

HOST HOTELS & RESORTS, INC.

Form 8-K

October 29, 2010

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

**FORM 8-K**

**CURRENT REPORT**

**PURSUANT TO SECTION 13 OR 15(d) OF THE**

**SECURITIES EXCHANGE ACT OF 1934**

**Date of report (Date of earliest event reported): October 25, 2010**

**HOST HOTELS & RESORTS, INC.**

**(Exact Name of Registrant as Specified in Charter)**

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(State or Other Jurisdiction  
of Incorporation)

(Commission  
File Number)

(IRS Employer

Identification No.)

**6903 Rockledge Drive**

**Suite 1500**

**Bethesda, Maryland 20817**

(Address of Principal Executive Offices and Zip Code)

**(240) 744-1000**

**Registrant's telephone number, including area code:**

Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

- Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)
- Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)
- Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))
- Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

**Item 1.01. Entry into a Material Definitive Agreement.**

The information required by this item is included in Item 2.03 below and is incorporated herein by reference.

**Item 2.03. Creation of a Direct Financial Obligation or an Obligation under an Off-Balance Sheet Arrangement of a Registrant.**

On October 25, 2010, Host Hotels & Resorts, L.P. ( Host L.P. ), for whom Host Hotels & Resorts, Inc. ( Host REIT ) acts as sole general partner, issued \$500 million aggregate principal amount of Series U senior notes bearing interest at a rate of 6% per year due in 2020. The notes pay interest semi-annually in arrears. The notes were offered in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933, as amended.

*Optional Redemption Provisions and Change of Control Repurchase Right*

At any time prior to November 1, 2015, the Series U senior notes will be redeemable at Host L.P.'s option, in whole or in part, at a price equal to 100% of their principal amount, plus a make-whole premium as set forth in the senior notes indenture, plus accrued and unpaid interest to the applicable redemption date. Beginning November 1, 2015, Host L.P. may redeem, in whole or in part, the Series U senior notes at any time subject to the payment of a redemption price together with any accrued and unpaid interest to the applicable redemption date. The redemption price includes a call premium that varies (from 3% to 0%) depending on the year of redemption.

Prior to November 1, 2013, Host L.P. may redeem up to 35% of the aggregate principal amount of the Series U senior notes at a redemption price equal to 106% of the principal amount thereof, together with any accrued and unpaid interest to the applicable redemption date, with the net cash proceeds of sales of equity securities by Host L.P. or Host REIT.

The holders of Series U senior notes will also have the right to require Host L.P. to repurchase their notes upon the occurrence of a change in control triggering event, as defined in the senior notes indenture, at an offer price equal to 101% of the principal amount of the senior notes plus accrued and unpaid interest to the date of purchase.

*Ranking and Security*

The notes were issued pursuant to a supplement to Host L.P.'s Amended and Restated Indenture, dated August 5, 1998, originally among HMH Properties, Inc. (now, Host L.P.), the subsidiary guarantors named therein, and HSBC Bank USA f/k/a Marine Midland Bank (now succeeded by The Bank of New York Mellon), as trustee. Under the terms of the senior notes indenture, the senior notes are equal in right of payment with all of Host L.P.'s unsubordinated indebtedness and senior to all subordinated obligations of Host L.P., subject to certain limitations set forth in the senior notes indenture. The senior notes are guaranteed by certain of Host L.P.'s subsidiaries and are currently secured by pledges of equity interests in certain of Host L.P.'s subsidiaries. The guarantees and pledges ratably benefit the notes outstanding under Host L.P.'s senior notes indenture, as well as Host L.P.'s credit facility and certain other senior debt, and interest rate swap agreements and other hedging agreements with lenders that are parties to the credit facility.

*Restrictive Covenants*

Under the terms of the senior notes indenture, Host L.P.'s ability to incur indebtedness and make distributions is subject to restrictions and the satisfaction of various conditions, including the achievement of an EBITDA-to-interest coverage ratio of at least 2.0x by Host L.P. (1.7x in the case of distributions to enable Host REIT to pay dividends on its preferred stock). This ratio is calculated in accordance with Host L.P.'s senior notes indenture and excludes from interest expense items such as call premiums and deferred financing charges that are included in interest expense on Host L.P.'s consolidated statement of operations. In addition, the calculation is based on Host L.P.'s pro forma results for the four prior fiscal quarters giving effect to certain transactions, such as acquisitions, dispositions and financings, as if they occurred at the beginning of the period. Other covenants limiting Host L.P.'s ability to incur indebtedness and make distributions include maintaining total indebtedness of less than 65% of adjusted total assets (using un-depreciated real estate values) and secured indebtedness of less than 45% of adjusted total assets. So long as Host L.P. maintains the required level of interest coverage and satisfies these and other conditions in the senior notes indenture, it may make distributions and incur additional debt under the senior notes indenture. There are exceptions permitting distributions by Host L.P. to Host REIT, and other holders of partnership interests, that are necessary for Host REIT to pay dividends required to maintain its status as a real estate investment trust, even when Host L.P. does not meet the financial covenant tests set forth above.

