholders equity		1,236,635		1,233,535
Noncontrolling interest		8,719		6,929
Total stockholders equity		1,245,354		1,240,464
Total liabilities and stockholders equity	$	1,856,569	$	1,841,989

See notes to the condensed consolidated financial statements.

FOSSIL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

UNAUDITED

IN THOUSANDS, EXCEPT PER SHARE DATA

	For the 13 Weeks Ended			
	March 30, 2013		March 31, 2012	
Net sales	$	680,899	$	589,533
Cost of sales		302,428		260,553
Gross profit		378,471		328,980
Operating expenses:				
Selling and distribution		203,189		181,438
General and administrative		80,961		64,681
Total operating expenses		284,150		246,119
Operating income		94,321		82,861
Interest expense		1,231		814
Other income-net		9,784		2,549
Income before income taxes		102,874		84,596
Provision for income taxes		28,894		23,524
Net income		73,980		61,072
Less: Net income attributable to noncontrolling interest		1,794		2,932
Net income attributable to Fossil, Inc.	$	72,186	$	58,140
Other comprehensive (loss) income, net of taxes:				
Currency translation adjustment	$	(19,837)	$	10,071
Unrealized (loss) gain on securities available for sale		(71)		50
Forward contracts hedging intercompany foreign currency payments-change in fair values		3,391		(1,349)
Total other comprehensive (loss) income		(16,517)		8,772
Total comprehensive income		57,463		69,844
Less: Comprehensive income attributable to noncontrolling interest		1,794		2,932
Comprehensive income attributable to Fossil, Inc.	$	55,669	$	66,912
Earnings per share:				
Basic	$	1.22	$	0.94
Diluted	$	1.21	$	0.93
Weighted average common shares outstanding:				
Basic		59,393		61,859
Diluted		59,783		62,459

See notes to the condensed consolidated financial statements.

FOSSIL, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

UNAUDITED

IN THOUSANDS

	For the 13 Weeks Ended	
	March 30, 2013	**March 31, 2012**
Operating Activities:		
Net income	$ 73,980	$ 61,072
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and accretion	18,758	15,227
Stock-based compensation	2,546	3,144
Decrease in allowance for returns-net of inventory in transit	(238)	(2,917)
Loss on disposal of assets	266	517
Equity in income of joint venture	0	(270)
Gain on equity method investment	(6,410)	0
Decrease in allowance for doubtful accounts	(4,202)	(1,396)
Excess tax benefits from stock-based compensation	(4,082)	(9,901)
Deferred income taxes and other	8,292	3,919
Changes in operating assets and liabilities:		
Accounts receivable	99,403	88,197
Inventories	(11,507)	(19,355)
Prepaid expenses and other current assets	(14,721)	(5,527)
Accounts payable	(20,369)	(45,310)
Accrued expenses	(49,000)	(60,930)
Income taxes payable	(6,813)	9,029
Net cash provided by operating activities	85,903	35,499
Investing Activities:		
Additions to property, plant and equipment	(19,485)	(10,029)
Increase in intangible and other assets	(723)	(27)
Net change in restricted cash	452	(157)
Business acquisitions-net of cash acquired	(15,165)	0
Net cash used in investing activities	(34,921)	(10,213)
Financing Activities:		
Acquisition of common stock	(61,188)	(67,878)
Distribution of noncontrolling interest earnings	(4)	(3,786)
Excess tax benefits from stock-based compensation	4,082	9,901
Debt borrowings	218,098	3,899
Debt payments	(142,718)	(4)
Proceeds from exercise of stock options	1,991	4,352
Net cash provided by (used in) financing activities	20,261	(53,516)
Effect of exchange rate changes on cash and cash equivalents	(7,083)	1,210
Net increase (decrease) in cash and cash equivalents	64,160	(27,020)
Cash and cash equivalents:		
Beginning of period	177,236	287,498

End of period	$	241,396	$	260,478

See notes to the condensed consolidated financial statements.

FOSSIL, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

UNAUDITED

1. FINANCIAL STATEMENT POLICIES

Basis of Presentation. The condensed consolidated financial statements include the accounts of Fossil, Inc., a Delaware corporation, and its wholly and majority-owned subsidiaries (the Company). The condensed consolidated financial statements reflect all adjustments that are, in the opinion of management, necessary to present a fair statement of the Company s financial position as of March 30, 2013, and the results of operations for the thirteen week periods ended March 30, 2013 (First Quarter) and March 31, 2012 (Prior Year Quarter), respectively. All adjustments are of a normal, recurring nature.

These interim condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Annual Report on Form 10-K filed by the Company pursuant to the Securities Exchange Act of 1934, as amended (the Exchange Act), for the fiscal year ended December 29, 2012 (the 2012 Form 10-K). Operating results for the First Quarter are not necessarily indicative of the results to be achieved for the full fiscal year.

The condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP), which require the Company to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the periods reported. Actual results could differ from those estimates. The Company has not made any changes in its significant accounting policies from those disclosed in the 2012 Form 10-K.

Business. The Company is a global design, marketing and distribution company that specializes in consumer fashion accessories. Its principal offerings include an extensive line of men s and women s fashion watches and jewelry, handbags, small leather goods, belts, sunglasses, soft accessories and clothing. In the watch and jewelry product categories, the Company has a diverse portfolio of globally recognized owned and licensed brand names under which its products are marketed. The Company s products are distributed globally through various distribution channels, including wholesale in countries where it has a physical presence, direct to the consumer through its retail stores and commercial websites and through third-party distributors in countries where the Company does not maintain a physical presence. The Company s products are offered at varying price points to meet the needs of its customers, whether they are value-conscious or luxury oriented. Based on its extensive range of accessory products, brands, distribution channels and price points, the Company is able to target style-conscious consumers across a wide age spectrum on a global basis.

Foreign Currency Hedging Instruments. The Company s foreign subsidiaries periodically enter into foreign exchange forward contracts to hedge the future payment of intercompany inventory transactions denominated in U.S. dollars. If the Company s foreign subsidiaries were to settle their contracts designated as cash flow hedges that were denominated in Euros, British Pounds, Mexican Pesos, Australian Dollars, Canadian Dollars and Japanese Yen, the net result would have been a gain of approximately $4.4 million, net of taxes, as of March 30, 2013. The Company applies the hedge accounting rules as required by Accounting Standard Codification (ASC) 815, *Derivatives and Hedging* (ASC 815). See Note 8 Derivatives and Risk Management for additional disclosures about the Company s use of forward contracts.

Earnings Per Share (EPS). Basic EPS is based on the weighted average number of common shares outstanding during each period. Diluted EPS adjusts basic EPS for the effects of dilutive common stock equivalents outstanding during each period using the treasury stock method.

The following table reconciles the numerators and denominators used in the computations of both basic and diluted EPS (in thousands except per share data):

	For the 13 Weeks Ended March 30, 2013	For the 13 Weeks Ended March 31, 2012
Numerator:		
Net income attributable to Fossil, Inc.	$ 72,186	$ 58,140
Denominator:		
Basic EPS computation:		
Basic weighted average common shares outstanding	59,393	61,859
Basic EPS	$ 1.22	$ 0.94
Diluted EPS computation:		
Basic weighted average common shares outstanding	59,393	61,859
Stock options, stock appreciation rights and restricted stock units	390	600
Diluted weighted average common shares outstanding	59,783	62,459
Diluted EPS	$ 1.21	$ 0.93

Approximately 201,000 and 237,000 shares issuable under stock-based awards were not included in the diluted EPS calculation at the end of the First Quarter and Prior Year Quarter, respectively, because they were antidilutive.

Restricted Cash. As of March 30, 2013 and December 29, 2012, the Company had short-term restricted cash balances of $0.2 million and $0.3 million, respectively, and long-term restricted cash balances of $0.7 million and $1.0 million, respectively, primarily pledged as collateral to secure bank guarantees for the purpose of obtaining retail space. Short-term restricted cash is reported in prepaid expenses and other current assets in the Company s condensed consolidated balance sheets as a component of current assets. Long-term restricted cash is reported in intangible and other assets-net in the Company s condensed consolidated balance sheets as a component of long-term assets.

Recently Issued Accounting Standards. In March 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-05, *Foreign Currency Matters (Topic 830): Parent s Accounting for the Cumulative Translation Adjustment upon Derecognition of Certain Subsidiaries or Groups of Assets within a Foreign Entity or of an Investment in a Foreign Entity* (ASU 2013-05). ASU 2013-05 addresses the accounting for the cumulative translation adjustment when a parent either sells a part or all of its investment in a foreign entity or no longer holds a controlling financial interest in a subsidiary or group of assets that is a nonprofit activity or a business within a foreign entity. The guidance outlines the events when cumulative translation adjustments should be released into net income and is intended by FASB to eliminate some disparity in current accounting practice. The guidance in ASU 2013-05 will become effective for the Company for annual and interim periods beginning after December 15, 2013. The Company will apply the guidance prospectively to any derecognition events that may occur after the effective date, and does not expect the adoption of ASU 2013-05 to have a material impact on the Company s condensed consolidated results of operations or financial position.

In February 2013, the FASB issued ASU 2013-04, *Liabilities (Topic 405): Obligations Resulting From Joint and Several Liability Arrangements for Which the Total Amount of the Obligation is Fixed at the Reporting Date* (ASU 2013-04). The update requires an entity to measure obligations resulting from joint and several liability arrangements for which the total amount of the obligation is fixed as of the reporting date. The amount is equal to the sum of the obligation the entity agreed to pay among its co-obligors and any additional amount the entity expects to pay on behalf of its co-obligors. ASU 2013-04 will become effective for the Company for annual and interim periods beginning after December 15, 2013 and is required to be applied retrospectively to all prior periods presented for obligations that existed upon adoption of ASU 2013-04. The Company does not expect the adoption of ASU 2013-04 to have a material impact on the Company s condensed consolidated results of operations or financial position.

