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U.S. PATENT AND TRADEMARK OFFICE

U.S. Patent & TMO/c/TM Mail Rcpt Dt. #39

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To the Honorable Commissioner of Patents and Trademarks. Please record the attached original documents or copy thereof.

1. Name of conveying party(ies):

CAPSTAR HOTEL COMPANY

- Individual(s)
- General Partnership
- Corporation-State: DELAWARE
- Other:

Additional name(s) of conveying party(ies) attached?
 Yes No

3. Nature of conveyance:

- Assignment
- Security Agreement
- Other:
- Merger
- Change of Name

Execution Date: August 3, 1998

2. Name and address of receiving party(ies)

Name: MERISTAR HOTELS & RESORTS, INC.

Internal Address: SUITE 650

Street Address: 1010 WISCONSIN AVENUE, N.W.

City: WASHINGTON State: DC ZIP: 20007

- Individual(s) citizenship:
- Association:
- General Partnership:
- Limited Partnership:
- Corporation-State: DELAWARE
- Other:

If assignee is not domiciled in the United States, a domestic representative is attached: Yes No

(Designation must be separate document from Assignment)
Additional name(s) & address(es) attached? Yes No

4. Application number(s) or registration number(s):

A. Trademark Application No.(s):

B. Trademark registration No.(s): 1,792,073

Additional numbers attached? Yes No

5. Name and address of party to whom correspondence concerning document should be mailed:

Name: DAVID R. BENNETT

Internal Address: ROPER & QUIGG

Street Address: 200 S. MICHIGAN AVENUE, SUITE 1000

City: CHICAGO State: ILLINOIS ZIP: 60604

6. Total number of applications and registrations involved: [1]

7. Total Fee (37 CFR 3.41) \$ 40.00

- Enclosed
- Authorization to charge any additional fees to deposit account

8. Deposit account number: 18-1942

DO NOT USE THIS SPACE

9. Statement and signature.

To the best of my knowledge and belief, the foregoing information is true and correct and any attached copy is a true copy of the original document.

DAVID R. BENNETT
Name of Person Signing

Signature

8/30/99
Date

Total number of pages including cover sheet, attachments, and document: [67]

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MeriStar Hotels & Resorts, Inc.

Shares of Common Stock and Rights to acquire up to 8,400,000 of such shares

MeriStar Hotels & Resorts, Inc. ("MeriStar Hotels" or the "Company") is distributing to holders of record of (a) the common stock, par value \$0.01 per share (the "REIT Common Stock"), of MeriStar Hospitality Corporation, a Maryland corporation operating as a real estate investment trust (the "REIT"), and (b) the units of limited partnership (the "REIT OP Units") of MeriStar Hospitality Operating Partnership, L.P., a Delaware limited partnership (the "REIT Operating Partnership"), other than REIT OP Units held by the REIT or any of its subsidiaries, as of the effective time of the Merger defined below (the "Record Date"), non-transferable rights (the "Rights") to subscribe for and purchase shares of the common stock, par value \$0.01 per share (the "Common Stock"), of MeriStar Hotels, at a subscription price (the "Subscription Price") of \$2.84 per share, which is equal to 95% of the average of the daily high and low prices of the Common Stock on the New York Stock Exchange Inc. ("NYSE") for the period (the "Measurement Period") of five consecutive trading days (a "Trading Day") on the NYSE immediately following the first three Trading Days of the Common Stock on the NYSE.

The Company has been spun off (the "Spin-Off") by CapStar Hotel Company, which was a Delaware corporation ("CapStar"), and certain of its affiliates, as further described below, to become the lessee, manager and operator of various hotel assets, including those which were owned, leased and managed by CapStar and its affiliates. CapStar transferred or caused to be transferred certain assets and liabilities constituting the hotel management and leasing business operated by CapStar and its subsidiaries to MeriStar Hotels, which was a wholly owned subsidiary of CapStar. CapStar distributed, on a share-for-share basis, to its stockholders of record as of the effective time of the Merger (the "Spin-Off Record Date") all of the outstanding capital stock of MeriStar Hotels in the Spin-Off. The Spin-Off provided the stockholders of CapStar as of the Spin-Off Record Date with the opportunity to participate in the benefits of both the real estate operations of the REIT, and the leasing and management operations of MeriStar Hotels.

Pursuant to an Agreement and Plan of Merger, dated as of March 15, 1998 (the "Merger Agreement"), among American General Hospitality Corporation, a Maryland corporation operating as a real estate investment trust ("AGH"), American General Hospitality Operating Partnership, L.P., a Delaware limited partnership ("AGH Operating Partnership"), CapStar, CapStar Management Company, L.P., a Delaware limited partnership, ("CapStar Management"), and CapStar Management Company II, L.P., a Delaware limited partnership ("CapStar Management II"), as amended, CapStar after spinning-off MeriStar Hotels merged with and into AGH (the "Merger"), with the result that (a) AGH was the surviving corporation operating under the name MeriStar Hospitality Corporation and (b) each outstanding share of common stock, par value \$0.01 per share, of CapStar ("CapStar Common Stock") was converted into 1.0 share of REIT Common Stock, and each outstanding share of common stock, par value \$0.01 per share, of AGH ("AGH Common Stock") was converted into 0.8475 shares of REIT Common Stock.

Immediately following the Spin-Off and the effective date of the Merger, the Company acquired 100% of the partnership interests in the third-party lessee of most of the hotels owned by AGH and substantially all of the assets and certain liabilities of the third-party manager of most of the hotels owned by AGH, pursuant to an Acquisition Agreement, dated as of March 15, 1998 (the "Lessee-Manager Acquisition Agreement"). See "The Merger and the Spin-Off—The Lessee-Manager Acquisition Agreement."

(Continued on next page)

Prior to deciding to exercise the Rights, Rightholders should carefully consider the material risks set forth under "Risk Factors" beginning on page 12 hereof.

THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS THE COMMISSION OR ANY STATE SECURITIES COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

	Subscription Price	Proceeds to Company(1)(2)(3)(4)
Per Share	\$2.84	\$2.81
Total	\$23,856,000	\$23,617,440

- (1) The Company has agreed to indemnify Lehman Brothers Inc. (the "Dealer Manager") against certain liabilities, including liabilities under the Securities Act of 1933, as amended. See "Plan of Distribution."
- (2) The Company has agreed to pay the Dealer Manager a fee equal to the greater of (a) 1% of the aggregate Subscription Price for all Shares sold in the Rights Offering, or (b) \$50,000. The Company has also agreed to reimburse the Dealer Manager for its expenses in connection with its services as Dealer Manager. See "Plan of Distribution."
- (3) Before deducting expenses payable by the Company estimated at \$250,000.
- (4) Assumes the sale of all of the 8,400,000 shares offered hereby.

LEHMAN BROTHERS
Dealer Manager

AVAILABLE INFORMATION

As a result of the Spin-off, MeriStar Hotels is subject to the informational requirements of the Exchange Act, and in accordance therewith will file reports, proxy statements and other information with the Securities and Exchange Commission (the "Commission"). Copies of such reports, proxy statements and other information filed with the Commission can be inspected and copied at the public reference facilities maintained by the Commission at Room 1024, 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549 and at the following Regional Offices of the Commission: 7 World Trade Center, Suite 1300, New York, New York 10048 and Citicorp Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661-2511. Copies of such material can be obtained from the Public Reference Section of the Commission at 450 Fifth Street, N.W., Judiciary Plaza, Washington, D.C. 20549 at prescribed rates. MeriStar Hotels will file information electronically with the Commission, and the Commission maintains a Web Site that contains reports, proxy and information statements and other information regarding registrants that file electronically with the Commission. The address of the Commission's Web Site on the Internet is <http://www.sec.gov>. In addition, the Common Stock is listed on the NYSE. MeriStar Hotels will file reports, proxy and information statements and other information with the NYSE. These documents may be inspected at the offices of the NYSE, 20 Broad Street, New York, New York 10005.

MeriStar Hotels has filed with the Commission a registration statement on Form S-1 (together with all amendments, exhibits and schedules thereto, the "Registration Statement") under the Securities Act, relating to the Rights and the shares of Common Stock that will be issued to Rightholders upon exercise thereof in connection with the Rights Offering. This Prospectus does not contain all of the information set forth in the Registration Statement and the exhibits thereto filed by MeriStar Hotels with the Commission, certain portions of which are omitted in accordance with the rules and regulations of the Commission. Such additional information is available for inspection and copying at the offices of the Commission. Statements contained in this Prospectus as to the contents of any contract or other document referred to herein are not necessarily complete, and in each instance reference is made to the copy of such contract or other document filed as an exhibit to the Registration Statement, each such statement being qualified in all respects by such reference.

The distribution of this Prospectus and the offering of the Rights and the shares of Common Stock in certain jurisdictions may be restricted by law. No action has been taken by MeriStar Hotels that would permit an offering of the Rights or such shares or the circulation or distribution of this Prospectus or any offering material in relation to the Company, the Rights or such shares in any country outside the United States where action for that purpose is required. Persons into whose possession this Prospectus comes are required by the Company to inform themselves about and to observe any such restrictions.