The senior notes indenture also imposes restrictions on customary matters, such as limitations on the capital expenditures, acquisitions, investments, and transactions with affiliates and the incurrence of liens.

#### *Registration Rights Agreement*

In connection with the issuance of the Series U senior notes, Host L.P. also entered into a registration rights agreement, dated as of October 25, 2010, (the Registration Rights Agreement ) under which Host L.P. agreed pursuant to customary terms to make an offer to exchange the Series U senior notes for registered, publicly tradable notes that have substantially identical terms to the Series U senior notes. Under the terms of the Registration Rights Agreement, Host L.P. also agreed, in certain limited circumstances, to file a shelf registration statement that would allow certain holders of the Series U senior notes to resell their respective notes to the public.

#### *Use of Proceeds*

Host L.P. intends that the net proceeds of the offering will be used to redeem at least \$250 million of the \$500 million in aggregate principal amount outstanding of the 7 1/8% Series K senior notes due 2013 and for general corporate purposes, future acquisitions or repayment of other indebtedness. Pending application of the net proceeds, the proceeds may be invested in short-term securities.

#### **Forward-Looking Statements**

The discussion in this report on Form 8-K contains forward-looking statements within the meaning of federal securities regulations. These forward-looking statements are identified by their use of terms and phrases such as anticipate, believe, could, estimate, expect, forecast, may, plan, predict, project, will, continue and other similar terms and phrases, including references to assumption and forecasts of future. Forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the actual results to differ materially from those anticipated at the time the forward-looking statements are made. These risks include, but are not limited to: national and local economic and business conditions, including the potential for terrorist attacks, that will affect occupancy rates at our hotels and the demand for hotel products and services; operating risks associated with the hotel business; risks associated with the level of our indebtedness and our ability to meet covenants in our debt agreements; relationships with property managers; our ability to maintain our properties in a first-class manner, including meeting capital expenditure requirements; the effect of anticipated renovations on our hotel occupancy and financial results; our ability to compete effectively in areas such as access, location, quality of accommodations and room rate structures; changes in travel patterns, taxes and government regulations, which influence or determine wages, prices, construction procedures and costs; our ability to complete acquisitions and dispositions; and our ability to continue to satisfy complex rules in order for Host REIT to qualify as a real estate investment trust for federal income tax purposes and other risks and uncertainties associated with our business described in our filings with the SEC. Although we believe the expectations reflected in such forward-looking statements are based upon reasonable assumptions, we can give no assurance that the expectations will be attained or that any deviation will not be material.

#### **Item 9.01. Financial Statements and Exhibits**

(d) Exhibits

<b>Exhibit No.</b>	<b>Description</b>
4.1	Thirty-Sixth Supplemental Indenture, dated October 25, 2010, by and among Host Hotels & Resorts, L.P., the Subsidiary Guarantors named therein and The Bank of New York Mellon, as successor to HSBC Bank USA (formerly Marine Midland Bank), as trustee, to the Amended and Restated Indenture dated August 5, 1998.

**SIGNATURE**

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

HOST HOTELS & RESORTS, INC.

Date: October 29, 2010

By: /s/ Brian G. Macnamara  
Brian G. Macnamara  
Senior Vice President, Corporate Controller

**EXHIBIT INDEX**

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**Compensation of Directors**

Neither employee nor non-employee directors receive any compensation for their services as such. The Company reimburses each director for reasonable out-of-pocket expenses incurred in attending meetings of the Board of Directors and any of its committees.

**Compensation Committee Interlocks and Insider Participation**

The following non-employee directors were the members of the Compensation Committee of the Board of Directors during 2003: Randall E. Poliner (Chairman) and Robert P. O'Block. None of the members of the Compensation Committee is an executive officer of the Company.