In December 2011, the FASB issued ASU 2011-11, *Balance Sheet (Topic 210)*: *Disclosures about Offsetting Assets and Liabilities* (ASU 2011-11), to address certain comparability issues between financial statements prepared in accordance with GAAP and those prepared in accordance with International Financial Reporting Standards. In January 2013, the FASB issued ASU 2013-01, *Balance Sheet (Topic 210): Clarifying the Scope of Disclosures about Offsetting Assets and Liabilities* (ASU 2013-01), which clarifies which instruments and transactions are subject to the offsetting disclosure requirements established by ASU 2011-11. ASU 2011-11 will require an entity to provide enhanced disclosures about certain financial instruments and derivatives, as defined in ASU 2013-01, to enable users to understand the effects of offsetting in the financial statements as well as the effects of master netting arrangements on an entity s financial condition. The amendments in ASU 2011-11 and ASU 2013-01 are effective for annual and interim reporting periods beginning on or after January 1, 2013, with respective disclosures required for all comparative periods presented. The Company does not expect the adoption of ASU 2011-11 and ASU 2013-01 to have a material impact on the Company s condensed consolidated results of operations or financial position.

Recently Adopted Accounting Standards. In July 2012, the FASB issued ASU 2012-02, *Intangibles Goodwill and Other (Topic 350): Testing Indefinite-Lived Intangible Assets for Impairment* (ASU 2012-02). The amendments in this update permit an entity to make a qualitative assessment to determine if it is more likely than not that an indefinite-lived intangible asset other than goodwill is impaired. If an entity concludes that it is more likely than not that the fair value of an indefinite-lived intangible asset other than goodwill is less than its carrying amount, it is required to perform the quantitative impairment test for that asset. This ASU aligns the guidance of impairment testing for indefinite-lived intangible assets other than goodwill with that in ASU 2011-08, *Intangibles Goodwill and Other (Topic 350): Testing Goodwill for Impairment* (ASU 2011-08). The guidance in ASU 2012-02 was effective for the Company beginning December 30, 2012 and did not have a material impact on the Company s condensed consolidated results of operations or financial position.

In February 2013, the FASB issued ASU 2013-02, *Comprehensive Income (Topic 220): Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (ASU 2013-02). FASB issued ASU 2013-02 to improve the transparency of changes in other comprehensive income (OCI) and items reclassified out of accumulated other comprehensive income (AOCI) in financial statements. ASU 2013-12 requires an entity to provide information about amounts reclassified out of AOCI by component. In addition, an entity must present either on the face of the income statement or in the notes, significant amounts reclassified out of AOCI by the respective line items of net income. See Note 6 Stockholders Equity and Benefit Plans for additional disclosures about the Company s OCI. The guidance in ASU 2013-02 became effective for the Company on December 30, 2012 and did not have a material impact on the Company s condensed consolidated results of operations or financial position.

2. ACQUISITIONS AND GOODWILL

Skagen Designs, Ltd. Acquisition. On April 2, 2012, the Company acquired Skagen Designs, Ltd. and certain of its international affiliates (Skagen Designs). Skagen Designs was a privately held Nevada-based company that globally marketed and distributed contemporary Danish design accessories including watches, clocks, jewelry and sunglasses. The primary purpose of the acquisition was to add an attractive brand to the Company s portfolio that the Company could grow using its established distribution channels. The purchase price was $231.7 million in cash and 150,000 shares of the Company s common stock valued at $19.9 million based on the mean between the highest and lowest sales price of the Company s common stock on NASDAQ on April 2, 2012. To fund the cash purchase price, the Company utilized approximately $200 million of availability under its $350 million revolving line of credit and excess cash available in its international subsidiaries to fund the international portion of the purchase price. In addition, subject to the purchase agreement, the sellers could have received up to 100,000 additional shares of the Company s common stock if the Company s net sales of SKAGEN® branded products exceeded certain thresholds over a defined period of time (the Earnout).

The Company recorded the Earnout as a $9.9 million contingent consideration liability in accrued expenses-other in the Company s condensed consolidated balance sheets as of the acquisition date. As of December 29, 2012, the contingent consideration liability was remeasured at zero, which resulted in a decrease in operating expenses of $9.9 million during fiscal year 2012. During the First Quarter, the contingent consideration liability remained valued at zero. The results of Skagen Designs operations have been included in the Company s consolidated financial statements since April 2, 2012.

Prior to closing the Skagen Designs acquisition, the Company incurred approximately $600,000 of acquisition-related expenses for legal, accounting and valuation services during fiscal year 2011 and the Prior Year Quarter. The Company incurred additional acquisition and integration related costs of approximately $8.2 million in fiscal year 2012, subsequent to the closing date. Acquisition and integration costs were reflected in general and administrative expenses on the Company s consolidated statements of comprehensive income. There were no acquisition and integration costs incurred during the First Quarter.

The Company s consolidated statements of comprehensive income for fiscal year 2012 included $93.8 million of net sales and $11.2 million of operating income, related to the results of operations of Skagen Designs since April 2, 2012. Operating income for fiscal year 2012 was favorably impacted by $10.0 million related to Skagen Designs ongoing operations.

During the First Quarter, the purchase accounting was finalized with no change since fiscal year end December 29, 2012. Assets acquired and liabilities assumed in the transaction were recorded at their acquisition date fair values, while transaction costs associated with the acquisition were expensed as incurred. Because the total purchase price exceeded the fair values of the tangible and intangible assets acquired, goodwill was recorded equal to the difference. The element of goodwill that is not separable into identifiable intangible assets represents expected synergies. The following table summarizes the allocation of the purchase price to the fair value of the assets acquired and the liabilities assumed as of April 2, 2012, the effective date of the acquisition (in thousands):

Cash paid, net of cash acquired	$	229,012
Value of common stock issued		19,899
Contingent consideration		9,950
Total transaction consideration	$	258,861
Accounts receivable	$	16,595
Inventories		22,638
Prepaid expenses and other current assets		3,306
Property, plant and equipment		4,232
Goodwill		140,387
Trade name		64,700
Customer lists		24,400
Patents		1,500
Noncompete agreement		1,900
Other long-term assets		2,972
Current liabilities		(20,840)
Long-term liabilities		(2,929)
Total net assets acquired	$	258,861

The goodwill and trade name assets recognized from the acquisition have indefinite useful lives, were tested for impairment at fiscal year end 2012 and will continue to be tested for impairment annually. The amortization periods for the acquired customer lists, patents and noncompete agreements have amortization periods of three years to nine years. Approximately $133.8 million of the goodwill recognized in the acquisition is expected to be deductible for tax purposes.

The following unaudited pro forma information presents the combined results of operations of Fossil, Inc. and Skagen Designs as if the acquisition had occurred at the beginning of each period presented below. The pro forma information is not necessarily indicative of what the financial position or results of operations actually would have been had the acquisition been completed at the beginning of each period presented below. In addition, the unaudited pro forma financial information is not indicative of, nor does it purport to project, the future financial position or operating results of Fossil, Inc. The unaudited pro forma information does not give effect to any potential cost savings or other operating efficiencies that could result from the acquisition. The following table presents the unaudited pro forma financial information (in thousands, except per share data):

	For the 13 Weeks Ended			
		March 30, 2013		**March 31, 2012**
Net sales	$	680,899	$	619,977
Net income attributable to Fossil, Inc.		72,186		58,637
Earnings per share:				
Basic	$	1.22	$	0.95
Diluted	$	1.21	$	0.94

Fossil Spain Acquisition. On August 10, 2012, the Company s joint venture company, Fossil, S.L. (Fossil Spain) entered into a Framework Agreement (the Framework Agreement) with several related and unrelated parties, including General De Relojeria, S.A. (General De Relojeria), the Company s joint venture partner. Pursuant to the Framework Agreement, Fossil Spain was granted the right to acquire the outstanding 50% of its shares owned by General De Relojeria upon the expiration of the joint venture agreement on December 31, 2015.

Effective January 1, 2013, pursuant to the Framework Agreement, the Company assumed control over the board of directors and the day-to-day management of Fossil Spain. As a result of this change, the Company now controls Fossil Spain and began consolidating it in accordance with ASC 810, *Consolidation*, instead of treating it as an equity method investment. In accordance with ASC 805, *Business Combinations*, the

Company remeasured its preexisting investment in Fossil Spain to fair value as of January 1, 2013, resulting in a gain of $6.4 million, which was recorded in other income-net on the Company s condensed consolidated statements of comprehensive income. The results of Fossil Spain s operations have been included in the Company s condensed consolidated financial statements since January 1, 2013. The Company recorded approximately $10.7 million of goodwill related to the acquisition.

The purchase price for the shares has a fixed and variable component. The fixed portion is based on 50% of the net book value of Fossil Spain as of December 31, 2012. The fixed portion was measured at 5.1 million Euros (approximately $6.7 million at December 31, 2012). The Company recorded a contingent consideration liability of 5.9 million Euros (approximately $7.8 million) related to the variable portion of the purchase price as of January 1, 2013. The variable portion will be determined based on Fossil Spain s aggregated results of operations less dividends distributed by Fossil Spain to General De Relojeria with a minimum annual variable price of 2.0 million Euros (approximately $2.6 million at March 30, 2013) and a maximum annual variable price of 3.5 million Euros (approximately $4.5 million at March 30, 2013) for each of the calendar years 2013, 2014, and 2015.

Both the fixed and variable portions of the purchase price were recorded in other long-term liabilities in the condensed consolidated balance sheets at March 30, 2013.