AGH Leasing. Pursuant to the Formation Transactions, the Company leases and manages 201 hotels containing 42,476 rooms (the "Hotels"). Of the Hotels, MeriStar Hotels (i) leases and manages 99 hotels owned by MeriStar Hospitality Corporation, a Maryland corporation operating as a real estate investment trust (the "REIT"), containing 25,854 rooms (the "REIT Owned Hotels"), (ii) leases 47 (of which they manage 36) hotels that are not REIT Owned Hotels containing 6,800 rooms, and (iii) manages an additional 55 hotels that are not REIT Owned Hotels containing 9,822 rooms. The Hotels are located throughout the United States and Canada including most major metropolitan areas and rapidly growing secondary cities. The Hotels include hotels operated under nationally recognized brand names such as Hilton®, Sheraton®, Westin®, Marriott®, Doubletree® and Embassy Suites®. The Company's business strategy is to renovate, reposition and operate each hotel according to a business plan specifically tailored to the characteristics of the hotel and its market. See "The Merger and the Spin-Off," "The Company," "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources" and "Business."

The Spin-Off

CapStar distributed on a share-for-share basis to its stockholders of record as of the effective time of the Merger (the "Spin-Off Record Date") all of the outstanding Common Stock, par value \$0.01 per share, of MeriStar Hotels (the "Common Stock"). The Spin-Off provided the stockholders of CapStar as of the Spin-Off Record Date with the opportunity to participate in the benefits of both ownership of real estate through the REIT, and the leasing and management operations (including the ownership of certain non-real estate assets) of MeriStar Hotels.

The Merger

Pursuant to the Agreement and Plan of Merger dated as of March 15, 1998 (the "Merger Agreement"), among AGH, American General Hospitality Operating Partnership, L.P., a Delaware limited partnership ("AGH Operating Partnership"), CapStar, CapStar Management Company, L.P., a Delaware limited partnership, ("CapStar Management"), and CapStar Management Company II, L.P., a Delaware limited partnership ("CapStar Management II"), as amended, CapStar after spinning-off MeriStar Hotels merged with and into AGH (the "Merger"), with the result that (a) AGH was the surviving corporation operating under the name MeriStar Hospitality Corporation (the "REIT") and (b) each outstanding share of common stock, par value \$0.01 per share of CapStar ("CapStar Common Stock"), was converted into 1.0 share of common stock of the REIT, par value \$0.01 per share ("REIT Common Stock") and each outstanding share of common stock, par value \$0.01 per share of AGH ("AGH Common Stock"), was converted into 0.8475 shares of REIT Common Stock. See "The Merger and the Spin-Off."

("Hotels OP Units"). Upon consummation of the transactions contemplated by the Lessee-Manager Acquisition Agreement, Hotels OP became the lessee and manager of most of the AGH Owned Hotels that were leased and/or managed by AGH Leasing. Pursuant to the Lessee-Manager Acquisition Agreement, the REIT and the Company entered into new lease agreements with respect to all of the CapStar Owned Hotels and amend the lease agreements with respect to most of the AGH Owned Hotels. See "The Merger and the Spin-Off—The Lessee-Manager Acquisition Agreement."

The Rights Offering The distribution of the Rights by the Company and the sale of shares of Common Stock upon the exercise of the Rights are referred to herein as the "Rights Offering."

Rights Non-transferable rights (the "Rights") to subscribe for and purchase shares at the Subscription Price.

Recipients of Rights; Rights Received MeriStar Hotels is distributing the Rights to holders of record of (a) the REIT Common Stock and/or (b) the units of limited partnership (the "REIT OP Units") of the REIT Operating Partnership (other than REIT OP Units held by the REIT or any of its subsidiaries) as of the Record Date defined below. Each holder of record of REIT Common Stock and/or REIT OP Units on the Record Date (a "Rightholder") will receive one-sixth of a Right for each share of REIT Common Stock and/or each REIT OP Unit so held.

Record Date The effective time of the Merger, August 3, 1998, before open of business (the "Record Date").

Expiration Date The Rights will be exercisable at any time following 5:00 p.m., New York City time, on the last day of the Measurement Period until 5:00 p.m., New York City time, on August 31, 1998, or such later date as the Company may determine (the "Expiration Date"), unless the Rights Offering is earlier cancelled.

Subscription Price; Measurement Period \$2.84 per share of Common Stock, which is equal to 95% of the average of the daily high and low prices of the Common Stock on the New York Stock Exchange Inc. ("NYSE") for the period (the "Measurement Period") of five consecutive trading days (a "Trading Day") on the NYSE immediately following the first three Trading Days of the Common Stock on the NYSE (the "Subscription Price").

Subscription Privilege Each whole Right will entitle the Rightholder (but not a subsequent transferee of the REIT Common Stock and/or REIT OP Units held

transactions relating to the Rights on their behalf, should contact the appropriate institution or nominee and request it to effect the transactions for them. Such Rightholders should be aware that brokers or other nominee holders may establish deadlines for receiving instructions from beneficial holders significantly in advance of the Expiration Date. See "The Rights Offering—Exercise of Rights."

Issuance of Common Stock Certificates representing shares of Common Stock purchased pursuant to the exercise of Rights will be delivered to subscribers as soon as practicable following the fourth business day after the Expiration Date. Although fractional Rights will be issued to Rightholders, the Company reserves the right, in its sole discretion, to pay cash in lieu of fractional shares of Common Stock that would otherwise be issued or issuable in respect of fractional Rights exercised by Rightholders, based on a value per whole share of Common Stock equal to the closing price of the Common Stock on the NYSE on the Expiration Date. Any such cash payment will be made to the applicable Rightholder at the same time that shares of Common Stock are issued in respect of whole rights exercised by Rightholders. Fractional Rights can only be exercised concurrently with the exercise of whole Rights. The Company intends to pay cash in lieu of all such fractional shares of Common Stock. See "The Spin-Off and the Merger," "The Rights Offering—Conditions to the Sale of Shares."

Use of Proceeds MeriStar Hotels will use the proceeds of the Rights Offering to repay existing indebtedness and for general corporate purposes. See "Use of Proceeds."

Subscription Agent Continental Stock Transfer & Trust Company.

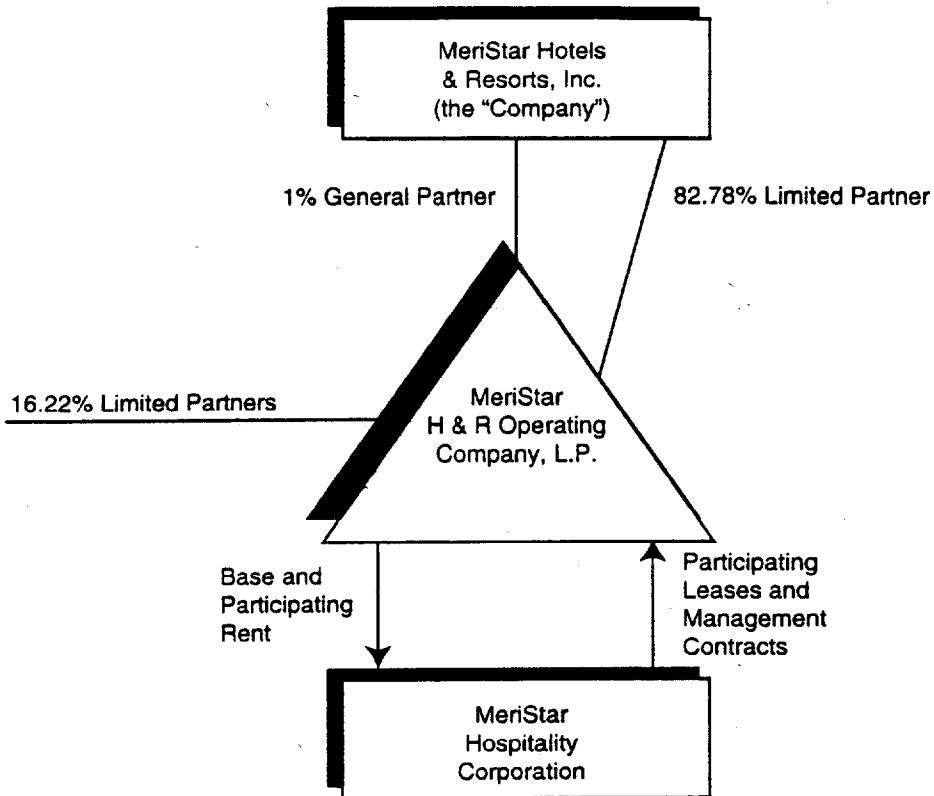
Market for Common Stock; Proposed Trading Symbol The Common Stock is listed on the NYSE, under the symbol "MMH". No listing has been applied for with respect to the Rights.

Risk Factors The purchase of the Common Stock involves certain risks. See "Risk Factors."