**COMPENSATION COMMITTEE REPORT ON EXECUTIVE COMPENSATION**

**General**

The Compensation Committee of the Company's Board of Directors has furnished the following report on executive compensation in accordance with the rules and regulations of the Commission. This report outlines the duties of the Compensation Committee with respect to executive compensation, the various components of the Company's compensation program for executive officers and other key employees, and the basis on which the 2003 compensation was determined for the executive officers, with particular detail given to the 2003 compensation for the Company's Chief Executive Officer.

**Compensation of Executive Officers Generally**

The Compensation Committee is responsible for establishing compensation levels for the executive officers of the Company, including the annual bonus plan for executive officers, and for administering the Company's equity compensation plans. The Compensation Committee is comprised of two non-employee directors: Messrs. Poliner (Chairman) and O Block. The Compensation Committee's overall objective is to establish a compensation policy that will (1) attract, retain and reward executives who contribute to the achievement of the Company's business objectives; (2) motivate executives to attain these objectives; and (3) align the interests of executives with those of the Company's long-term investors. The Company compensates executive officers with a combination of salary and incentives designed to focus their efforts on maximizing both the near-term and long-term financial performance of the Company. In addition, the Company's compensation program rewards individual performance that furthers Company goals. The executive compensation program includes base salary, incentive bonuses, long-term equity incentive awards in the form of stock option grants, and other benefits. Each executive officer's compensation package is designed to provide an appropriately weighted mix of these elements, which cumulatively provide a level of compensation roughly equivalent to that paid by companies of similar size and complexity.

*Base Salary.* Base salary levels for each of the Company's executive officers, including the Chief Executive Officer, are generally set within a range of base salaries that the Compensation Committee believes are paid to executive officers at companies deemed comparable to the Company based on similarities in revenue levels, industry segments and competitive employment markets. In addition, the Compensation Committee generally takes into account the Company's past financial performance and future expectations, as well as the performance of the executives and changes in the executives' responsibilities. The annual base salary paid to Ms. DeMarse (\$300,000) is the amount specified in her employment agreement with the Company.

*Incentive Bonuses.* The Compensation Committee recommends the payment of bonuses to provide an incentive to executive officers. Bonuses are awarded only if the Company achieves or exceeds certain corporate performance objectives. The incentive bonus to each executive officer is based on the individual executive's performance as it relates to the Company's performance. Pursuant to the Company's employment agreement with Elisabeth DeMarse, the Company is required to pay, and has paid, Ms. DeMarse a bonus of \$100,000 per year.

*Equity Incentives.* Stock options are used by the Company to provide a stock-based incentive to improve the Company's financial performance and to assist in the recruitment, retention and motivation of professional, managerial and other personnel. Stock options are also designed to align the interests of the Company's executive officers with those of its stockholders by encouraging executive officers to enhance the value of the Company, the price of the Common Stock, and hence, the stockholders' return over the long term. Generally, stock options are granted to executive officers from time to time based primarily upon the individual's actual and/or potential contributions to the Company and the Company's financial performance over the long term.

#### *Compensation of the Chief Executive Officer*

Pursuant to her employment agreement with the Company, the Company has paid Ms. DeMarse an annual salary of \$300,000 plus an annual bonus of \$100,000. The Committee believes the compensation paid to Ms. DeMarse is reasonable.

#### *Policy with Respect to Qualifying Compensation for Deductibility*

Section 162(m) of the Internal Revenue Code imposes a limit on tax deductions for annual compensation (other than performance-based compensation) in excess of one million dollars paid by a corporation to its Chief Executive Officer and the other four most highly compensated executive officers. The Company has not established a policy with regard to Section 162(m) of the Internal Revenue Code, because the Company has not paid and does not currently anticipate paying annual compensation in excess of one million dollars to any employee. None of the compensation paid by the Company in 2003 was subject to limitations on deductibility. The Board of Directors will continue to assess the impact of Section 162(m) on its compensation practices and determine what further action, if any, is appropriate.

Members of the  
Compensation Committee  
Randall E. Poliner, Chairman  
Robert P. O Block



**STOCK PERFORMANCE GRAPH**

The following graph provides a comparison of the cumulative total stockholder return on the Company's Common Stock for the period from May 13, 1999 (the closing date of the Company's initial public offering) through December 31, 2003, against the cumulative stockholder return during such period achieved by the Nasdaq Stock Market Index for U.S. Companies ( Nasdaq US ) and the CoreData Internet Information Providers Index ( CoreData Group Index ). The graph assumes that \$100 was invested on May 13, 1999 in the Company's Common Stock and in each of the comparison indices, and assumes reinvestment of dividends.