Bentrani Watches, LLC Acquisition. On December 31, 2012, the Company purchased substantially all of the assets of Bentrani Watches, LLC (Bentrani). Bentrani was a distributor of watch products in 16 Latin American countries and was based in Miami, Florida. Bentrani was the Company s largest third-party distributor and had partnered with the Company for ten years. The purchase price was $26.0 million, comprised of $18.7 million in cash and $7.3 million in forgiveness of a payable to the Company. The Company recorded approximately $8.1 million of goodwill related to the acquisition. The results of Bentrani s operations have been included in the Company s condensed consolidated financial statements since the acquisition date.

Goodwill is the excess of the cost of an acquired entity over the net of the amounts assigned to assets acquired and liabilities assumed. The changes in the carrying amount of goodwill, which is not subject to amortization, were as follows (in thousands):

	North America wholesale	Europe wholesale	Asia Pacific wholesale	Total
Balance at December 29, 2012	$ 109,270	$ 63,884	$ 11,639	$ 184,793
Acquisitions	8,130	10,723	0	18,853
Foreign currency changes	102	(2,306)	(86)	(2,290)
Balance at March 30, 2013	$ 117,502	$ 72,301	$ 11,553	$ 201,356

3. INVENTORIES

Inventories consisted of the following (in thousands):

	March 30, 2013	December 29, 2012
Components and parts	$ 60,566	$ 62,731
Work-in-process	6,757	8,071
Finished goods	452,983	435,512
Inventories	$ 520,306	$ 506,314

4. WARRANTY RESERVE

The Company s warranty liabilities are primarily related to watch products. The Company s FOSSIL® watch products sold in the U.S. are covered by a limited warranty against defects in materials or workmanship for a period of 11 years from the date of purchase. RELIC® watch products sold in the U.S. are covered by a comparable 12 year warranty, while certain other watches sold by the Company are covered by a comparable two year limited warranty. SKAGEN branded watches are covered by a lifetime warranty against defects due to faulty material or workmanship, subject to normal conditions of use. The Company s warranty liability is recorded using historical warranty repair expense and is recorded in accrued expenses-other in the condensed consolidated balance sheets. As changes in warranty costs are experienced, the warranty accrual is adjusted as necessary. Warranty liability activity consisted of the following (in thousands):

	For the 13 Weeks Ended	
	March 30, 2013	March 31, 2012
Beginning balance	$ 13,383	$ 10,996
Settlements in cash or kind	(2,461)	(993)
Warranties issued and adjustments to preexisting warranties (1)	2,396	2,085
Liabilities assumed in acquisition	340	0
Ending balance	$ 13,658	$ 12,088

(1) Changes in cost estimates related to preexisting warranties are aggregated with accruals for new standard warranties issued and foreign currency changes.

5. INCOME TAXES

The Company s income tax expense and related effective rate were as follows (in thousands, except percentage data):

	For the 13 Weeks Ended	
	March 30, 2013	March 31, 2012
Income tax expense	$ 28,894	$ 23,524
Income tax rate	28.1%	27.8%

The lower effective tax rate in the Prior Year Quarter was attributable to management s decision to indefinitely reinvest the undistributed earnings of certain foreign subsidiaries. The First Quarter effective tax rate was favorably impacted by audit settlements.

As of March 30, 2013, the total amount of unrecognized tax benefits, excluding interest and penalties, was $9.2 million, of which $6.0 million would favorably impact the effective tax rate in future periods, if recognized. The U.S. Internal Revenue Service completed its examination of the Company s 2007-2009 federal income tax returns, and the Company has settled all outstanding federal income tax liabilities for those years. The Company is subject to examinations in various state and foreign jurisdictions for its 2005-2012 tax years, none of which the Company believes are individually significant. Audit outcomes and timing of audit settlements are subject to significant uncertainty.

The Company has classified uncertain tax positions as long-term income taxes payable, unless such amounts are expected to be paid within twelve months of the condensed consolidated balance sheet date. As of March 30, 2013, the Company had recorded $0.1 million of unrecognized tax benefits, excluding interest and penalties, for positions that could be settled within the next twelve months. Consistent with its past practice, the Company recognizes interest and/or penalties related to income tax overpayments and income tax underpayments in income tax expense and income taxes receivable/payable, respectively. The total amount of accrued income tax-related interest and penalties included in the condensed consolidated balance sheets at March 30, 2013 was $0.8 million and $0.3 million, respectively. For the First Quarter, the Company accrued income tax-related interest expense of $0.1 million.

6. STOCKHOLDERS EQUITY AND BENEFIT PLANS

Common Stock Repurchase Programs. Purchases of the Company s common stock are made from time to time pursuant to its repurchase programs, subject to market conditions and at prevailing market prices, through the open market. Repurchased shares of common stock are recorded at cost and become authorized but unissued shares which may be issued in the future for general corporate or other purposes. The Company may terminate or limit its stock repurchase program at any time. In the event the repurchased shares are cancelled, the Company accounts for retirements by allocating the repurchase price to common stock, additional paid-in capital and retained earnings. The repurchase price allocation is based upon the equity contribution associated with historical issuances. The repurchase programs are conducted pursuant to Rule 10b-18 of the Exchange Act. During the First Quarter, the Company completed its $750 million buyback plan authorized in August 2010. The Company repurchased 9.6 million shares of common stock under that plan, of which $38.6 million, or 0.4 million shares, were repurchased during the First Quarter. In addition, the Company repurchased $18.0 million of its common stock in the First Quarter, or 0.2 million shares, under the Company s $1 billion repurchase plan, which was authorized in 2012. As of March 30, 2013, the Company had $1.0 billion of repurchase authorizations remaining under the combined repurchase plans.

During the First Quarter, the Company effectively retired 0.6 million shares of common stock repurchased under its repurchase programs. The effective retirement of repurchased common stock decreased common stock by $6,000, additional paid-in capital by $2.0 million, retained earnings by $54.6 million and treasury stock by $56.5 million.

At December 29, 2012 and March 30, 2013, all treasury stock had been effectively retired.

The following table reflects the Company s common stock repurchase activity for the periods indicated (in millions):

			For the 13 Weeks Ended March 30, 2013		For Fiscal Year 2012	
Fiscal Year Authorized	**Dollar Value Authorized**	**Termination Date**	**Number of Shares Repurchased**	**Dollar Value Repurchased**	**Number of Shares Repurchased**	**Dollar Value Repurchased**
2012	$ 1,000.0	December 2016	0.2	$ 18.0	0.0	$ 0.0

Tax Matters

As the general partner, we are the tax matters partner of our operating partnership and, as such, have authority to make tax elections under the Code on behalf of our operating partnership.

Extraordinary Transactions

The Partnership Agreement provides that we may not generally engage in any merger, consolidation, or other combination with any other person or sale of all or substantially all of our assets, or any reclassification, recapitalization or change of outstanding shares of our common stock or adopt a plan of liquidation and dissolution (an extraordinary transaction) unless the holders of units will receive, or have the opportunity to receive, at least the same consideration per unit as holders of our common stock receive per share of common stock in the transaction. If holders of units will not be treated in this manner in connection with a proposed extraordinary transaction, we cannot engage in such a transaction unless limited partners (other than us) holding more than 50% of the units held by limited partners vote to approve the extraordinary transaction.

We may also engage in an extraordinary transaction without the consent or approval of the limited partners if we engage in a merger, or other combination of assets with another entity and:

substantially all of the assets of the surviving entity are held directly or indirectly by the operating partnership or another limited partnership or limited liability company which is the surviving partnership of a merger, consolidation or combination of assets with the operating partnership;

the rights, preferences and privileges of such unit holders in the surviving partnership are at least as favorable as those in effect immediately prior to the consummation of the transaction and as those applicable to any other limited partners or non-managing members of the surviving partnership; and

the limited partners may exchange their units in the surviving partnership for either the same consideration per unit as holders of our common stock receive per share of common stock in the transaction, or if the ultimate controlling person of the surviving partnership has common equity securities, at an exchange ratio based on the relative fair market value of those securities and our common stock.

Term

The operating partnership will continue in full force and effect until 2104, or until sooner dissolved in accordance with the terms of the Partnership Agreement or as otherwise provided by law.

Exculpation and Indemnification of the General Partner

The Partnership Agreement generally provides that we will incur no liability to the operating partnership or any limited partner for losses sustained or liabilities incurred as a result of errors in judgment or mistakes of fact or law or of any act or omission unless we acted in bad faith and the act or omission was material to the matter giving rise to the loss or liability. In addition, we are not responsible for any misconduct or negligence on the part of our agents, provided we appointed our agents in good faith. We may consult with legal counsel, accountants, appraisers, management consultants, investment bankers and other consultants and advisors, and any action we may take or omit to take in reliance upon the opinion of such persons, as to matters that we reasonably believe to be within such persons professional or expert competence, shall be conclusively presumed to have been done or omitted in good faith and in accordance with such opinion. The Partnership Agreement also provides for indemnification of us, our directors and officers, limited partners and such other persons as we may from time to time designate against any losses, claims, damages, judgments, penalties, fines, settlements and reasonable expenses actually incurred by such person in connection with the preceding unless it is established that:

- the act or omission of the indemnitee was material to the matter giving rise to the proceeding and either was committed in bad faith or was the result of active and deliberate dishonesty;

- the indemnitee actually received an improper personal benefit in money, property or services; or

- in the case of any criminal proceeding, the indemnitee had reasonable cause to believe that the act or omission was unlawful.

INVESTMENT POLICIES

The following is a discussion of our investment policies. These policies may be amended or revised from time to time at the discretion of our board of directors, without a vote of our stockholders. Any change to any of these policies by our board, however, would be made only after a thorough review and analysis of that change, in light of then-existing business and other circumstances, and then only if, in the exercise of its business judgment, our board of directors believes that a change is in our and our stockholders best interests. We cannot assure you that our investment objectives will be attained.