Potential Anti-takeover Effect of Certain Provisions of Delaware Law and of the MeriStar Hotels Charter and By-laws Certain provisions of Delaware General Corporation Law ("DGCL") and of the Amended and Restated Certificate of Incorporation of MeriStar Hotels (the "Charter") and the By-Laws of MeriStar Hotels (the "By-laws") may have the effect of

Ownership Structure

The diagram set forth below illustrates the ownership structure of the Company.



Initial Capitalization; Limited Financial Resources

The Company will initially have a \$75 million credit facility, provided by the REIT. CapStar initially capitalized the Company with approximately \$48 million of cash, including approximately \$18 million of forgiveness of indebtedness and a \$30 million draw on the Company's credit facility. In addition, in connection with the consummation of the transactions contemplated by the Lessee—Manager Acquisition Agreement, the Company has drawn an additional \$35 million from the revolving credit facility. The rate on the revolving credit facility will not exceed 350 basis points over LIBOR. There can be no assurance that the Company will be able to satisfy its obligations under, or to pay amounts due under, such revolving credit facility.

Risk of IRS Recharacterization of the Rights Offering

Although MeriStar Hotels, CapStar, AGH, the REIT and the REIT Operating Partnership intend to take the position that the federal income tax treatment of the issuance of Rights to former CapStar stockholders, former AGH stockholders and holders of REIT OP Units is as described in "Federal Income Tax Consequences," it is possible that the Internal Revenue Service ("IRS") might attempt to recharacterize the Rights Offering. For example, in the case of former CapStar and AGH stockholders, it is possible that the IRS could treat the Rights as a distribution of property by CapStar and AGH to their stockholders subject to the rules governing dividend distributions, rather than as boot received by such stockholders in the Merger. It is also possible that, in the case of holders of REIT OP Units, the IRS could view the REIT Operating Partnership, and not MeriStar Hotels, as the distributor of the Rights.

If the distribution of the Rights to former holders of AGH and CapStar Common Stock were treated as a distribution of property by AGH and CapStar to its stockholders, an amount equal to the fair market value of the Rights on the date of distribution would be treated as a dividend to former holders of AGH and CapStar common stock to the extent of the current and accumulated earnings and profits of AGH, in the case of AGH stockholders, or CapStar, in the case of CapStar stockholders, including earnings and profits resulting from the distribution of the Rights. Any amount in excess of the earnings and profits of AGH, in the case of AGH stockholders, or CapStar, in the case of CapStar stockholders, would be treated first as a tax-free return of capital, reducing the stockholder's tax basis in its AGH or CapStar common stock, and any amount in excess of tax basis would be taxable as gain from the sale or exchange of such stockholder's shares of AGH or CapStar common stock. Such gain would be capital gain if such stockholder's shares of AGH or CapStar common stock were held as a capital asset at the time of the AGH recapitalization, in the case of AGH stockholders or at the time of the Merger, in the case of CapStar stockholders.

If the distribution of the Rights to holders of REIT OP Units were treated as a distribution by the REIT Operating Partnership, it would be treated as a distribution by a partnership of marketable securities so that such unit-holder would have to recognize capital gain to the extent that the fair market value of the Rights as of the date of distribution exceeds such holder's basis in such Units. Under such a view, holders of REIT OP Units would take a basis in the Rights equal to the fair market value of the Rights as of the date of distribution.

See "The Rights Offering—Federal Income Tax Consequences" for a description of the potential recharacterization.

Adverse Effects Resulting from the Merger Transactions

Integration Risks

MeriStar Hotels must be able to successfully integrate all of the operations of AGHI and AGH Leasing with and into the management and operating businesses of CapStar, and the REIT must be able to successfully integrate operations for the hotels owned by CapStar (the "CapStar Owned Hotels") and those owned by AGH (the "AGH Owned Hotels"). The consolidation of functions and integration of departments, systems and procedures and the spin-off of MeriStar Hotels to manage the hotels owned by the REIT (the "REIT Owned Hotels") will present a significant management challenge, and the failure to integrate all of such hotels into

Hotels only if the REIT determines, in its sole discretion, that MeriStar Hotels is qualified to be the lessee. Because of the provisions of the Intercompany Agreement and the Charter, the nature of MeriStar Hotels' business and the opportunities it may pursue are restricted.

Conflicts Relating to Sale of Hotels Subject to Leases

The REIT generally will be obligated under its master leases with MeriStar Hotels to pay a lease termination fee to MeriStar Hotels if the REIT elects to sell a hotel or if it elects not to restore a hotel after a casualty and does not replace it with another hotel on terms that would create a leasehold interest in such hotel with a fair market value equal to MeriStar Hotels' remaining leasehold interest under the lease to be terminated. Where applicable, the termination fee is equal to the fair market value of MeriStar Hotels' leasehold interest in the remaining term of the lease to be terminated. A decision to sell a hotel may, therefore, have significantly different consequences for MeriStar Hotels and the REIT.

No Arm's Length Bargaining

The terms of the Intercompany Agreement, the agreement pursuant to which (i) the REIT and the Company will provide to each other a right of first opportunity with respect to certain investment opportunities available to each of them, (ii) the Company will provide certain corporate and other general services to the REIT and (iii) the REIT and the Company agree to cooperate and coordinate with each other with regard to certain matters, was not negotiated on an arm's length basis. Because Messrs. Whetsell, Jorns, Worms and Doctoroff are directors of both the REIT and the Company and Messrs. Whetsell and Jorns are executive officers of both the REIT and the Company, there is a potential conflict of interest with respect to the enforcement and termination of the Intercompany Agreement to benefit the REIT to the detriment of the Company or benefit of the Company to the detriment of the REIT. Because of these conflicts, Messrs. Whetsell, Jorns, Worms and Doctoroff may have conflicts of interest with respect to their decisions relating to the enforcement of the Intercompany Agreement.

Tax Risks in Relationship Between the REIT and MeriStar Hotels

A real estate investment trust generally is not subject to federal corporate income taxes on that portion of its income distributed currently to stockholders. Section 269B(a)(3) of the Internal Revenue Code of 1986, as amended (the "Code") provides that if the shares of a real estate investment trust are stapled with the shares of any other entity, then the real estate investment trust and such other entity shall be treated as one entity for purposes of determining whether the real estate investment trust qualifies as a real estate investment trust for federal income tax purposes. If Section 269B(a)(3) of the Code applied to the Company and the REIT, the REIT would not qualify as a real estate investment trust under the Code. MeriStar Hotels and the REIT are not stapled entities because the Common Stock will be issued independently of the shares of the REIT and will be traded separately as well. However, because at least initially some employees and members of management of the Company and the REIT will be the same, it is possible that the Internal Revenue Service could seek to assert that the Company should be treated as an agent of the REIT or that the Company and the REIT should be treated as one entity for federal income tax purposes. If such assertion were successful, the REIT would not qualify as a real estate investment trust under the Code.

AGH and CapStar received an opinion of counsel in connection with the Merger providing in part that the Company and the REIT would not be treated as stapled entities under Section 269B(a)(3) of the Code and that, based upon the intended operations of each entity and certain other factors and upon representations made by certain persons who are members of management of the Company and the REIT, the separate corporate identities of MeriStar Hotels and the REIT would be respected and the Company would not be treated as an agent of the REIT for federal income tax purposes.

Paper-Clip Structure Risks

Pursuant to the Intercompany Agreement, the Hotel Parties and the REIT Parties will provide each other with reciprocal rights to participate in certain transactions entered into by such parties. In particular, subject to

expenditures. Moreover, the loss of a franchise license could have a material adverse effect upon the operations or the underlying value of the hotel covered by the franchise because of the loss of associated name recognition, marketing support and centralized reservation systems provided by the franchisor. The Franchise Agreements covering the hotels expire or terminate, without specified renewal rights, at various times and have differing remaining terms. As a condition to renewal, the Franchise Agreements frequently contemplate a renewal application process, which may require substantial capital improvements to be made to a hotel.

Competition in the Lodging Industry

The lodging industry is highly competitive. There is no single competitor or small number of competitors of the REIT and MeriStar Hotels that will be dominant in the industry. MeriStar Hotels will operate in areas that contain numerous competitors, some of which may have substantially greater resources than MeriStar Hotels and the ability to accept more risk than MeriStar Hotels will be able to manage. Competition in the lodging industry is based generally on location, room rates and range and quality of services and guest amenities offered. New or existing competitors could significantly lower rates or offer greater conveniences, services or amenities or significantly expand, improve or introduce new facilities in markets in which MeriStar Hotels will compete, thereby adversely affecting MeriStar Hotels' operations and the number of suitable business opportunities.