Measurement Period	Bankrate,	Nasdaq US	CoreData
	Inc.	Index	Index
Measurement point May 13, 1999	\$ 100.00	\$ 100.00	\$ 100.00
June 30, 1999	50.48	105.34	92.57
September 30, 1999	40.38	107.05	89.15
December 31, 1999	34.62	158.11	156.60
March 31, 2000	20.19	179.90	135.68
June 30, 2000	8.65	154.73	97.52
September 29, 2000	9.14	142.79	87.52
December 29, 2000	1.45	95.95	46.09
March 31, 2001	3.85	72.34	30.43
June 29, 2001	7.69	84.78	35.86
September 28, 2001	4.00	58.88	14.23
December 31, 2001	5.00	76.74	26.11
March 31, 2002	9.23	72.74	25.02
June 30, 2002	10.85	58.34	19.06
September 30, 2002	15.69	46.79	13.35
December 31, 2002	29.62	53.43	21.88
March 31, 2003	35.31	53.71	28.59
June 30, 2003	93.23	65.05	41.78
September 30, 2003	107.85	71.86	46.99
December 31, 2003	95.23	80.50	55.65

The Stock Performance Graph shall not be deemed incorporated by reference by any general statement incorporating by reference this Proxy Statement into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that the Company specifically incorporates this information by reference, and shall not otherwise be deemed filed under either of such Acts.

#### Section 16(a) Beneficial Ownership Reporting Compliance

Under Section 16(a) of the Securities Exchange Act of 1934, the Company's directors, certain of its officers, and beneficial owners of more than 10% of the outstanding Common Stock are required to file reports with the Commission concerning their ownership of and transactions in Common Stock; such persons are also required to furnish the Company with copies of such reports. Based solely upon the reports and related information furnished to the Company, the Company believes that all such filing requirements were complied with in a timely manner during and with respect to 2003, except that Bruns H. Grayson filed one late Form 4.

#### Certain Transactions

The Company renewed its lease with Bombay Holdings, Inc. for its principal corporate offices and facilities effective January 1, 2004. Bombay is wholly-owned by Peter C. Morse, a director and principal stockholder of the Company. The lease is for three years, expiring on December 31, 2006, and requires the Company to pay a percentage of the common maintenance charges. Rent expense paid to Bombay for the year ended December 31, 2003 was approximately \$305,000. The Company believes that the terms of the lease agreement are no less favorable to us than those that could have been obtained from unaffiliated third parties.

The Board of Directors has adopted a resolution requiring that all future transactions with related parties be approved by a majority of the Board of Directors, including a majority of the independent and disinterested members of the Board of Directors, or a majority of the disinterested stockholders, and be on terms no less favorable to the Company than could be obtained from unaffiliated third parties.



**PROPOSAL 2****RATIFICATION OF SELECTION OF INDEPENDENT PUBLIC ACCOUNTANTS**

The Audit Committee of the Board of Directors has appointed the accounting firm of KPMG LLP to serve as the Company's independent public accountants for the fiscal year ending December 31, 2004. A proposal to ratify that appointment will be presented at the Annual Meeting. Representatives of KPMG LLP are expected to be present at the meeting. They will have the opportunity to make a statement if they desire to do so and will be available to respond to appropriate questions from stockholders.

**The Board of Directors recommends a vote FOR ratification of the selection of the independent public accountants.**

**Information Regarding Our Independent Public Accountants**

KPMG LLP served as our independent accountants for the fiscal year ended December 31, 2003. The appointment of this firm was recommended to our Board of Directors by our Audit Committee and was ratified by stockholders at the 2003 annual meeting. KPMG LLP has been our independent public accountants since 1998.

**Audit and Non-Audit Fees**

The following table presents fees for professional audit services rendered by KPMG LLP for the audit of the Company's annual financial statements for the years ended December 31, 2003 and 2002 and fees billed for other services rendered by KPMG LLP during those periods.

	<u>Fiscal 2003</u>	<u>Fiscal 2002</u>
Audit fees (1)	\$ 119,050	\$ 105,000
Audit related fees (2)	7,500	
Tax fees (3)	5,000	
All other fees (4)	20,000	
	<u>          </u>	<u>          </u>
<b>Total</b>	<b>\$ 146,550</b>	<b>\$ 105,000</b>

- (1) **Audit Fees**—Audit fees billed to the Company by KPMG LLP for auditing the Company's annual financial statements and reviewing the financial statements included in the Company's Quarterly Reports on Form 10-Q.
- (2) **Audit-Related Fees**—Audit-related fees billed to the Company by KPMG LLP include fees related to the review of the Company's registration statement filed on Form S-3 in December 2003.