Investments in Real Estate or Interests in Real Estate

We are a lodging-focused real estate company that owns premium hotels and resorts, located throughout the United States. We conduct our business through a traditional umbrella partnership REIT, or UPREIT, in which our hotels are owned by subsidiaries of our operating partnership. We are the sole general partner of our operating partnership and currently own, either directly or indirectly, all of the limited partnership units of our operating partnership. We seek to invest in assets primarily for current income generation; however, during the current recession, our corporate goals and objectives are focused on preserving and enhancing our liquidity. In general, our primary investment objectives are to:

- enhance stockholder value over time by generating strong risk-adjusted returns on invested capital;
- pay distributions to our stockholders, where such distributions do not conflict with our liquidity strategy; and
- achieve long-term appreciation in the value of our hotel property investments through innovative investment management strategies, such as rebranding, renovating and repositioning our hotels.

There are no limitations on the amount or percentage of our total assets that may be invested in any one hotel property. Additionally, no limits have been set on the concentration of investments in any one location or by brand, type of market or other limits. Furthermore, other than the financial covenants under our corporate credit facility or property-level debt, there are no limitations on the number of mortgages that may be placed on any one piece of property.

Additional criteria with respect to our hotel property investments is described in our Annual Report on Form 10-K for the fiscal year ended December 31, 2008 under the caption Our Business.

Investments in Real Estate Mortgages, Structured Financings and Other Lending Policies

We have no current intention of investing in loans secured by properties or making loans to persons. However, we do not have a policy limiting our ability to invest in loans secured by properties or to make loans to other persons. In the future, we may acquire first mortgages on hotel properties and invest in other mortgage-related instruments such as subordinated or mezzanine loans to hotel owners and operators. In addition, we may invest in hotel properties and lease them back to their existing owners. We may also consider offering purchase money financing in connection with the sale of properties where the provision of that financing will increase the value to be received by us for the property sold. We may make loans to joint ventures in which we may participate in the future. However, we do not intend to engage in significant lending activities. Any such lending or financing activities would be subject to restrictions applicable to REITs.

Investments in Securities of or Interests in Persons Primarily Engaged in Real Estate Activities and Other Issuers

Generally, we do not expect to engage in any significant investment activities with other entities, although we may consider joint venture investments with other investors. We may also invest in the securities of other issuers in connection with acquisitions of indirect interests in hotel properties (normally general or limited partnership units in special purpose partnerships owning properties). We may in the future acquire some, all or substantially all of the securities or assets of other REITs or similar entities where that investment would be consistent with our investment policies and the REIT qualification requirements. There are no limitations on the amount or percentage of our total assets that may be invested in any one issuer, other than those imposed by the gross income and asset tests that we must satisfy to qualify as a REIT. However, we do not anticipate investing in other issuers of securities for the purpose of exercising control or acquiring any investments primarily for sale in the ordinary course of business or holding any investments with a view to making short-term profits from their sale. In any event, we do not intend that our investments in securities will require us to register as an investment company under the Investment Company Act of 1940, and we intend to divest securities before any registration would be required.

We do not intend to engage in trading, underwriting, agency distribution or sales of securities of other issuers.

FEDERAL INCOME TAX CONSIDERATIONS RELATED TO OUR REIT ELECTION

The following summary outlines certain U.S. federal income tax considerations related to our REIT status which we anticipate to be material to holders of our securities. This summary does not attempt to address any aspects of federal income taxation that may be relevant to your ownership of our securities. Instead, the material federal income tax considerations relating to your ownership and sale or other disposition of our securities will be provided in the applicable prospectus supplement that relates to those securities. Your tax treatment will vary depending upon the terms of the specific securities that you acquire, as well as your particular situation. Moreover, this summary does not address any foreign, state, or local tax consequences of our election to be taxed as a REIT. The provisions of the Code concerning the federal income tax treatment of a REIT are highly technical and complex; the following discussion sets forth only certain aspects of those provisions. This summary is intended to provide you with general information only and is not intended as a substitute for careful tax planning.

This summary is based on provisions of the Code, applicable final and temporary Treasury Regulations, judicial decisions, and administrative rulings and practice, all in effect as of the date of this prospectus, and should not be construed as legal advice. No assurance can be given that future legislative or administrative changes or judicial decisions will not affect the accuracy of the descriptions or conclusions contained in this summary. In addition, any such changes may be retroactive and apply to transactions entered into prior to the date of their enactment, promulgation or release. We do not expect to seek a ruling from the Internal Revenue Service, or IRS, regarding any of the federal income tax issues discussed in this prospectus, and no assurance can be given that the IRS will not challenge any of the positions we take and that such a challenge will not succeed. ***Prospective purchasers of our securities are urged to consult their own tax advisors prior to any investment in our securities concerning the potential federal, state, local, and foreign tax consequences of the investment with specific reference to their own tax situations. Prospective purchasers also are urged to refer to the applicable prospectus supplement for any amendments or changes to this summary.***

Except as otherwise noted, references in this discussion of Federal Income Tax Considerations Related to Our REIT Election to we, our, us and our company refer to DiamondRock Hospitality Company and not our taxable REIT subsidiaries.

Taxation of Our Company

We have elected to be taxed as a REIT starting with the calendar year ended December 31, 2005 and for subsequent taxable years. We decided to be taxed as a C corporation for 2004 and defer the REIT election until 2005. Beginning January 1, 2005, we believe we have qualified as a REIT, and except as otherwise noted, the following discussion assumes that we qualify as a REIT effective January 1, 2005.

In connection with this filing, we will receive an opinion of Goodwin Procter LLP that, commencing with our taxable year ended December 31, 2005, we have been organized and operated in conformity with the requirements for qualification and taxation as a REIT under the Code and our current and proposed ownership and operations will allow us to satisfy the requirements for qualification and taxation as a REIT under the Code for subsequent taxable years. The opinion of Goodwin Procter LLP will be based on various assumptions and on our representations to Goodwin Procter LLP concerning our current and continuing organization, our prior, current and proposed ownership and operations, and our stockholders current and future relationships with our hotel management companies, and other matters relating to our ability to qualify as a REIT. The opinion will be expressly conditioned upon the accuracy of such assumptions and representations, which Goodwin Procter LLP will not verify. Moreover, our qualification and taxation as a REIT will depend upon our ability to meet, through actual annual operating results, distribution levels, diversity of stock ownership and the absence of prohibited relationships with our hotel management companies, the various and complex REIT qualification tests imposed under the Code, the results of which will not be reviewed or verified by Goodwin Procter LLP. See Qualification as a REIT below. Accordingly, no assurance can be given that we will in fact satisfy such requirements. The opinion of Goodwin Procter LLP will be based upon current law, which is subject to change either prospectively or retroactively. Changes in applicable law could modify the conclusions expressed in the opinion. Moreover, unlike a ruling from the IRS, an opinion of Goodwin Procter LLP is not binding on the IRS, and no assurance can be given that the IRS could not successfully challenge our status as a REIT.

If we qualify as a REIT, we generally will be allowed to deduct dividends paid to our stockholders, and, as a result, we generally will not be subject to federal income tax on that portion of our ordinary income or net capital gain that we currently distribute to our stockholders. We expect to make distributions to our stockholders on a regular basis as necessary to avoid material federal income tax and to comply with the REIT requirements. See Qualification as a REIT Annual Distribution Requirements below.

Notwithstanding the foregoing, even if we qualify for taxation as a REIT, we nonetheless may be subject to federal income tax in certain circumstances, including the following:

We will be required to pay federal income tax on our undistributed taxable income, including net capital gain;

We may be subject to the alternative minimum tax;

We may be subject to tax at the highest corporate rate on certain income from foreclosure property (generally, property acquired by reason of default on a lease or indebtedness held by us);

We will be subject to a 100% federal income tax on net income from prohibited transactions (generally, certain sales or other dispositions of property, sometimes referred to as dealer property, held primarily for sale to customers in the ordinary course of business) unless such property has been held by us for two years (four years if such property was sold before July 30, 2008) and certain other requirements are satisfied or the gain is realized in a TRS;

If we fail to satisfy the 75% gross income test or the 95% gross income test (discussed below), but nonetheless maintain our qualification as a REIT pursuant to certain relief provisions, we will be subject to a 100% federal income tax on the greater of (i) the amount by which we fail the 75% gross income test or (ii) the amount by which we fail the 95% gross income test, multiplied by a fraction intended to reflect our profitability;

If we fail to satisfy any of the asset tests, other than the 5% or the 10% asset tests that qualify under the De Minimis Exception, and the failure qualifies under the General Exception, as described below under Qualification as a REIT Asset Tests, then we will have to pay an excise tax equal to the greater of (i) $50,000 and (ii) an amount determined by multiplying the net income generated during a specified period by the assets that caused the failure by the highest federal income tax applicable to corporations;

If we fail to satisfy any REIT requirements other than the income test or asset test requirements, described below under Qualification as a REIT Income Tests and Qualification as a REIT Asset Tests, respectively, and we qualify for a reasonable cause exception, then we will have to pay a penalty equal to $50,000 for each such failure;

We will be subject to a 4% excise tax if certain distribution requirements are not satisfied;

Because we were a C corporation for our taxable year ended December 31, 2004, we generally will be subject to a corporate-level tax on a taxable disposition of any appreciated asset we hold as of the effective date of our REIT election, which was January 1, 2005. Specifically, if we dispose of a built-in-gain asset in a taxable transaction prior to tenth anniversary of the effective date of our REIT election, we would be subject to tax at the highest regular corporate rate (currently 35%) on the lesser of the gain recognized and the asset s built-in-gain;

If we dispose of an asset acquired by us from a C corporation in a transaction in which we took the C corporation s tax basis in the asset, we may be subject to tax at the highest regular corporate rate on the appreciation inherent in such asset as of the date of acquisition by us;

We will be required to pay a 100% tax on any redetermined rents, redetermined deductions, and excess interest. In general, redetermined rents are rents from real property that are overstated as a result of services furnished to any of our non-TRS tenants by one of our TRSs. Redetermined deductions and excess interest generally represent amounts that are deducted by a TRS lessee or other TRS for amounts paid to us that are in excess of the amounts that would have been deducted based on arm s-length negotiations; and

Income earned by our TRS lessees, Bloodstone TRS, Inc. and certain other TRSs will be subject to tax at regular corporate rates.