Costs of Compliance with Environmental Laws

Under various federal, state and local environmental laws, ordinances and regulations, a current or previous owner or operator of real property may be liable for the costs of removal or remediation of hazardous or toxic substances on, under or in such property. Such laws often impose liability whether or not the owner or operator knew of, or was responsible for, the presence of such hazardous or toxic substances. In addition, the presence of contamination from hazardous or toxic substances, or the failure to properly remediate such contaminated property, may adversely affect the owner's ability to sell or rent such real property or to borrow using such real property as collateral. Persons who arrange for the disposal or treatment of hazardous or toxic substances may also be liable for the costs of removal or remediation of such substances at the disposal or treatment facility, whether or not such facility is or ever was owned or operated by such person. The operation and removal of certain underground storage tanks are also regulated by federal and state laws. In connection with the ownership and operation of the hotels, the REIT could be held liable for the costs of remedial action with respect to such regulated substances and storage tanks and claims related thereto. Activities have been undertaken to close or remove storage tanks located on the property of several of the REIT Owned Hotels.

All of the REIT Owned Hotels have undergone Phase I environmental site assessments ("Phase Is"), which generally provide a nonintrusive physical inspection and database search, but not soil or groundwater analyses, by a qualified independent environmental engineer, within the last 18 months. The purpose of a Phase I is to identify potential sources of contamination for which the REIT Owned Hotels may be responsible and to assess the status of environmental regulatory compliance. The Phase Is have not revealed and the Company is not aware of any environmental liability or compliance concerns that MeriStar Hotels believes would have a material adverse effect on MeriStar Hotels' results of operation or financial condition.

In addition, the REIT Owned Hotels have been inspected to determine the presence of asbestos. Federal, state and local environmental laws, ordinances and regulations also require abatement or removal of certain asbestos-containing materials ("ACMs") and govern emissions of and exposure to asbestos fibers in the air. ACMs are present in various building materials such as sprayed-on ceiling treatments, roofing materials or floor tiles at some of the REIT Owned Hotels. Operations and maintenance programs for maintaining such ACMs have been or are in the process of being designed and implemented, or the ACMs have been scheduled to be or have been abated, at such hotels. However, there can be no assurance that this will be the case. Any liability resulting from non-compliance or other claims relating to environmental matters could have a material adverse effect on MeriStar Hotels' results of operations or financial condition.

Governmental Regulation

A number of states regulate the licensing of hotels and restaurants, including liquor license grants, by requiring registration, disclosure statements and compliance with specific standards of conduct. MeriStar Hotels

Potential Antitakeover Effect of Certain Provisions of Delaware Law and of the Charter and By-laws

Certain provisions of Delaware law and of the Charter and By-Laws may have the effect of discouraging a third party from making an acquisition proposal for MeriStar Hotels and could delay, defer or prevent a transaction or a change in control of MeriStar Hotels under circumstances that could otherwise give the holders of Common Stock the opportunity to realize a premium over the then prevailing market prices of the Common Stock. Certain provisions of the Charter and By-laws, as each will be in effect as of the Rights Offering, and of the DGCL, have the effect of making more difficult an acquisition of control of the Company in a transaction not approved by the Board of Directors. These provisions include (i) a provision for a classified Board, with only approximately one-third of the Board to be elected in any year, to serve for three-year terms, (ii) a requirement that directors be removed only for cause upon the affirmative vote of holders of at least 66 $\frac{2}{3}$ % of the total voting power, (iii) a requirement that actions of stockholders be taken at a meeting of stockholders, rather than by written consent, (iv) a prohibition on the stockholders' ability to call a special meeting, (v) an advance notice requirement for stockholders to make nominations of candidates for directors or to bring other business before an annual meeting of stockholders, (vi) a requirement that certain amendments to the Charter and By-Laws be approved by the affirmative vote of 66 $\frac{2}{3}$ % of total voting power and (vii) a provision that the chair of any meeting of stockholders shall have the power to adjourn such meeting. See "Description of Capital Stock" and "Certain Antitakeover Provisions." The Company adopted the Rights Plan prior to the Spin-Off. Certificates issued in the Rights Offering representing Common Stock will also initially represent an equivalent number of associated Preferred Share Purchase Rights. The Rights Plan will make more difficult an acquisition of control of the Company in a transaction not approved by the Company's Board. See "Certain Antitakeover Provisions."

	Three Months Ended March 31,			Year Ended December 31,					
	Pro Forma 1998 (Unaudited)	1998 (Unaudited)	1997 (Unaudited)	Pro Forma 1997 (Unaudited)	1997	1996	1995	1994	1993
(dollars in thousands, except per share data)									
Operating Results:									
Revenue:									
Rooms	\$176,474	\$23,404	\$ —	\$674,197	\$ 9,880	\$ —	\$ —	\$ —	\$ —
Food, beverage and other	65,321	2,576	—	253,906	1,871	—	—	—	—
Management services and other revenues	2,085	4,150	1,139	10,510	12,088	7,050	5,354	4,418	4,234
Total revenues	243,880	30,130	1,139	938,613	23,839	7,050	5,354	4,418	4,234
Operating expenses:									
Departmental expenses:									
Rooms	41,232	5,124	—	165,633	2,533	—	—	—	—
Food, beverage and other	46,755	1,493	—	185,021	1,170	—	—	—	—
Undistributed operating expenses:									
Administrative and general	43,794	6,963	2,202	159,909	10,473	6,140	4,745	4,508	4,065
Participating lease expense	85,592	10,655	—	297,201	4,135	—	—	—	—
Property operating costs	29,962	4,142	—	114,699	1,917	—	—	—	—
Depreciation and amortization	1,224	421	96	4,690	636	349	84	23	14
Total operating expenses	248,559	28,798	2,298	927,153	20,864	6,489	4,829	4,531	4,079
Net operating income (loss)	(4,679)	1,332	(1,159)	11,460	2,975	561	525	(113)	155
Equity in earnings (loss) of affiliates:									
Interest expense, net	2,006	18	14	5,297	56	123	44	—	—
Minority interest	(1,074)	35	—	1,047	103	—	—	—	—
Income tax provision (benefit)	(2,244)	—	—	2,065	—	—	—	—	—
Net income (loss)	\$ (3,367)	\$ 758	\$ (1,173)	\$ 3,097	\$ 2,862	\$ 438	\$ 481	\$ (113)	\$ 155
Basic and diluted net income (loss) per common share	\$ (0.14)	\$ —	\$ —	\$ 0.12	\$ —	\$ —	\$ —	\$ —	\$ —
Balance Sheet Data:									
Total assets	\$198,879	\$84,719	\$25,415	\$ —	\$84,419	\$24,366	\$2,881	\$1,232	\$1,458
Debt	65,776	776	800	—	981	885	950	—	—
Other Financial Data:									
EBITDA (A)	(3,455)	1,753	(1,063)	16,150	3,611	910	609	(90)	169
Net cash provided by (used in) operating activities	(1,583)	2,760	682	9,697	4,465	1,226	208	66	(101)
Net cash used in investing activities	(84,125)	(326)	(902)	(90,300)	(6,501)	(1,826)	(61)	(41)	(24)
Net cash provided by (used in) financing activities	64,795	(205)	(85)	69,208	4,208	699	59	—	244

(A) EBITDA represents earnings before interest expense, income taxes, depreciation and amortization. Management believes that EBITDA is a useful measure of operating performance because (i) it is industry practice to evaluate hotel companies based on operating income before interest, depreciation and amortization and minority interests, which is generally equivalent to EBITDA, and (ii) EBITDA is unaffected by the debt and equity structure of the entity. EBITDA does not represent cash flow from operations as defined by generally accepted accounting principles ("GAAP"), is not necessarily indicative of cash available to fund all cash flow needs, should not be considered as an alternative to net income under GAAP for purposes of evaluating the Company's results of operations and may not be comparable to other similarly titled measures used by other companies.

	Three Months Ended March 31,			Year Ended December 31,					
	Pro Forma 1998 (Unaudited)	1998 (Unaudited)	1997 (Unaudited)	Pro Forma 1997 (Unaudited)	1997	1996	1995	1994	1993
EBITDA Calculation									
Net operating income (loss)	(4,679)	1,332	(1,159)	11,460	2,975	561	525	(113)	155
Add:									
Depreciation and amortization	1,224	421	96	4,690	636	349	84	23	14
EBITDA	(3,455)	1,753	(1,063)	16,150	3,611	910	609	(90)	169

MeriStar Hotels

Unaudited Pro Forma Balance Sheet

March 31, 1998

(dollars in thousands)