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- (3) **Tax Fees** Tax fees billed to the Company by KPMG LLP include fees related to preparing the 2003 U.S. corporate income and state income and franchise tax returns.
- (4) **All Other Fees** All other fees billed to the Company by KPMG LLP include fees related to providing advice and assistance to management in planning compliance with The Sarbanes-Oxley Act of 2002 Section 404, internal control over financial reporting.

### **Policy on Audit Committee Pre-Approval of Audit and Non-Audit Services of Independent Auditor**

The Audit Committee of the Board of Directors has implemented procedures under the Company's Audit Committee Pre-Approval Policy for Audit and Non-Audit Services (the Pre-Approval Policy) to ensure that all audit and permitted non-audit services provided to the Company are pre-approved by the Audit Committee.

Specifically, the Audit Committee pre-approves the use of KPMG LLP for specific audit and non-audit services, within approved monetary limits. If a proposed service has not been pre-approved pursuant to the Pre-Approval Policy, then it must be specifically pre-approved by the Audit Committee before it may be provided by KPMG LLP. Any pre-approved services exceeding the pre-approved monetary limits require specific approval by the Audit Committee. The Audit Committee may delegate pre-approval authority to one or more of its members when expedition of services is necessary. All of the audit-related, tax and all other services provided by KPMG LLP to the Company in 2003 were approved by the Audit Committee by means of specific pre-approvals or pursuant to the procedures contained in the Pre-Approval Policy.

The Audit Committee has determined that all non-audit services provided by KPMG LLP in 2003 were compatible with maintaining its independence in the conduct of its auditing functions.

### **Report of the Audit Committee**

The Audit Committee operates under a written charter adopted by the Board of Directors and revised in 2004 to reflect changes required by the Sarbanes-Oxley Act of 2002 and the NASD. The Audit Committee's charter was first published in its entirety as an appendix to the Company's 2001 Proxy Statement. The revised charter, which was approved by the Board of Directors, is included as Appendix A to this Proxy Statement. This report reviews the actions taken by the Audit Committee with regard to the Company's financial reporting process during 2003 and particularly with regard to the Company's audited consolidated financial statements as of December 31, 2003 and 2002 and for the three years ended December 31, 2003.

The Audit Committee selects of the Company's independent public accountants and meets with the Company's independent public accountants to discuss the scope and review the results of the annual audit.

The Audit Committee has implemented procedures to ensure that during the course of each fiscal year it devotes the attention that it deems necessary or appropriate to each of the matters assigned to it under the Committee's Charter. The Audit Committee met four times during 2003.

All of the directors who serve on the Audit Committee are independent for purposes of the National Association of Securities Dealers listing standards. That is, the Board of Directors has determined that none of the members of the Committee has any relationship to the Company that may interfere with his independence from the Company and its management.

The Audit Committee has reviewed the Company's 2003 financial statements and met with both management and KPMG LLP, the Company's independent public accountants, to discuss those financial statements. Management has represented to us that the financial statements were prepared in conformity with accounting principles generally accepted in the United States of America. The Committee also has received from and discussed with KPMG LLP the letter required by Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees), relating to that firm's independence from the Company. The Audit Committee has also discussed with KPMG LLP any matters required to be discussed by Statement on Auditing Standards No. 61 (Communication with Audit Committees).

On the basis of these reviews and discussions, the Audit Committee has recommended to the Board of Directors that the Board approve the inclusion of the Company's audited financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2003, for filing with the Securities and Exchange Commission.

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Members of the Audit Committee

Robert P. O Block, Chairman

Randall E. Poliner

Bruns H. Grayson

### STOCKHOLDER PROPOSALS

Rules of the Commission require that any proposal by a stockholder for consideration at the 2005 annual meeting of stockholders must be received by the Company no later than January 7, 2005, if it is to be eligible for inclusion in the Company's proxy materials for its 2005 annual meeting of stockholders. Under these rules, the Company is not required to include stockholder proposals in its proxy materials unless certain other conditions specified in such rules are met.

In order for a stockholder to bring any other business or nominations before an annual meeting of stockholders, certain conditions set forth in Article II, Sections 16 and 17, of the Company's Amended and Restated Bylaws must be complied with, including delivery of notice to the Company in sufficient time prior to the meeting.