No assurance can be given that the amount of any such federal income taxes will not be substantial. We note that the assets we acquired during 2004 were acquired on or after October 27, 2004, and we do not believe the built-in gain in such assets as of January 1, 2005 was material. Accordingly, we do not expect to be subject to significant corporate tax liabilities if we decide to sell an asset we acquired in 2004 within the 10-year period following the effective date of our REIT election.

Qualification as a REIT

In General

The REIT provisions of the Code apply to a domestic corporation, trust, or association (i) that is managed by one or more trustees or directors, (ii) the beneficial ownership of which is evidenced by transferable shares or by transferable certificates of beneficial interest, (iii) that properly elects to be taxed as a REIT, (iv) that is neither a financial institution nor an insurance company, (v) that uses a calendar year for federal income tax purposes and complies with applicable recordkeeping requirements, and (vi) that meets the additional requirements discussed below.

Ownership Tests

Commencing with our second REIT taxable year, which was the calendar year ended December 31, 2006, (i) the beneficial ownership of our common stock must be held by 100 or more persons during at least 335 days of a 12-month taxable year (or during a proportionate part of the taxable year of less than 12 months) for each of our taxable years and (ii) during the last half of each taxable year, no more than 50% in value of our stock may be owned, directly or indirectly, by or for five or fewer individuals (the 5/50 Test). Stock ownership for purposes for the 5/50 Test is determined by applying the constructive ownership provisions of Section 544(a) of the Code, subject to certain modifications. The term individual for purposes of the 5/50 Test includes a private foundation, a trust providing for the payment of supplemental unemployment compensation benefits, and a portion of a trust permanently set aside or to be used exclusively for charitable purposes. A qualified trust described in Section 401(a) of the Code and exempt from tax under Section 501(a) of the Code generally is not treated as an individual; rather, shares held by it are treated as owned proportionately by its beneficiaries. However, if (i) treating qualified trusts as individuals would cause us to fail the 5/50 Test and (ii) we are predominantly held by qualified trusts, we will be treated as a pension-held REIT. We will be predominantly held by qualified trusts if either (i) a single qualified trust holds more than 25% by value of our stock or (ii) one or more qualified trusts, each owning more than 10% by value of our stock, hold in the aggregate more than 50% by value of our stock. In the event we are a pension held REIT, a qualified trust owning 10% or more of our shares should expect to recognize UBTI as a result of its investment. We cannot assure you that we will never be treated as a pension held REIT. Before making an investment in shares of our common stock, a tax-exempt stockholder should consult its own tax advisors with regard to UBTI and the suitability of the investment in our stock.

We believe we have issued sufficient common stock to satisfy the above ownership requirements. In addition, our charter restricts ownership and transfers of our stock that would violate these requirements, although these restrictions may not be effective in all circumstances to prevent a violation. We will be deemed to have satisfied the

5/50 Test for a particular taxable year if we have complied with all the requirements for ascertaining the ownership of our outstanding stock in that taxable year and have no reason to know that we have violated the 5/50 Test.

Income Tests

In order to maintain qualification as a REIT, we must annually satisfy two gross income requirements:

1) First, at least 75% of our gross income (excluding gross income from prohibited transactions and certain other income and gains as described below) for each taxable year must be derived, directly or indirectly, from investments relating to real property or mortgages on real property or from certain types of temporary investments (or any combination thereof). Qualifying income for the purposes of this 75% gross income test generally includes: (a) rents from real property, (b) interest on debt secured by mortgages on real property or on interests in real property, (c) dividends or other distributions on, and gain from the sale of, shares in other REITs, (d) gain from the sale of real estate assets (other than gain from prohibited transactions), (e) income and gain derived from foreclosure property, and (f) income from certain types of temporary investments; and

2) Second, in general, at least 95% of our gross income (excluding gross income from prohibited transactions and certain other income and gains as described below) for each taxable year must be derived from the real property investments described above and from other types of dividends and interest, gain from the sale or disposition of stock or securities that are not dealer property, or any combination of the above.

For purposes of the 75% and the 95% gross income tests, we are treated as receiving our proportionate share of our operating partnership s gross income.

If we fail to satisfy one or both of the 75% or the 95% gross income tests, we may nevertheless qualify as a REIT for a particular year if we are entitled to relief under certain provisions of the Code. Those relief provisions generally will be available if our failure to meet such tests is due to reasonable cause and not due to willful neglect and we file a schedule describing each item of our gross income for such year(s) in accordance with the applicable Treasury Regulations. It is not possible, however, to state whether in all circumstances we would be entitled to the benefit of these relief provisions. As discussed above in Taxation of Our Company, even if these relief provisions were to apply, we would be subject to federal income tax with respect to our excess net income.

Foreclosure property. Foreclosure property is real property (including interests in real property) and any personal property incident to such real property (1) that is acquired by a REIT as a result of the REIT having bid in the property at foreclosure, or having otherwise reduced the property to ownership or possession by agreement or process of law, after there was a default (or default was imminent) on a lease of the property or a mortgage loan held by the REIT and secured by the property, (2) for which the related loan or lease was made, entered into or acquired by the REIT at a time when default was not imminent or anticipated and (3) for which such REIT makes an election to treat the property as foreclosure property. REITs generally are subject to tax at the maximum corporate rate (currently 35%) on any net income from foreclosure property, including any gain from the disposition of the foreclosure property, other than income that would otherwise be qualifying income for purposes of the 75% gross income test. Any gain from the sale of property for which a foreclosure property election has been made will not be subject to the 100% tax on gains from prohibited transactions described above, even if the property is held primarily for sale to customers in the ordinary course of a trade or business.

Hedging transactions. We may enter into hedging transactions with respect to one or more of our assets or liabilities. Hedging transactions could take a variety of forms, including interest rate swaps or cap agreements, options, futures contracts, forward rate agreements or similar financial instruments. Except to the extent as may be provided by future Treasury Regulations, any income from a hedging transaction which is clearly identified as such before the close of the day on which it was acquired, originated or entered into, including gain from the disposition or termination of such a transaction, will not constitute gross income for purposes of the 95% and 75% gross income tests, provided that the hedging transaction is entered into after July 30, 2008 (i) in the normal course of our business primarily to manage risk of interest rate or price changes or currency fluctuations with respect to indebtedness incurred or to be incurred by us to acquire or carry real estate assets or (ii) primarily to manage the risk of currency fluctuations with respect to any item of income or gain that would be qualifying income under the 75% or 95% income tests (or any property which generates such income or gain). To the extent we enter into other types of hedging transactions, the income from those transactions is likely to be treated as non-qualifying income for purposes of both the 75% and 95% gross income tests. Prior to July 30, 2008, the rules applicable to hedging transactions were more restrictive. We intend to structure any hedging transactions in a manner that does not jeopardize our ability to qualify as a REIT.

Foreign Currency Gains. In addition to the Frenchman s Reef & Morning Star Marriott Beach Resort, we may acquire other properties located outside of the United States in the future, through a taxable REIT subsidiary or otherwise. We do not have any foreign currency gains in connection with our investment in Frenchman s Reef & Morning Star Marriott Beach Resort. Any foreign currency gains recognized after July 30, 2008, to the extent attributable to specified assets or items of qualifying income or gain for purposes of the 75% or 95% gross income test, generally will not constitute gross income for purposes of the applicable test, and therefore will be exempt from such test, provided we do not deal in or engage in substantial and regular trading in securities, which we do not intend to do.

Hotels

Operating revenues from our hotels are not qualifying income for purposes of either the 75% or the 95% gross income test. Accordingly, in order for us to generate qualifying income with respect to our hotel investments under the REIT rules, we must master-lease our hotels. Specifically, our operating partnership has formed a subsidiary, Bloodstone TRS, Inc., that has elected to be treated as our TRS and may, in the future, form other subsidiaries that elect to be treated as our TRSs. Bloodstone TRS, Inc. has formed subsidiaries (each a TRS lessee) that master-lease hotels from the operating partnership (or subsidiaries of the operating partnership). We expect to form additional TRS lessees (under Bloodstone TRS, Inc. or other of our TRSs) as we acquire additional properties. In certain instances we may own a hotel through a TRS. For example, we have elected to treat DiamondRock Frenchman s Owner, Inc., through which we hold the Frenchman s Reef & Morning Star Marriott Beach Resort, as a TRS and we may hold other non-U.S. investments through TRSs. One or more hotel management companies will manage the hotels leased to each TRS lessee or owned by a TRS. We also may lease a hotel to an unrelated lessee.

In general, rent paid by a related party tenant, such as a TRS lessee, is not qualifying rents from real property for purposes of the REIT gross income tests, but rent paid by a TRS lessee to our operating partnership with respect to a lease of a qualified lodging facility from the operating partnership can be qualifying rents from real property under the REIT rules as long as such TRS lessee does not directly or indirectly operate or manage any hotel or provide rights to any brand name under which any hotel is operated. Instead, the hotel must be operated on behalf of the TRS lessee by a person who qualifies as an eligible independent contractor, defined as an independent contractor who is, or is related to a person who is, actively engaged in the trade or business of operating qualified lodging facilities for any person unrelated to us and the TRS lessee. See Investments in Taxable REIT Subsidiaries below for a further discussion of the issue and a discussion of the definition of an independent contractor and the qualification of Marriott (or another hotel management company) as an eligible independent contractor. A qualified lodging facility is a hotel, motel, or other establishment more than one-half of the dwelling units in which are used on a transient basis, provided that wagering activities are not conducted at or in connection with such facility by any person who is engaged in the business of accepting wagers and who is legally authorized to engage in such business at or in connection with such facility. A qualified lodging facility includes customary amenities and facilities operated as part of, or associated with, the lodging facility as long as such amenities and facilities are customary for other properties of a comparable size and class owned by other unrelated owners. We believe that our hotels are qualified lodging facilities. Rent paid by a TRS lessee that failed to qualify as rents from real property under the REIT rules would be non-qualifying income for purposes of the REIT gross income tests.