	<u>Historical (A)</u>	<u>Spin-Off (B)</u>	<u>Participating Leases (C)</u>	<u>Subtotal</u>	<u>Acquire AGH Leasing and AGHI (D)</u>	<u>Pro Forma</u>
Assets						
Cash and cash equivalents	\$28,602	\$ 30,000	\$ —	\$ 58,602	\$(48,799)	\$ 9,803
Prepaid expenses, deposits and other	17,498	—	37,959	55,457	—	55,457
Intangible and fixed assets, net	38,619	—	—	38,619	95,000	133,619
Total assets	<u>\$84,719</u>	<u>\$ 30,000</u>	<u>\$37,959</u>	<u>\$152,678</u>	<u>\$ 46,201</u>	<u>\$198,879</u>
Liabilities, Minority Interest and Owners'/Stockholders' Equity						
Due to affiliate	\$18,372	\$(18,372)	\$ 871	\$ 871	\$ —	\$ 871
Other liabilities	20,069	—	37,088	57,157	—	57,157
Credit facilities	—	30,000	—	30,000	35,000	65,000
Capital leases and other debt	776	—	—	776	—	776
Total liabilities	<u>39,217</u>	<u>11,628</u>	<u>37,959</u>	<u>88,804</u>	<u>35,000</u>	<u>123,804</u>
Minority interest	3,835	768	—	4,603	11,201	15,804
Common stock	—	249	—	249	—	249
Additional paid-in capital	—	59,022	—	59,022	—	59,022
Retained earnings	—	—	—	—	—	—
Owners' equity	<u>41,667</u>	<u>(41,667)</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>
Owners'/Stockholders' equity	<u>41,667</u>	<u>17,604</u>	<u>—</u>	<u>59,271</u>	<u>—</u>	<u>59,271</u>
Total liabilities, minority interest and owners'/stockholders' equity	<u>\$84,719</u>	<u>\$ 30,000</u>	<u>\$37,959</u>	<u>\$152,678</u>	<u>\$ 46,201</u>	<u>\$198,879</u>

- (A) Reflects the unaudited historical condensed combined balance sheet of the Company as of March 31, 1998.
- (B) Reflects adjustments to capitalize MeriStar Hotels upon the Spin-Off for (i) \$30,000 of cash drawn from MeriStar Hotels' credit facilities, and (ii) contributions of \$18,372 to MeriStar Hotels shareholders (\$17,604) and OP Unit holders (\$768) by CapStar upon forgiveness of \$18,372 due to CapStar.
- (C) Reflects the transfer of net hotel operating assets from CapStar (\$37,959 of operating assets and \$37,088 of operating liabilities) in conjunction with the execution of the Participating Leases and the resulting due to affiliates of \$871 for the amount by which operating assets transferred to MeriStar Hotels exceed operating liabilities assumed by MeriStar Hotels.
- (D) Reflects the acquisitions of AGH Leasing and AGHI for \$95,000. Based on preliminary estimates, the purchase price will be allocated \$26,500 to intangible hotel leases acquired, to be amortized over 26 years (representing the average remaining initial lease terms plus the assumed exercise of three 5-year renewal options) and \$68,500 to goodwill, to be amortized over 35 years. The transaction is to be financed with \$48,799 in cash, an additional \$35,000 drawn from MeriStar Hotels' credit facilities, and \$11,201 in OP Units.

MeriStar Hotels

Unaudited Pro Forma Statement of Operations
Year Ended December 31, 1997
(dollars in thousands except per share amounts)

	Historical(A)	Spin-Off Pro Forma(B)	Participating Leases(C)	Subtotal	Acquire AGH Leasing and AGHI			Pro Forma
					AGH Leasing(D)	AGHI(D)	Other Adjustments(E)	
Revenue from hotel operations:								
Rooms	\$ 9,880	\$68,738	\$343,066	\$421,684	\$252,513	\$ —	\$ —	\$674,197
Food and beverage	1,397	3,316	137,358	142,071	61,655	—	—	203,726
Other	474	3,237	26,265	29,976	20,204	—	—	50,180
Hotel management, accounting and other	12,088	—	(7,238)	4,850	—	7,351	(1,691)	10,510
Total revenue	23,839	75,291	499,451	598,581	334,372	7,351	(1,691)	938,613
Hotel operating expense by department:								
Rooms	2,533	14,300	89,297	106,130	59,503	—	—	165,633
Food and beverage	909	2,215	109,096	112,220	48,406	—	—	160,626
Other operating departments	261	1,648	14,227	16,136	8,259	—	—	24,395
Undistributed operating expenses:								
Administrative and general	10,473	11,169	77,254	98,896	54,873	7,242	(1,102)	159,909
Property operating costs	1,917	12,265	60,265	74,447	47,607	—	(7,355)	114,699
Participating lease expense	4,135	32,002	140,936	177,073	120,128	—	—	297,201
Depreciation and amortization	636	826	—	1,462	104	124	3,000	4,690
Total expenses	20,864	74,425	491,075	586,364	338,880	7,366	(5,457)	927,153
Interest expense and other, net	10	2,775	—	2,785	(373)	(135)	2,974	5,251
Total expenses	20,874	77,200	491,075	589,149	338,507	7,231	(2,483)	932,404
Income (loss) before minority interest and income taxes	2,965	(1,909)	8,376	9,432	(4,135)	120	792	6,209
Minority interest	103	(14)	350	439	(1,663)	—	2,271	1,047
Income (loss) before income taxes	2,862	(1,895)	8,026	8,993	(2,472)	120	(1,479)	5,162
Income tax provision (benefit)	—	387	3,210	3,597	—	—	(1,532)	2,065
Net income (loss)	\$ 2,862	\$(2,282)	\$ 4,816	\$ 5,396	\$(2,472)	\$ 120	\$ 53	\$ 3,097
Basic net income per common share	—	—	—	—	—	—	—	\$ 0.12(F)
Diluted net income per common share	—	—	—	—	—	—	—	\$ 0.12(F)

(A) Reflects the audited historical condensed combined statement of operations of the Company for the year ended December 31, 1997.

(B) Reflects the pre-acquisition operations of the management operations and leases acquired during 1997 as if they were acquired at the beginning of the year. The pre-acquisition operations were obtained from each entity's pre-acquisition financial statements. Also reflects adjustments to (i) record pro forma depreciation and amortization at MeriStar Hotels' cost basis for its acquisitions, (ii) record interest expense of \$2,775 at 9.25% relating to the \$30,000 drawn from MeriStar Hotels' credit facilities, (iii) adjust minority interest for the effects of the acquisitions and (i) and (ii), and (iv) record income taxes at 40% in conjunction with the change in tax status to a C-corporation.

(C) Reflects the execution of the Participating Leases to (i) present a full year of hotel operations for hotels leased from CapStar, (ii) eliminate \$7,238 of management fee revenue earned from CapStar-owned hotels, (iii) adjust minority interest for the effects of (i) and (ii), and (iv) record income taxes at 40%. Lease expense was calculated based on contractual terms of existing leases or expected terms of leases that will be entered into concurrently with the Merger.

**MANAGEMENT'S DISCUSSION AND ANALYSIS OF
FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

General

The Company's financial condition and results of operations both on a pro forma basis as of March 31, 1998 and December 31, 1997 and for the periods then ended and on a historical basis as of March 31, 1998 and 1997 and December 31, 1997 and for the periods then ended reflect differing numbers of managed and leased hotels throughout the periods. The historical results of operations for the years ended December 31, 1996 and 1995 reflect the same number of managed hotels; however, the number of rooms under management increased significantly during 1996. The following table outlines the Company's pro forma and historical portfolio of managed and leased hotels:

	CapStar Hotels Managed		Leased Hotels		Third-Party Hotels Managed		Total	
	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms	Hotels	Rooms
Pro Forma:								
March 31, 1998	—	—	146	32,654	55	9,822	201	42,476
December 31, 1997	—	—	146	32,654	55	9,822	201	42,476
Historical:								
March 31, 1998	55	14,414	45	6,410	40	6,899	140	27,723
December 31, 1997	47	12,019	40	5,687	27	4,631	114	22,337
March 31, 1997	24	6,348	—	—	28	4,482	52	10,830
December 31, 1996	19	5,166	—	—	28	4,619	47	9,785
December 31, 1995	6	2,101	—	—	41	6,089	47	8,190

The increases described above affect the comparability of the Company's financial condition and results of operations for these pro forma and historical periods.

Financial Condition

Pro Forma March 31, 1998 compared with Historical March 31, 1998

Total assets increased by \$114.2 million to \$198.9 million at March 31, 1998 on a pro forma basis from \$84.7 million at March 31, 1998 on a historical basis. The increase is primarily due to the proposed acquisition of AGH Leasing and AGHI for \$95 million. The remaining increase reflects primarily the net effect of the transactions to finance the acquisition of AGH Leasing and AGHI and to execute the leases on CapStar-owned hotels.

Total liabilities increased by \$84.6 million to \$123.8 million at March 31, 1998 on a pro forma basis from \$39.2 million on a historical basis. This overall increase was primarily due to the Company's draws on its revolving credit facilities of \$65.0 million to partially finance both the Spin-Off and the acquisition of AGH Leasing and AGHI. The remaining increase reflects the net effect of this transaction to complete the Spin-Off and to execute the leases on CapStar-owned hotels.

Minority interests increased by \$12.0 million to \$15.8 million on a pro forma basis from \$3.8 million at March 31, 1998 on a historical basis. This increase was due to \$11.2 million in REIT OP Units issued to third parties to finance the acquisition of AGH Leasing and AGHI and allocations to minority interests in the Spin-Off.