### HOUSEHOLDING

If a stockholder and other residents at his or her mailing address own shares of the Company's Common Stock in street name, the stockholder's broker or bank may have given notice that each household will receive only one annual report and one proxy statement for each company in which stock is held through that broker or bank. This practice is known as householding. Unless the stockholder responded to that notice that he or she did not wish to participate in householding, he or she would be deemed to have consented to participating, and only one copy of each company's annual report and proxy statement would be sent to that address (however, each stockholder would continue to receive a separate proxy card).

Any stockholder who wishes to receive his or her own set of the Company's future annual reports and proxy statements, or who shares an address with another stockholder of the Company and together would like to receive only one set of annual disclosure documents, should contact the Company at 11811 U.S. Highway One, Suite 101, North Palm Beach, Florida 33408, Attention: Secretary, being sure to supply the names of all stockholders at the same address, the name of the bank or brokerage firm, and the account number(s). The revocation of a consent to householding should be effective 30 days after the notice is received.

BY ORDER OF THE BOARD OF DIRECTORS,

Elisabeth DeMarse

President and Chief Executive Officer



**AUDIT COMMITTEE OF THE BOARD OF DIRECTORS**

**CHARTER**

**Purpose**

The Audit Committee (the **Committee**) is appointed by the Board of Directors (the **Board**) of Bankrate, Inc. (the **Company**). The primary function of the Committee is to assist the Board in fulfilling its oversight responsibilities, primarily through:

overseeing management's conduct of the Company's financial reporting process and systems of internal accounting and financial controls;

monitoring the independence and performance of the Company's outside auditors; and

providing an avenue of communication among the outside auditors, management and the Board.

**Composition**

1. The Committee shall have at least three (3) members at all times, each of whom must be independent of management, as well the Company and each of its affiliates. A member of the Committee shall be considered independent if:

(a) in the sole discretion of the Board, it is determined that he or she has no relationship that may interfere with the exercise of his or her independent judgment; and

(b) he or she meets The Nasdaq Stock Market, Inc. Marketplace Rules regarding independence of audit committee members.

2. If any member of the Committee develops a conflict of interest (as that term is defined in The Nasdaq Stock Market, Inc. Marketplace Rules, Rule 4350 (h)), that member shall have an affirmative obligation to promptly disclose such relationship to the Board.

3. No member of the Committee shall accept any consulting, advisory or other compensatory fee from the Company other than in connection with serving on the Committee or as a member of the Board.

4. All members of the Committee shall have a practical knowledge of finance and accounting and be able to read and understand fundamental financial statements or be able to do so within a reasonable period of time after appointment to the Committee.
5. At least one member of the Committee shall have accounting or related financial management expertise, as the Board interprets such qualification in its business judgment.
6. Each member of the Committee shall be appointed by the Board and shall serve until the earlier to occur of the date on which he or she shall be replaced by the Board, resigns from the Committee, or resigns from the Board.

**Meetings**

1. The Committee shall meet as frequently as circumstances dictate, but no less than four times annually. The Board shall name a chairperson of the Committee, who shall prepare and/or approve an agenda in advance of each meeting. A majority of the members of the Committee shall constitute a quorum. The Committee shall maintain minutes or other records of meetings and activities of the Committee.

2. The Committee shall, through its chairperson, report regularly to the Board following the meetings of the Committee, addressing such matters as the quality of the Company's financial statements, the Company's compliance with legal or regulatory requirements, the performance and independence of the outside auditors, the performance of the internal audit function or other matters related to the Committee's functions and responsibilities.

### **RESPONSIBILITIES AND DUTIES**

The Committee's principal responsibility is one of oversight. The Company's management is responsible for preparing the Company's financial statements and the outside auditors are responsible for auditing and/or reviewing those financial statements.

While the Committee has the powers and responsibilities set forth in this charter, it is not the responsibility of the Committee to plan or conduct audits or to determine that the Company's financial statements present fairly the financial position, the results of operations and the cash flows of the Company, in conformity with accounting principles generally accepted in the United States of America. This is the responsibility of management and the outside auditors. In carrying out these oversight responsibilities, the Committee is not providing any expert or special assurance as to the Company's financial statements or any professional certification as to the outside auditors' work.

The Committee's specific responsibilities are as follows:

#### **General**

1. The Committee shall have the power to conduct or authorize investigations into any matters within the Committee's scope of responsibilities. The Committee shall have unrestricted access to members of management and other employees of the Company, as well as all information relevant to the carrying out of its responsibilities.