Two other limitations may affect our ability to treat rent paid by a TRS lessee or other lessee as qualifying rents from real property under the REIT rules. If the rent attributable to personal property leased by the TRS lessee (or other lessee) in connection with a lease of real property is greater than 15% of the total rent under the lease, then the portion of the rent attributable to such personal property will not qualify as rents from real property. Also, an amount received or accrued will not qualify as rents from real property for purposes of either the 75% or the 95% gross income test if it is based in whole or in part on the income or profits derived by any person from such property. However, an amount received or accrued will not be excluded from rents from real property solely by reason of being based on a fixed percentage or percentages of receipts or sales. To comply with the limitation on rents attributable to personal property, a TRS lessee may acquire furnishings, equipment, and/or personal property used in hotel, at least to the extent that they exceed this 15% limit. To comply with the prohibition on rent based on net income, the leases will provide that each TRS lessee is obligated to pay our operating partnership a minimum base rent together with a gross percentage rent, at rates intended to equal market rental rates.

In addition, rent paid by a TRS lessee or other lessee that leases a hotel from our operating partnership will constitute rents from real property for purposes of the REIT gross income tests only if the lease is respected as a true lease for federal income tax purposes and is not treated as a service contract, joint venture, or some other type of arrangement. The determination of whether a lease is a true lease depends upon an analysis of all the surrounding facts and circumstances. We believe that the leases with our TRS lessees should be treated as true leases. However, that there are no controlling regulations, published administrative rulings, or judicial decisions involving leases with terms substantially similar to the leases between our operating partnership and the TRS lessees that discuss whether the leases constitute true leases for federal income tax purposes. Thus, there can be no assurance that the IRS will not assert a contrary position and that a court will not sustain such a challenge. If any leases between our operating partnership and a TRS lessee are re-characterized as service contracts or partnership agreements, rather than as true leases, part or all of the payment that we receive from such TRS lessee would not be considered rent or would otherwise fail the various requirements for qualification as rents from real property.

Finally, for rents received by or attributed to us to qualify as rents from real property, we generally must not furnish or render any services to tenants, other than through a TRS or an independent contractor from whom we derive no income, except that we and our operating partnership may directly provide services that are usually or customarily rendered in connection with the rental of properties for occupancy only, or are not otherwise considered rendered to the occupant for his convenience. Neither we nor our operating partnership provides, or intends to provide, any services to our TRSs, TRS lessees or any other tenants.

We believe that, for purposes of both the 75% and the 95% gross income tests, our operating partnership s investments in hotels generally give rise to qualifying income in the form of rents from real property, and that gains on the sales of the hotels will also constitute qualifying income. However, no assurance can be given that either the rents or the gains will constitute qualifying income. In that case, we may not be able to satisfy either the 75% or the 95% gross income test and, as a result, could lose our REIT status.

We hold the Frenchman s Reef & Morning Star Marriott Beach Resort through a Cayman Islands corporation that holds a U.S. Virgin Islands corporation that we have elected to be treated as our TRS. In the case of hotels owned, rather than leased, by a TRS, dividends paid by such TRS out of its earnings and gains from the sale of stock of such a TRS would not be qualifying income for purposes of the 75% gross income test, although such dividends and gains would be qualifying income for purposes of the 95% gross income test.

Asset Tests

At the close of each quarter of our taxable year, we must also satisfy four tests relating to the nature of our assets. First, real estate assets, cash and cash items, and government securities must represent at least 75% of the value of our total assets. Second, not more than 25% of our total assets may be represented by securities other than those in the 75% asset class. Third, of the investments that are not included in the 75% asset class and that are not securities of our TRS lessees or other TRSs, (i) the value of any one issuer s securities owned by us may not exceed 5% of the value of our total assets and (ii) we may not own more than 10% by vote or by value of any one issuer s outstanding securities. For purposes of the 10% value test, debt instruments issued by a partnership are not classified as securities to the extent of our interest as a partner in such partnership (based on our proportionate share of the partnership s equity interests and certain debt securities) or if at least 75% of the partnership s gross income, excluding income from prohibited transactions, is qualifying income for purposes of the 75% gross income test. For purposes of the 10% value test, the term securities also does not include debt securities issued by another REIT, certain straight debt securities (for example, qualifying debt securities of a corporation of which we own no more than a de minimis amount of equity interest), loans to individuals or estates, and accrued obligations to pay rent. Fourth, securities of our TRS lessees or other TRSs cannot represent more than 25% (20% for taxable years beginning before July 31, 2008) of our total assets. Although we believe that we have met and intend to continue to meet these asset tests, no assurance can be given that we will be able to do so. For purposes of these asset tests, we are treated as holding our proportionate share of our operating partnership s assets.

We will monitor the status of our assets for purposes of the various asset tests and will endeavor to manage our portfolio in order to comply at all times with such tests. If we fail to satisfy the asset tests at the end of a calendar quarter, we will not lose our REIT status if one of the following exceptions applies:

We satisfied the asset tests at the end of the preceding calendar quarter, and the discrepancy between the value of our assets and the asset test requirements arose from changes in the market values of our assets and was not wholly or partly caused by the acquisition of one or more non-qualifying assets; or

We eliminate any discrepancy within 30 days after the close of the calendar quarter in which it arose.

Moreover, if we fail to satisfy the asset tests at the end of a calendar quarter during a taxable year, we will not lose our REIT status if one of the following additional exceptions applies:

De Minimis Exception: The failure is due to a violation of the 5% or 10% asset tests referenced above and is de minimis (meaning that the failure is one that arises from our ownership of assets the total value of which does not exceed the lesser of 1% of the total value of our assets at the end of the quarter in which the failure occurred and $10 million), and we either dispose of the assets that caused the failure or otherwise satisfy the asset tests within 6 months after our identification of the failure; or

General Exception: All of the following requirements are satisfied: (i) the failure is not due to a de minimis violation of the 5% or 10% asset tests (as defined above), (ii) the failure is due to reasonable cause and not willful neglect, (iii) we file a schedule in accordance with Treasury Regulations providing a description of each asset that caused the failure, (iv) we either dispose of the assets that caused the failure or otherwise satisfy the asset tests within 6 months after the last day of the quarter in which our identification of the failure occurred, and (v) we pay an excise tax as described above in Taxation of Our Company.

Annual Distribution Requirements

In order to qualify as a REIT, we must distribute dividends (other than capital gain dividends) to our stockholders in an amount at least equal to (A) the sum of (i) 90% of our REIT taxable income (determined without regard to the dividends paid deduction and by excluding any net capital gain) and (ii) 90% of the net income (after tax), if any, from foreclosure property, minus (B) the sum of certain items of non-cash income. We generally must pay such distributions in the taxable year to which they relate, or in the following taxable year if declared before we timely file our tax return for such year and if paid on or before the first regular dividend payment after such declaration. We may satisfy our distribution requirement in part by paying a taxable stock dividend.

To the extent that we do not distribute all of our net capital gain and REIT taxable income, we will be subject to tax on the undistributed amount at corporate capital gains and ordinary tax rates, respectively. Furthermore, if we should fail to distribute during each calendar year at least the sum of (i) 85% of our ordinary income for such year, (ii) 95% of our capital gain net income for such year, and (iii) any undistributed ordinary income and capital gain net income from prior periods, we will be subject to a 4% nondeductible excise tax on the excess of such required distribution over the amounts actually distributed.

Under certain circumstances, we may be able to rectify a failure to meet the distribution requirement for a year by paying deficiency dividends to our stockholders in a later year that may be included in our deduction for dividends paid for the earlier year. Thus, we may be able to avoid being taxed on amounts distributed as deficiency dividends;

however, we will be required to pay interest based upon the amount of any deduction taken for deficiency dividends.

In addition, dividends we pay must not be preferential. If a dividend is preferential, it will not qualify for the dividends paid deduction. To avoid paying preferential dividends, we must treat every stockholder of the class of stock with respect to which we make a distribution the same as every other stockholder of that class, and we must not treat any class of stock other than according to its dividend rights as a class.

We may retain and pay income tax on net long-term capital gains we received during the tax year. To the extent we so elect, (i) each stockholder must include in its income (as long-term capital gains) its proportionate share of our undistributed long-term capital gains, (ii) each stockholder s basis in its shares of our stock is increased by the included amount of the undistributed long-term capital gains, and (iii) each stockholder is deemed to have paid, and receives a credit for, its proportionate share of the tax paid by us on the undistributed long-term capital gains.

To qualify as a REIT, we may not have, at the end of any taxable year, any undistributed earnings and profits accumulated in any non-REIT taxable year. Our non-REIT earnings and profits include any earnings and profits we accumulated before the effective date of our REIT election, which was January 1, 2005. We distributed sufficient earnings and profits before December 31, 2005 to eliminate any non-REIT earnings and profits, which distributions were in addition to distributions we were required to make to satisfy the 90% distribution test (as discussed above) and avoid incurring tax on our undistributed income.

Failure to Qualify

If we fail to qualify as a REIT and such failure is not an asset test or income test failure, we generally will be eligible for a relief provision if the failure is due to reasonable cause and not willful neglect and we pay a penalty of $50,000 with respect to such failure.