Historical March 31, 1998 compared with Historical December 31, 1997

Total assets increased by \$0.3 million to \$84.7 million at March 31, 1998 from \$84.4 million at December 31, 1997. Total liabilities decreased by \$0.5 million to \$39.2 million at March 31, 1998 from \$39.7 million at December 31, 1997. There were no material changes in the Company's financial condition.

Equity in loss of affiliates was \$0.5 million in the three-month period ended March 31, 1998, due to the Company's share of net loss of affiliates accounted for using the equity method. The Company acquired all such investments in affiliates subsequent to March 31, 1997.

Pro Forma Year Ended December 31, 1997 compared with the Historical Year Ended December 31, 1997

Total revenue increased by \$914.8 million to \$938.6 million in 1997 on a pro forma basis compared to \$23.8 million in 1997 on a historical basis. Operating expenses increased to \$927.2 million in 1997 on a pro forma basis from \$20.9 million in 1997 on a historical basis. Net operating income increased to \$6.2 million in 1997 on a pro forma basis compared to \$3.0 million in 1997 on a historical basis, and earnings before interest expense, income taxes, depreciation and amortization ("EBITDA") increased to \$16.1 million in 1997 on a pro forma basis from \$3.6 million in 1997 on a historical basis. These increases result primarily from the increase in total leased and managed hotels on a pro forma basis, as compared to a historical basis.

Net interest and other expense increased by \$5.2 million in 1997 on a pro forma basis from \$0.01 million in 1997 on a historical basis. This increase results from the interest expense on the pro forma outstanding balance on the credit facilities.

Minority interest increased by \$0.9 million in 1997 on a pro forma basis from \$0.1 million in 1997 on a historical basis as a result of the net effect of the changes described above and the issuance of the REIT OP Units in connection with the acquisition of AGH Leasing and AGHI.

The pro forma statement of operations for 1997 reflects income tax expense at an effective rate of 40 percent, as a result of the change in tax status to a C-Corporation.

Historical Year Ended December 31, 1997 compared with the Historical Year Ended December 31, 1996

Total revenue increased by \$16.7 million or 235% to \$23.8 million in 1997 compared to \$7.1 million in 1996. The increase results from revenue of \$11.8 million from hotel leases acquired in 1997 and an increase of \$4.9 million in management fees and other revenue. The Company did not lease any hotels in 1996. The increase in management fees and other revenue is primarily due to the increase in the number of managed hotels in 1997 and additional fees resulting from improved operations of the managed hotels. Hotel management and other revenue earned by the Company from hotels owned by CapStar were \$7.2 million or 30% of total revenue in 1997, and \$2.6 million or 37% of total revenue in 1996.

Operating expenses increased to \$20.9 million in 1997 from \$6.5 million in 1996. This increase reflects the increase in the number of managed hotels and the hotel leases acquired in 1997, which resulted in includes the costs of additional personnel and other administrative costs incurred in conjunction with the Company's growth.

Net operating income increased by 430% to \$3.0 million in 1997 compared to \$0.6 million in 1996 and EBITDA grew to \$3.6 million in 1997 from \$0.9 million in 1996. These increases resulted primarily from the increase in the number of managed hotels and the hotel leases acquired in 1997, offset partially by the costs of additional personnel and other administrative costs incurred as described above.

Minority interests of \$0.1 million in 1997 are due to the Company's allocated portion of minority interests related to the REIT OP Units issued to third parties in 1997.

Historical Year Ended December 31, 1996 compared with the Historical Year Ended December 31, 1995

Total revenue increased to \$7.1 million in 1996 from \$5.4 million in 1995. The growth in management fees and other revenues between 1995 and 1996 reflects the increase in the number of hotel rooms managed and additional fees resulting from improved operations of the managed hotels and new services offered, such as tour and travel services. Hotel management and other revenue earned by the Company from hotels owned by CapStar were \$2.6 million or 37% of total revenue in 1996, and \$0.9 million or 17% of total revenue in 1995.

The Company financed the transactions set forth in the Lessee-Manager Acquisition Agreement by entering into a \$75 million revolving credit facility, provided by the REIT, at an interest rate no greater than LIBOR plus 350 basis points, with other customary terms and conditions. In addition to funding the Lessee-Manager Acquisition Agreement transactions, the available capacity under the new credit facility are expected to be used by the Company to pursue investments in additional joint ventures and to secure additional third-party management arrangements, as discussed above.

Following the Merger, pursuant to the Intercompany Agreement the Company will have a right of first refusal to become the lessee of any real property acquired by the REIT. In addition, the Intercompany Agreement prohibits the Company from making certain acquisitions or investments in real estate unless such acquisitions or investments are first offered to the REIT and the REIT elects not to pursue such acquisitions or investments. As a result of these provisions, the Company's future operations immediately following the Spin-Off and the Merger are expected to rely significantly on the REIT to identify business opportunities for the Company. There is no assurance that MeriStar will identify opportunities for the Company or that any opportunities that either identifies will be within the Company's financial, operational or management parameters.

Also, the Company's current operations after the Merger are predominantly with its affiliate, the REIT; based on pro-forma operating results for 1997, approximately 89% of the Company's revenue is expected to come from hotels owned by and leased from the REIT. Accordingly, the Company's current operations are highly dependent upon the performance of the REIT Owned Hotels.

Following the Spin-Off, Merger and related transactions described above, the Company believes cash generated by operations, together with its new borrowing capacity under its credit facility, will be sufficient to fund its existing working capital, ongoing capital expenditures, debt service requirements, and future acquisitions and investment opportunities. The Company believes these sources of capital are sufficient to provide for the Company's short-term capital needs.

Under the terms of the Participating Leases between the Company and the REIT, the REIT will generally be required to fund significant capital expenditures at the Hotels. Consequently, the Company's ongoing capital expenditures are likely to be substantially reduced from the levels of such expenditures prior to the Formation Transactions. Additionally, the Company expects to finance future acquisitions and investments through a combination of cash generated by operations, borrowing capacity under the credit facility, and the issuance of OP Units and/or Common Stock. The Company believes these sources of capital will be sufficient to provide for the Company's long-term capital needs.

Seasonality

Demand in the lodging industry is affected by recurring seasonal patterns. Demand is lower in the winter months due to decreased travel and higher in the spring and summer months during peak travel season. Therefore, the Company's operations are seasonal in nature. Assuming other factors remain constant, the Company has lower revenue, operating income and cash flow in the first and fourth quarters and higher revenue, operating income and cash flow in the second and third quarters.

Inflation

The rate of inflation has not had a material effect on the revenues or operating results of the Company during the three most recent fiscal years.

Pursuant to the Intercompany Agreement, subject to certain exceptions, the Hotel Parties will have a right of first refusal to become the lessee of any real property acquired by the REIT Parties if the REIT Parties determine that, consistent with the REIT's status as a real estate investment trust, the REIT Parties are required to enter into such a lease arrangement; provided that the Hotel Parties or an entity controlled by the Hotel Parties is, as determined by the REIT in its sole discretion, qualified to be the lessee based on experience in the industry and financial and legal qualifications.

As to opportunities for the Hotel Parties to become the lessee of any assets under a lease arrangement, the Intercompany Agreement provides that the REIT Parties must provide the Hotel Parties with written notice of the lessee opportunity. During the 30 days following such notice, the Hotel Parties have a right of first refusal with regard to the offer to become a lessee and the right to negotiate with the REIT Parties on an exclusive basis regarding the terms and conditions of the lease. If a mutually satisfactory agreement cannot be reached within the 30-day period, or if the Hotel Parties indicate that they are not interested in pursuing the lessee opportunity, the REIT Parties may offer the opportunity to others for a period of one year thereafter, at a price and on terms and conditions that are not more favorable to such other parties than the price and terms and conditions proposed by the REIT Parties to the Hotel Parties, before it must again offer the opportunity to the Hotel Parties in accordance with the procedures specified above.

The REIT Parties and the Hotel Parties will each establish, following the closing of the Merger, a leasing committee which will review all hotel leases to be entered into between the REIT Parties and the Hotel Parties. The REIT Parties' leasing committee will consist of directors of the REIT that are not also directors of MeriStar Hotels and the Hotel Parties' leasing committee will consist of directors of MeriStar Hotels that are not also directors of the REIT.

The Hotel Parties will agree not to acquire or make (i) investments in real estate which, for purposes of the Intercompany Agreement, includes the provision of services related to real estate and investments in hotel properties, real estate mortgages, real estate derivatives or entities that invest in real estate assets or (ii) any other investments that may be structured in a manner that qualifies under the federal income tax requirements applicable to real estate investment trusts unless in either case they have provided written notice to the REIT Parties of the material terms and conditions of the acquisition or investment opportunity, and the REIT Parties have determined not to pursue such acquisitions or investments either by providing written notice to the Hotel Parties rejecting the opportunity within 20 days from the date of receipt of notice of the opportunity or by allowing such 20-day period to lapse. The Hotel Parties also have agreed to assist the REIT Parties in structuring and consummating any such acquisition or investment which the REIT Parties elect to pursue, on terms determined by the REIT Parties.