2. The Committee shall, with the assistance of management, the outside auditors and legal counsel, as the Committee deems appropriate, review and evaluate, at least annually, the Committee's:

(a) charter;

(b) powers and responsibilities; and

(c) performance.

The Committee shall report and make recommendations to the Board with respect to the foregoing, as appropriate.

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3. The Committee shall ensure inclusion of its then-current charter in the proxy statement for the Company's annual meetings of shareholders, at least once every three years in accordance with regulations of the SEC.

4. The Committee shall prepare annual Committee reports for inclusion in the proxy statements for the Company's annual meetings, as required by rules promulgated by the SEC.

5. The Committee shall, in addition to the performance of the duties described in this charter, undertake such additional duties as from time to time may be:

(a) delegated to it by the Board;

(b) required by law or under The Nasdaq Stock market, Inc. Marketplace Rules; or

(c) deemed desirable, in the Committee's discretion, in connection with its functions described in this charter.

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6. The Committee shall be empowered to retain, at the Company's expense, independent counsel, accountants or other advisors for such purposes as the Committee, in its sole discretion, determines to be appropriate to carry out its responsibilities. The Company will provide for appropriate funding, as determined by the Committee, for payment of compensation to the independent auditor for the purpose of rendering or issuing an audit report and to any advisors employed by the Committee.

#### **Internal Controls and Risk Assessment**

1. The Committee shall review annually, with management and the outside auditors, if deemed appropriate by the Committee, the effectiveness of or weaknesses in the Company's internal controls, including computerized information system controls and security, the overall control environment and accounting and financial controls.

2. The Committee shall obtain from the outside auditors their recommendations regarding internal controls and other matters relating to the accounting procedures and the books and records of the Company.

3. The Committee shall, in accordance with SEC regulations, establish procedures for:

(a) the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters; and

(b) the confidential, anonymous submission by employees of the Company of concerns regarding questionable accounting or auditing matters.

4. The Committee shall review major financial risk exposures and the guidelines and policies which management has put in place to govern the process of monitoring, controlling and reporting such exposures.

#### **Outside Auditors; Their Performance and Independence**

1. The outside auditors report directly to the Committee, are ultimately accountable to the Board and the Committee, as the representatives of the shareholders of the Company. The Committee shall evaluate and recommend to the Board the selection and, where appropriate, the replacement of the outside auditors. The Committee shall recommend to the Board the outside auditors to be proposed for shareholder approval in any proxy statement.

2. The Committee shall:

(a) confer with the outside auditors concerning the scope of their examinations of the books and records of the Company and its subsidiaries;

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- (b) review the scope, plan and procedures to be used on the annual audit, as recommended by the outside auditors;
  
- (c) review the results of the annual audits and interim financial reviews performed by the outside auditors, including:
  - (1) the outside auditors' audit of the Company's annual financial statements, accompanying footnotes and its report thereon;
  
  - (2) any significant changes required in the outside auditors' audit plans or scope;
  
  - (3) any material differences or disputes with management encountered during the course of the audit (the Committee to be responsible for overseeing the resolution of such differences and disputes);
  
  - (4) any material management letter comments and management's responses to recommendations made by the outside auditors in connection with the audit;

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- (5) matters required to be discussed by Statement on Auditing Standards No. 61, as amended (Communications with Audit Committees), relating to the conduct of the audit;
- (d) authorize the outside auditors to perform such supplemental reviews or audits as the Committee may deem desirable; and
- (e) obtain from the outside auditors assurance that they have complied with Section 10A, as amended, of the Securities Exchange Act of 1934.
3. The Committee shall inquire into any accounting adjustments that were noted or proposed by the outside auditors but were passed as immaterial or otherwise.
4. The Committee shall inquire as to any matters that were referred to the outside auditors national office relating to accounting policies and/or financial statement disclosure within the Company s financial statements and, to the extent deemed appropriate, request an opportunity to address such issues directly with a representative of such national office.
5. Pre-approval by the Committee shall be required with respect to the fees for all audit and other services performed by the outside auditors as negotiated by management.
6. The Committee s approval of any non-audit services to be rendered by the outside auditors must be obtained in advance of engaging the outside auditors to render such services. The Committee shall not approve the engagement of the outside auditors to render non-audit services prohibited by law or rules and regulations promulgated by the SEC. The Committee shall consider whether the provision of non-audit services is compatible with maintaining the outside auditors independence, including, but not limited to, the nature and scope of the specific non-audit services to be performed and whether the audit process would require the outside auditors to review any advice rendered by the outside auditors in connection with the provision of non-audit services.
7. The Committee shall receive from the outside auditors on a periodic basis a formal written statement delineating all relationships between the outside auditors and the Company, consistent with the Independence Standards Board, Standard No. 1, regarding relationships and services, which may impact the objectivity and independence of the outside auditors, and other applicable standards. The statement shall include a description of all services provided by the outside auditors and the related fees. The Committee shall actively engage in a dialogue with the outside auditors regarding any disclosed relationships or services that may impact the objectivity and independence of the outside auditors and shall evaluate, after gathering information from management, and other Board members, the performance of the outside auditors and recommend that the Board take action to satisfy itself of the independence of the outside auditors.
8. The Committee shall establish written hiring policies for current and former employees of the outside auditors.
9. The Committee shall consider whether it is appropriate to adopt a policy of insisting upon the rotation of the outside auditors lead audit partner or rotating the outside auditors on a periodic basis. Based upon its evaluation, the Committee shall take, or recommend that the Board take, appropriate action to monitor the independent status of the outside auditors.