If we fail to qualify for taxation as a REIT in any taxable year and no relief provisions apply, we generally will be subject to tax (including any applicable alternative minimum tax) on our taxable income at regular corporate rates. Distributions to our stockholders in any year in which we fail to qualify as a REIT will not be deductible by us nor will they be required to be made. In such event, to the extent of current or accumulated earnings and profits, all distributions to our stockholders will be taxable as dividend income. Subject to certain limitations in the Code, corporate stockholders may be eligible for the dividends received deduction, and individual, trust and estate stockholders may be eligible to treat the dividends received from us as qualified dividend income taxable as net capital gains, under the provisions of Section 1(h)(11) of the Code, through the end of 2010. Unless entitled to relief under specific statutory provisions, we also will be ineligible to elect REIT status again prior to the fifth taxable year following the first year in which we failed to qualify as a REIT under the Code.

Our qualification as a REIT for federal income tax purposes will depend on our continuing to meet the various requirements summarized above governing the ownership of our outstanding shares, the nature of our assets, the sources of our income, and the amount of our distributions to our stockholders. Although we intend to operate in a manner that will enable us to comply with such requirements, there can be no certainty that such intention will be realized. In addition, because the relevant laws may change, compliance with one or more of the REIT requirements may become impossible or impracticable for us.

Qualified REIT Subsidiaries and Disregarded Entities

If we own a corporate subsidiary that is a qualified REIT subsidiary (QRS), or if we or our operating partnership own 100% of the membership interests in a limited liability company or other unincorporated entity that does not elect to be treated as a corporation for federal income tax purposes, the separate existence of the QRS, limited liability company or other unincorporated entity generally will be disregarded for federal income tax purposes. Generally, a QRS is a corporation, other than a TRS, all of the stock of which is owned by a REIT. A limited liability company or other unincorporated entity 100% owned by a single member that does not elect to be treated as a corporation for federal income tax purposes generally is disregarded as an entity separate from its owner for federal income tax purposes. All assets, liabilities, and items of income, deduction, and credit of the QRS or disregarded entity will be treated as assets, liabilities, and items of income, deduction, and credit of its owner. If we own a QRS or a disregarded entity, neither will be subject to federal corporate income taxation, although such entities may be subject to state and local taxation in some states.

Taxation of the Operating Partnership

Our operating partnership currently is a disregarded entity because we own 100% of the interests in it, directly or through other disregarded entities. If we admit other limited partners, our operating partnership will be treated as a partnership for tax purposes, as described below.

Under the Code, a partnership is not subject to federal income tax, but is required to file a partnership tax information return each year. In general, the character of each partner s share of each item of income, gain, loss, deduction, credit, and tax preference is determined at the partnership level. Each partner is then allocated a distributive share of such items in accordance with the partnership agreement and is required to take such items into account in determining the partner s income. Each partner includes such amount in income for any taxable year of the partnership ending within or with the taxable year of the partner, without regard to whether the partner has received or will receive any cash distributions from the partnership. Cash distributions, if any, from a partnership to a partner generally are not taxable unless and to the extent they exceed the partner s basis in its partnership interest immediately before the distribution. Any amounts in excess of such tax basis will generally be treated as a sale of such partner s interest in the partnership.

If and when our operating partnership becomes taxable as a partnership, rather than a disregarded entity, we generally will be treated for federal income tax purposes as contributing our properties to the operating partnership at such time. If our properties are appreciated at such time, we could recognize a smaller share of tax depreciation, and a larger share of tax gain on sale, from such properties subsequent to that deemed contribution, as compared to our percentage interest in the operating partnership. This deemed contribution also could trigger tax gain in some circumstances, but we expect to structure the admission of outside partners in a manner that should avoid any such gain.

As noted above, for purposes of the REIT income and asset tests, we are treated as holding or receiving our proportionate share of our operating partnership s income and assets, respectively. We control, and intend to continue to control, our operating partnership and intend to operate it consistently with the requirements for our qualification as a REIT.

We may use our operating partnership to acquire hotels in exchange for operating partnership units, in order to permit the sellers of such properties to defer recognition of their tax gain. In such a transaction, our initial tax basis in the hotels acquired generally will be less than the purchase price of the hotels. Consequently, our depreciation deductions for such properties may be less, and our tax gain on a sale of such properties may be more, than the deductions or gain, respectively, that we would have if we acquired these properties in taxable transactions. In addition, we may issue equity compensation to employees in the form of interests in our operating partnership that provides for capital gain treatment to the employees but does not generate a corresponding deduction for our operating partnership.

The discussion above assumes that our operating partnership will be treated as a partnership for federal income tax purposes once it is no longer treated as a disregarded entity. Generally, a domestic unincorporated entity such as our operating partnership with two or more partners is treated as a partnership for federal income tax purposes unless it affirmatively elects to be treated as a corporation. However, certain publicly traded partnerships are treated as corporations for federal income tax purposes. Once our operating partnership is no longer a disregarded entity for federal income tax purposes, we intend to comply with one or more exceptions from treatment as a corporation under the publicly traded partnership rules. Failure to qualify for such an exception would prevent us from qualifying as a REIT.

Investments in Taxable REIT Subsidiaries

We and each subsidiary intended to qualify as a TRS have made (or will make, as applicable) a joint election for such subsidiary to be treated as our taxable REIT subsidiary. A domestic TRS (or a foreign TRS with income from a U.S. business) pays federal, state, and local income taxes at the full applicable corporate rates on its taxable income prior to payment of any dividends. Thus, for example, Bloodstone TRS, Inc. generally will pay U.S. corporate tax on key money and yield support when it is paid, notwithstanding the treatment of key money and yield support payments for accounting purposes. A TRS owning or leasing a hotel outside of the U.S., such as DiamondRock Frenchman s Owner, Inc., may pay foreign taxes. The taxes owed by our TRSs could be substantial. To the extent that our TRSs are required to pay federal, state, local, or foreign taxes, the cash available for distribution by us will be reduced accordingly.

A TRS is permitted to engage in certain kinds of activities that cannot be performed directly by us without jeopardizing our REIT status. A TRS is subject to limitations on the deductibility of payments made to us which could materially increase its taxable income and also is subject to prohibited transaction taxes on certain other payments made, directly or indirectly, to us. We will be subject to a 100% tax on the amounts of any rents from real property, deductions, or excess interest received from a TRS that would be reduced through reapportionment under Section 482 of the Code in order to more clearly reflect the income of the TRS. In particular, this 100% tax would apply to our share of any rent paid by a TRS lessee that was determined to be in excess of a market rate rent.

As discussed above in Qualification as a REIT Income Tests, Bloodstone TRS, Inc., through our TRS lessees, leases qualified lodging facilities from our operating partnership (or its affiliates) and a TRS may own hotels (such as DiamondRock Frenchman s Owner, Inc. that owns Frenchman s Reef & Morning Star Marriott Beach Resort). However, a TRS may not directly or indirectly operate or manage any hotel or provide rights to any brand name under which any hotel is operated. Specifically, rents paid by a TRS lessee can qualify as rents from real property only so long as the property is operated and managed on behalf of the TRS lessee by an eligible independent contractor, which is a person (or entity) that satisfies the following requirements: (i) such person is, or is related to a person who is, actively engaged in the trade or business of operating qualified lodging facilities for any person unrelated to us or the TRS lessee; (ii) such person does not own, directly or indirectly, more than 35% of our stock; and (iii) not more than 35% of such person is owned, directly or indirectly, by one or more persons owning 35% or more of our stock. For purposes of determining whether these ownership limits are satisfied, actual ownership as well as constructive ownership under the rules of Section 318 of the Code (with certain modifications) is taken into account. For example, (a) interests owned by a partnership are also treated as owned proportionately by its partners, (b) interests held by a partner with a 25% or greater share of partnership capital interests or profits interests are also treated as owned by the partnership, (c) interests held by a 10% or greater stockholder are also treated as held by the corporation, and (d) interests held by a corporation are also treated as held by a 10% or greater stockholder (in the proportion that such stockholder s stock bears to all the stock of the corporation). However, if any class of our stock or the stock of a person attempting to qualify as an eligible independent contractor is regularly traded on an established securities market, only persons who own, directly or indirectly, more than 5% of such class of stock shall be taken into account as owning any of the stock of such class for purposes of applying the 35% limitation described in clause (iii) above. In addition, the IRS has ruled to the effect that an advisor or similar fiduciary to a REIT cannot also qualify as an eligible independent contractor with respect to the REIT.

Each TRS lessee (and any other of our TRSs that owns an interest in our hotels) has hired (or will hire) a hotel management company that we believe qualifies as an eligible independent contractor to manage and operate the hotels leased by (or owned through) the TRS. We believe that Marriott has qualified, and Marriott intends to continue to qualify, as an eligible independent contractor. In that regard, constructive ownership under Section 318 of the Code resulting, for example, from relationships between Marriott and our other stockholder could impact Marriott s ability to satisfy the applicable ownership limit. Because of the broad scope of the attribution rules of Section 318 of the Code, it is possible that not all prohibited relationships will be identified and avoided. The existence of such a relationship would disqualify Marriott (or another hotel management company) as an eligible independent contractor, which would in turn disqualify us as a REIT. Our charter restricts ownership and transfer of our shares in a manner intended to facilitate continuous qualification of Marriott (or another hotel management company) as an eligible independent contractor, but no assurances can be given that such transfer and ownership restrictions have or will ensure that Marriott (or another hotel management company), in fact, has been or will be an eligible independent contractor. As noted above, Goodwin Procter LLP s opinion as to REIT qualification is based upon our representations and covenants as to the absence of such relationships. Marriott s failure to qualify as an eligible independent contractor does not give us the right to terminate the management agreement.

State, Local, and Foreign Tax

We may be subject to state, local and foreign tax in states, localities and foreign countries in which we do business or own property. The tax treatment applicable to us and our stockholders in such jurisdictions may differ from the federal income tax treatment described above.