Provision of Services

The Hotel Parties will provide the REIT Parties with certain services as the REIT Parties may reasonably request from time to time, including administrative, corporate, accounting, financial, insurance, legal, tax, data processing, human resources and operational services. The REIT Parties will compensate the Hotel Parties for services provided in an amount determined in good faith by the Hotel Parties as the amount an unaffiliated third party would charge the REIT Parties for comparable services.

Equity Offerings

If either the REIT Parties or the Hotel Parties desire to engage in a securities issuance (the "Issuing Party"), then such Issuing Party will give notice to such other party (the "Non-Issuing Party") as promptly as practicable of their desire to engage in a securities issuance. The Non-Issuing Party will cooperate with the Issuing Party to effect any securities issuance of the Issuing Party by assisting in the preparation of any registration statement or other document required in connection with such issuance and, in connection therewith, providing the Issuing Party with such information as may be required to be included in such registration statement or other document.

Term

The Intercompany Agreement will terminate upon the earlier of (a) the tenth anniversary of the date of the Intercompany Agreement, and (b) a change in ownership or control of MeriStar Hotels.

CAPITALIZATION

The following table sets forth the historical and pro forma capitalization of the Company as of March 31, 1998. The pro forma capitalization is adjusted to reflect the Formation Transactions. The information below should be read in conjunction with the historical combined financial statements and notes thereto of the Company and the Unaudited Pro Forma Financial Statements and notes thereto of the Company included elsewhere in this Prospectus.

	As of March 31, 1998 (in thousands, except share data)	
	Pro Forma (unaudited)	Historical
Liabilities and Minority Interest:		
Credit facilities	\$ 65,000	\$ —
Capital leases and other debt	776	776
Minority interest	<u>15,804</u>	<u>3,835</u>
Total liabilities and minority interest	<u>81,580</u>	<u>4,611</u>
Owners'/Stockholders' Equity:		
Owners' Equity	—	41,667
Preferred Stock (\$0.01 par value, 10,000,000 shares authorized, no shares issued or outstanding)	—	—
Common Stock (\$0.01 par value, 100,000,000 shares authorized 24,890,355 shares issued and outstanding on a pro forma basis) ..	249	—
Additional paid-in capital and retained earnings	<u>59,022</u>	<u>—</u>
Total owners'/stockholders' equity	<u>59,271</u>	<u>41,667</u>
Total capitalization	<u><u>\$140,851</u></u>	<u><u>\$46,278</u></u>

DIVIDEND POLICY

The Company has not paid any cash dividends on the Common Stock and does not anticipate that it will do so in the foreseeable future. The Company intends to retain earnings to provide funds for the continued growth and development of the Company's business. Loan agreements and leases to be entered into by the Company may restrict the Company's ability to pay dividends on the Common Stock. Any determination to pay cash dividends in the future will be at the discretion of the Board of Directors and will be dependent upon the Company's results of operations, financial condition, contractual restrictions and other factors deemed relevant by the Board of Directors.

activities in addition to their investment interest in the REIT itself. A small number of real estate investment trusts, operating under tax provisions that no longer are available to newly formed real estate investment trusts, have shares that are "paired" or "stapled" with shares of a related operating company, and therefore cannot be owned or transferred independently. The shares of MeriStar Hotels and the REIT are not, and will not be, paired or stapled in any manner. Because the shares of the REIT and MeriStar Hotels can be owned and transferred separately and independently of each other, the REIT and MeriStar Hotels will not provide a paired investment on an ongoing basis to investors who purchase or sell shares of only one company or the other.

Although the Spin-Off was not to be effected unless the Merger was approved by the stockholders of CapStar and AGH and all other conditions precedent were satisfied or waived, the Spin-Off was separate from the Merger and the shares of MeriStar Hotels received by holders of CapStar Common Stock in the Spin-Off did not constitute a part of the Merger consideration. The stockholders of CapStar were asked to vote on the approval and adoption of the Merger Agreement, and were not asked to vote on the Spin-Off.

Restructuring and Spin-Off

General

In order to effectuate the Spin-Off, CapStar effected a series of mergers, asset and stock transfers and liability assumptions among itself and its subsidiaries (the "CapStar OP Restructuring"). The purpose and effect of the CapStar OP Restructuring was to separate substantially all of the management and leasing business of CapStar from the real estate investments of CapStar.

Substantially all of CapStar's assets were held indirectly by and operated through CapStar Management and CapStar Management II, CapStar's subsidiary operating partnerships. CapStar was the sole general partner of CapStar Management, and CapStar, certain wholly owned subsidiaries of CapStar (the "CapStar LP Entities"), and certain third parties were the sole limited partners of CapStar Management. CapStar General Corp., a wholly-owned subsidiary of CapStar ("CapStar General"), was the sole general partner of CapStar Management II, and CapStar Limited Corp., a wholly owned subsidiary of CapStar General ("CapStar Limited"), and certain third parties were the sole limited partners of CapStar Management II. The partnership agreements of CapStar Management and CapStar Management II gave the general partner full control over the business and affairs of the partnerships.

The Contributions

Prior to the effectiveness of the Merger, CapStar Management and CapStar Management II effectuated the following transactions (the "Contributions"):

1. Each of the CapStar LP Entities, CapStar General and CapStar Limited merged with and into CapStar;

2. Each of CapStar Management and CapStar Management II converted into a limited liability company (respectively, "CapStar Management LLC" and "CapStar Management II LLC").

3. CapStar Management LLC contributed all of its hotel related assets together with certain other assets, subject to all of its liabilities except as set forth in the Merger Agreement, to CapStar Hotel Operating Company, L.L.C., a newly-formed Delaware limited liability company ("CapStar Hotel LLC"), in exchange for interests in CapStar Hotel LLC and CapStar Management II LLC contributed all of its hotel related assets together with certain other assets, subject to all of its liabilities except as set forth in the Merger Agreement, to CapStar Hotel Operating Company, L.L.C., a newly-formed Delaware limited liability company ("CapStar Hotel II LLC"), in exchange for interests in CapStar Hotel II LLC;

4. CapStar Management contributed all its management and substantially all its leasehold related assets, together with certain other assets (including cash), subject to \$30 million in indebtedness and certain other liabilities, to Hotels OP in exchange for interests in Hotels OP and CapStar Management II LLC

MeriStar Hotels established new employee benefit plans substantially similar to the existing CapStar benefit plans, including but not limited to an Equity Incentive Plan and a Stock Purchase Plan. Employees who held CapStar Stock Options were granted new stock options in the REIT and MeriStar Hotels.

The Lessee-Manager Acquisition Agreement

Pursuant to the Lessee-Manager Acquisition Agreement, following the Spin-Off and immediately after the effective time of the Merger, Hotels OP acquired: (i) substantially all of the assets and certain liabilities of AGHI for a cash purchase price of \$10 million; and (ii) 100% of the partnership interests in AGH Leasing for a purchase price of \$85 million, consisting of approximately \$73.8 million in cash and approximately \$11.2 million in the form of Hotels OP Units convertible into Common Stock. Upon consummation of the transactions contemplated by the Lessee-Manager Acquisition Agreement, Hotels OP became the lessee and manager of most of the AGH Owned Hotels that are currently leased by AGH Leasing. The REIT and MeriStar Hotels entered into new lease agreements (the "Participating Leases") with respect to all of the CapStar Owned Hotels and amended the lease agreements with respect to most of the AGH Owned Hotels. See "Business—The Participating Leases."

Indemnification Obligations

MeriStar Hotels will indemnify, defend and hold harmless the REIT and its affiliates and any directors, officers, employees and agents of the foregoing, from and against any losses arising out of or resulting from the Assumed Liabilities, the Contributed Assets or the business and operations of Hotels OP.

The REIT will indemnify, defend and hold harmless MeriStar Hotels, its affiliates and their respective successors and any directors, officers, employees and agents of the foregoing, from and against any losses arising out of any assets or liabilities retained by the REIT and its affiliates.

such as business, group and leisure travelers. These facilities typically include large, upscale guest rooms, food and beverage facilities, extensive meeting and banquet space, and amenities such as health clubs, swimming pools and adequate parking.

Potential Performance Improvements. The Company seeks to operate underperforming hotels where intensive management and selective capital improvements can increase revenue and cash flow. These hotels represent opportunities where a systematic management approach and targeted renovations should result in improvements in revenue and cash flow.

The Company expects that its relationships throughout the industry will continue to provide it with a competitive advantage in identifying, evaluating and managing hotels that meet its criteria. Management has a record of successfully renovating and repositioning hotels, in situations with varying levels of service, room rates and market types, and the Company plans to continue such renovation programs as it acquires new leases and management contracts.