**Financial Reporting**

1. The Committee shall review and discuss with the outside auditors and management the Company's audited annual financial statements that are to be included in the Company's annual report on Form 10-K and the outside auditors' opinion with respect to such financial statements, including reviewing the nature and extent of any significant changes in accounting principles or the application of such accounting principles; and determine

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whether to recommend to the Board that the financial statements be included in the Company's annual report on Form 10-K for filing with the SEC.

2. The Committee shall review and discuss with the outside auditors and management, and require the outside auditors to review, the Company's interim financial statements to be included in the Company's quarterly reports on Form 10-Q prior to filing such reports with the SEC.

3. The Committee shall review and discuss:

(a) the existence of significant estimates and judgments underlying the financial statements, including the rationale behind those estimates as well as the details on material accruals and reserves and the Company's accounting principles;

(b) all critical accounting policies identified to the Committee by the outside auditors;

(c) major changes to the Company's accounting principles and practices, including those required by professional or regulatory pronouncements and actions, as brought to its attention by management and/or the outside auditors; and

(d) material questions of choice with respect to the appropriate accounting principles and practices to be used in the preparation of the Company's financial statements, as brought to its attention by management and/or the outside auditors.

4. The Committee shall review and discuss the Company's disclosure under Management's Discussion and Analysis of Financial Condition and Results of Operations included in any annual or quarterly report, or other report or filing filed with the SEC.

5. The Committee shall discuss generally with management earnings press releases of the Company, as well as financial information and earnings guidance provided by the Company to analysts and rating agencies.

6. The Committee shall review and discuss with outside auditors any related party transactions and relationships that could enable the negotiation of terms on other than an independent, arms-length basis.

7. The Committee shall discuss with the outside auditors any item not reported as a contingent liability or loss in the Company's financial statements as a result of a determination that such item does not satisfy a materiality threshold. The Committee shall review with the outside auditors the quantitative and qualitative analysis applied in connection with such assessment of materiality, including, without limitation, the consistency of such assessment with the requirements of SEC Staff Accounting Bulletin No. 99.

8. The Committee shall review and consider other matters in relation to the financial affairs of the Company and its accounts, and in relation to the internal and external audit of the Company as the Committee may, in its discretion, determine to be advisable.

9. The Committee shall meet at least annually with management, and the outside auditors in separate executive sessions to discuss any matters that the Committee or each of these groups believes should be discussed privately.

**Compliance with Laws, Regulations and Policies**

1. The Committee shall review with management actions taken to ensure compliance with any code or standards of conduct for the Company which may be established by the Board.

2. The Committee shall review with the Company's legal counsel any legal compliance matters, including securities trading practices and any other legal matters that could have a significant, adverse impact on the Company's financial statements.

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3. The Committee shall review with the Company's counsel and others any federal, tax or regulatory matters that may have a material impact on the Company's operations and the financial statements, related Company compliance programs and policies, and programs and reports received from regulators, and shall monitor the results of the Company's compliance efforts.

4. The Committee shall periodically review the rules promulgated by the SEC and the The Nasdaq Stock Market, Inc. relating to the qualifications, activities, responsibilities and duties of audit committees and shall take, or recommend that the Board take, appropriate action to comply with such rules.

Reviewed and approved:

April 23, 2004

/s/ RANDALL E. POLINER

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Randall E. Poliner

/s/ ROBERT P. O BLOCK

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Robert P. O Block

/s/ BRUNS H. GRAYSON

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Bruns H. Grayson