Stockholders should consult the applicable prospectus supplement, as well as their own tax advisers, for further information about federal, state, local, and other tax consequences of investing in the securities offered by the applicable prospectus supplement.

PLAN OF DISTRIBUTION

We may sell the securities offered by means of this prospectus domestically or abroad, in one or more transactions, including block transactions and transactions on the NYSE or on a delayed or continuous basis:

through underwriters or dealers;

through agents;

directly to one or more purchasers, including our affiliates;

directly to stockholders;

through a combination of any of these methods of sales; or

in any manner, as provided in the applicable prospectus supplement.

In addition, we may issue the securities as a dividend or distribution to our existing securities holders. The prospectus supplement relating to the offer and sale of such securities will include:

the name or names of any underwriters, dealers or agents and the amounts of securities underwritten or purchased by each of them;

the initial public offering price of the securities and the proceeds to us and any discounts, commissions, or concessions allowed or reallowed or paid to dealers; and

any securities exchange on which the securities may be issued.

The securities may be sold at (i) a fixed price or prices which may be changed, (ii) market prices prevailing at the time of sale, (iii) prices related to the prevailing market prices at the time of sale, or (iv) negotiated prices. The consideration may be cash or another form negotiated by the parties.

If we use underwriters for a sale of securities, the securities will be acquired by the underwriters for their own account and may be resold from time to time in one or more transactions. The securities may be offered to the public through underwriting syndicates represented by managing underwriters, or directly by the underwriters. Generally, the underwriters obligation to purchase the securities will be subject to certain conditions precedent. The underwriters will be obligated to purchase all of the securities if they purchase any of the securities. In connection with the sale of securities, underwriters may receive compensation from us or from purchasers of securities for whom the underwriters may acts as agents. Their compensation may be in the form of discounts, concessions or commissions.

Underwriters may sell the securities to or through dealers, and such dealers may receive compensation in the form of discounts, concessions or commissions (which may be changed from time to time) from the underwriters and/or from the purchasers for whom they act as agent.

We may agree to sell the securities to an underwriter for a delayed public offering and may further agree to adjustments before the public offering to the underwriters purchase price for the securities based on changes in the market value of the securities.

Offers to purchase the securities may be solicited by agents designated by us from time to time. Any such agent involved in the offer or sale of securities will be set forth in the prospectus supplement, and any commission payable by us to such agent will be set forth in the prospectus supplement. Unless otherwise indicated in the prospectus supplement, any such agent will be acting on a best efforts basis for the period of its appointment. Any such agent may be deemed to be an underwriter, as that term is defined in the Securities Act, of the securities so offered and sold.

Offers to purchase securities may be solicited directly by us and sales thereof may be made by us directly to institutional investors or others. The terms of any such sales, including the terms of any bidding or auction prices, if utilized, will be described in the proxy supplement related thereto.

We may from time to time engage a firm to act as our agent for one or more offerings of our securities. We sometimes refer to this agent as our offering agent. If we reach agreement with an offering agent with respect to a specific offering, including the number of securities and any minimum price below which sales may not be made, than the offering agent will try to sell such securities on the agreed terms. The offering agent could make sales in privately negotiated transactions or any other method permitted by law, including sales deemed to be an at-the-market offering as defined in Rule 415 promulgated under the Securities Act, including sales made directly on the NYSE, or sales made to or through a market maker other than on an exchange. The offering agent will be deemed to be an underwriter within the meaning of the Securities Act with respect to any sales effected through an at the market offering.

If so indicated in a prospectus supplement, we will authorize agents, underwriters or dealers to solicit offers by certain institutional investors to purchase offered securities for payment and delivery on a future date specified in such prospectus supplement. There may be limitations on the minimum amount which may be purchased by any such institutional investor or on the portion of the aggregate principal amount of the particular offered securities which may be sold pursuant to such arrangements. Institutional investors to which such offers may be made, when authorized, include commercial and savings banks, insurance companies, pension funds, investment companies, educational and charitable institutions and such other institutions as may be approved by us. The obligations of any purchaser under these contracts will be subject to the condition that the purchase of the offered securities shall not at the time of delivery be prohibited under the laws of the jurisdiction to which the purchaser is subject.

Unless we specify otherwise in the applicable prospectus supplement, any series of securities issued hereunder will be a new issue with no established trading market (other than our common stock, which is listed on the NYSE). If we sell any shares of our common stock pursuant to a prospectus supplement, such shares will be listed on the NYSE, subject to official notice of issuance. We may elect to list any other securities issued hereunder on any exchange, but we are not obligated to do so. Any underwriters or agents to or through whom such securities are sold by us for public offering and sale may make a market in such securities, but such underwriters or agents will not be obligated to do so and may discontinue any market making at any time without notice. We cannot assure you as to the liquidity of the trading market for any such securities.

To facilitate the offering of securities, certain persons participating in the offering may engage in transactions that stabilize, maintain or otherwise affect the price of the securities. This may include over-allotments or short sales of the securities, which involves the sale by persons participating in the offering of more securities than we sold to them. In these circumstances these persons would cover the over-allotments or short positions by making purchases in the open market or by exercising their over-allotment option. In addition, these persons may stabilize or maintain the prices of the securities by bidding for or purchasing securities in the open market or by imposing penalty bids whereby selling concessions allowed to dealers participating in the offering may be reclaimed if securities sold by them are repurchased in connection with stabilization transactions. The effect of these transactions may be to stabilize or maintain the market price of the securities at a level above that which might otherwise prevail in the open market. These transactions may be discontinued at any time.

Underwriters, dealers and agents participating in the distribution of the offered securities may be deemed to be underwriters, and any discounts or commissions received by them and any profit realized by them upon the resale of the offered securities may be deemed to be underwriting discounts and commissions, under the Securities Act. If such dealers or agents were deemed to be underwriters, they may be subject to statutory liabilities under the Securities Act. Underwriters, dealers and agents may be entitled, under agreements entered into with us, to indemnification against and contribution toward certain civil liabilities, including liabilities under the Securities Act.

Certain of the underwriters, dealers or agents and their affiliates and associates may engage in transactions with and perform services for us in the ordinary course of their business for which they receive compensation.

LEGAL MATTERS

The validity of the securities offered hereby will be passed upon for us by Goodwin Procter llp. Goodwin Procter llp has also issued an opinion to us regarding certain tax matters described under Federal Income Tax Considerations Related to Our REIT Election.

EXPERTS

The consolidated financial statements and schedule of DiamondRock Hospitality Company as of December 31, 2008 and 2007, and for each of the years in the three-year period ended December 31, 2008, and management s assessment of the effectiveness of internal control over financial reporting as of December 31, 2008 have been incorporated by reference herein and in the registration statement in reliance upon the reports of KPMG LLP, independent registered public accounting firm, incorporated by reference herein, and upon the authority of said firm as experts in accounting and auditing.

WHERE YOU CAN FIND MORE INFORMATION

We file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any document we file with the SEC at the SEC s public reference room at 100 F Street, N.E. Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information about the public reference room. The SEC also maintains a website that contains reports, proxy and information statements and other information regarding registrants that file electronically with the SEC at http://www.sec.gov. You can inspect reports and other information we file at the offices of the NYSE, 20 Broad Street, New York, NY 10005. In addition, we maintain a website that contains information about us at www.drhc.com. The information found on, or otherwise accessible through, our website is not incorporated into, and does not form a part of, this prospectus or any other report or documents we file with or furnish to the SEC.

We have filed with the SEC a shelf registration statement on Form S-3 under the Securities Act relating to the securities that may be offered by this prospectus. This prospectus is a part of that registration statement, but does not contain all of the information in the registration statement. We have omitted parts of the registration statement in accordance with the rules and regulations of the SEC. For more detail about us and any securities that may be offered by this prospectus, you may examine the registration statement on Form S-3 and the exhibits filed with it at the locations listed in the previous paragraph.

INCORPORATION OF CERTAIN DOCUMENTS BY REFERENCE

The SEC allows us to incorporate by reference in this prospectus certain information we file with the SEC, which means that we may disclose important information in this prospectus by referring you to the document that contains the information. The information incorporated by reference is considered to be a part of this prospectus, and the information we file later with the SEC will automatically update and supersede this information. We incorporate by reference the documents listed below that we filed with the SEC:

our Annual Report on Form 10-K for the year ended December 31, 2008;

our Quarterly Report on Form 10-Q for the quarter ended March 27, 2009;

our Quarterly Report on Form 10-Q for the quarter ended June 19, 2009;

our Definitive Proxy Statement on Schedule 14A filed on March 4, 2009, as amended by additional definitive proxy materials filed on March 6, 2009;

our Current Reports on Form 8-K filed on April 15, 2009 and July 27, 2009;

The description of our common stock, $0.01 par value per share, contained in our Registration Statement on Form 8-A filed on May 25, 2005, including any amendment or report filed for the purpose of updating such description (file number 001-32514); and

all documents filed by us with the SEC pursuant to Section 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act from the date of this prospectus and prior to the termination of the offering of the underlying securities; provided, however, that we are not incorporating by reference any additional documents or information furnished and not filed with the SEC.

You may request a copy of these documents, and any exhibits we have specifically incorporated by reference as an exhibit in this prospectus, at no cost by writing us at the following address or calling us at the telephone number listed below or via the Internet at the website listed below:

DiamondRock Hospitality Company
6903 Rockledge Drive, Suite 800
Bethesda, MD 20817
Attention: Investor Relations
(240) 744-1150
Internet Website: www.dhrc.com

Readers should rely on the information provided or incorporated by reference in this prospectus or in the applicable supplement to this prospectus. Readers should not assume that the information in this prospectus and the applicable supplement is accurate as of any date other than the date on the front cover of the document.

The information contained on our website does not constitute a part of this prospectus, and our website address supplied above is intended to be an inactive textual reference only and not an active hyperlink.