Operating Strategy

The Company's principal operating objectives will be to generate higher RevPAR and to increase net operating income while providing its hotel guests with high-quality service and value. The Company will seek to achieve these objectives by creating and executing management plans that are specifically tailored for each individual Hotel rather than by implementing an operating strategy that is designed to maintain a uniform corporate image or brand. Management believes that custom-tailored business plans are the most effective means of addressing the needs of a given hotel or market. The Company believes that skilled management of hotel operations is the most critical element in maximizing revenue and cash flow in hotels, especially in upscale, full-service hotels.

The Company's corporate headquarters will carry out financing and investment activities and provide services to support as well as monitor the Company's on-site hotel operating executives. Each of the Company's executive departments, including Sales and Marketing, Human Resources and Training, Food and Beverage, Technical Services, Development and Corporate Finance, will be headed by an executive with significant experience in that area. These departments will support decentralized decision-making by the hotel operating executives by providing accounting and budgeting services, property management software and other resources which cannot be economically maintained at the individual Hotels.

Key elements of the Company's management programs include the following:

Comprehensive Budgeting and Monitoring. The Company's operating strategy begins with an integrated budget planning process that is implemented by individual on-site managers and monitored by the Company's corporate staff. Management sets targets for cost and revenue categories at each of the Hotels based on historical operating performance, planned renovations, operational efficiencies and local market conditions. On-site managers coordinate with the central office staff to ensure that such targets are realistic. Through effective and timely use of its comprehensive financial information and reporting systems, the Company will be able to monitor actual performance and rapidly adjust prices, staffing levels and sales efforts to take advantage of changes in the market and to improve yield.

Targeted Sales and Marketing. The Company will employ a systematic approach toward identifying and targeting segments of demand for each Hotel in order to maximize market penetration. Executives at the Company's corporate headquarters and property-based managers will divide such segments into smaller subsegments, typically ten or more for each Hotel, and develop narrowly tailored marketing plans to suit each such segment. The Company will support each Hotel's local sales efforts with corporate sales executives who will develop new marketing concepts and monitor and respond to specific market needs and preferences. These executives will be active in implementing on-site marketing programs developed in the central management office. The Company will employ computerized revenue yield management systems to manage each Hotel's use

The following chart summarizes certain information with respect to the national franchise affiliations of the Hotels:

Franchise	REIT Owned Hotels			Third-Party Leased Hotels			Third-Party Managed Hotels		
	Guest Rooms	Hotels	% of Rooms	Guest Rooms	Hotels	% of Rooms	Guest Rooms	Hotels	% of Rooms
Hilton	5,499	21	21%	—	—	—	225	1	2%
Sheraton	2,978	9	11%	—	—	—	167	1	2%
Radisson [®]	2,712	9	10%	—	—	—	756	4	8%
Doubletree	2,055	6	8%	388	1	6%	363	2	4%
Marriott	1,494	4	5%	—	—	—	—	—	—
Holiday Inn [®]	2,571	12	10%	367	2	5%	1,763	9	18%
Embassy Suites	728	3	3%	—	—	—	248	1	3%
Westin	1,296	4	5%	—	—	—	—	—	—
Wyndham	1,122	3	4%	219	1	3%	—	—	—
Independent	674	6	3%	—	—	—	1,151	10	12%
Four Points [®]	213	1	1%	—	—	—	400	1	4%
Doubletree Guest Suites [®]	292	2	1%	—	—	—	—	—	—
Ramada [®]	665	3	3%	—	—	—	1,037	5	10%
Crowne Plaza [®]	715	3	3%	—	—	—	730	2	7%
Courtyard [®]	1,044	5	4%	490	3	7%	455	2	5%
Hilton Garden Inn	—	—	—	474	3	7%	—	—	—
Hilton Suites	—	—	—	—	—	—	174	1	2%
Comfort Suites [®]	—	—	—	277	2	4%	359	3	4%
Clarion [®]	—	—	—	—	—	—	432	2	4%
Quality Suites [®]	—	—	—	168	1	2%	177	1	2%
Residence Inn [®]	—	—	—	—	—	—	391	3	4%
Quality Inn [®]	—	—	—	—	—	—	265	2	3%
Days Inn [®]	—	—	—	—	—	—	96	1	1%
Holiday Inn Express [®]	159	1	1%	208	2	3%	78	1	1%
Best Western [®]	—	—	—	—	—	—	355	2	4%
Hampton Inn [®]	292	2	1%	1,965	16	29%	—	—	—
Comfort Inn [®]	—	—	—	1,293	9	19%	—	—	—
Holiday Inn Select [®]	1,245	4	5%	244	1	4%	—	—	—
Homewood Suites [®]	—	—	—	461	4	7%	—	—	—
Howard Johnson	100	1	1%	—	—	—	—	—	—
Hampton Inn & Suites [®]	—	—	—	136	1	2%	—	—	—
Fairfield Inn [®]	—	—	—	110	1	2%	200	1	2%
Total	<u>25,854</u>	<u>99</u>	<u>100.0%</u>	<u>6,800</u>	<u>47</u>	<u>100.0%</u>	<u>9,822</u>	<u>55</u>	<u>100%</u>

Emphasis on Food and Beverage. Management believes popular food and beverage ideas are a critical component in the overall success of a hotel. The Company utilizes its food and beverage operations to create local awareness of its hotel facilities, to improve the profitability of its hotel operations and to enhance customer satisfaction. The Company is committed to competing for patrons with restaurants and catering establishments by offering high-quality restaurants that garner positive reviews and strong local and/or national reputations. The Company has engaged food and beverage experts to develop several proprietary restaurant concepts. The REIT Owned Hotels contain restaurants ranging from Michel Richard's highly acclaimed CITRONELLE[®], to Morgan's[®], a CapStar-designed concept which offers popular, moderately-priced American cuisine. CapStar has also successfully placed national food franchises such as Starbuck's Coffee[®] and "TCBY"[®] Yogurt in casual, delicatessen-style restaurants in several of the REIT Owned Hotels. Popular food concepts will strengthen the Company's ability to attract business travelers and group meetings and improve the name recognition of the Hotels.

Commitment to Service and Value. The Company is dedicated to providing exceptional service and value to its customers on a consistent basis. The Company conducts extensive employee training programs to ensure personalized service at the highest levels. Programs such as "Be A Star" have been created and implemented by

Properties

The Company maintains its corporate headquarters in Washington, D.C., satellite offices in California, North Carolina and Texas and leases and/or manages hotel properties throughout the United States and Canada. The Company leases its offices. No one hotel property is material to the operation of the Company. A typical Hotel has meeting and banquet facilities, food and beverage facilities and guest rooms and suites.

The REIT Owned Hotels feature, or after contemplated renovation programs have been completed will feature, comfortable, modern guest rooms, extensive meeting and convention facilities and full-service restaurant and catering facilities that attract meeting and convention functions from groups and associations, upscale business and vacation travelers as well as banquets and receptions from the local community.

The following table sets forth the 1997 operating information with respect to the hotels owned by the REIT and leased and managed by the Company:

<u>Hotel</u>	<u>Location</u>	<u>Guest Rooms</u>	<u>Average Daily Rate ("ADR")</u>	<u>Average Occupancy</u>	<u>Rev PAR</u>
Sheraton Hotel	Mesa, AZ	273	\$ 89.49	53.6%	47.97
Crowne Plaza Phoenix	Phoenix, AZ	249	72.83	63.7	46.29
Embassy Suites	Tucson, AZ	204	74.39	78.5	58.40
Courtyard by Marriott Century City	Century City, CA	134	106.02	84.1	89.13
Orange County Airport Hilton	Irvine, CA	290	85.87	73.0	62.69
Marriott Hotel	Los Angeles, CA	469	118.56	60.5	71.73
Courtyard by Marriott Marina del Rey	Marina del Rey, CA	276	79.78	90.4	72.04
Monterey Hilton	Monterey, CA	204	107.33	66.4	71.29
DoubleTree Resort	Palm Springs, CA	289	97.45	66.9	65.19
Sacramento Hilton	Sacramento, CA	326	86.74	74.4	64.53
Holiday Inn Select Mission Valley	San Diego, CA	317	71.99	72.6	52.25
Sheraton Fisherman's Wharf	San Francisco, CA	524	133.28	84.5	112.62
Crowne Plaza Park Center	San Jose, CA	239	111.80	70.2	78.48
Wyndham San Jose Airport Hotel	San Jose, CA	356	115.93	59.3	68.76
San Pedro Hilton	San Pedro, CA	226	61.66	76.3	47.05
Santa Barbara Inn	Santa Barbara, CA	71	139.35	79.7	111.06
Holiday Inn	Colorado Springs, CO	201	67.16	70.7	47.48
Sheraton Hotel	Colorado Springs, CO	502	74.15	72.1	53.46
Embassy Suites Denver	Englewood, CO	236	103.75	76.2	79.06
Mystic Hotel	Mystic, CT	77	77.63	58.0	45.06
DoubleTree Bradley Airport	Windsor Locks, CT	200	84.27	67.4	56.80
Embassy Row Hilton	Washington, DC	195	119.63	73.5	87.93
Georgetown Inn	Washington, DC	95	137.95	72.4	99.88
The Latham Hotel	Washington, DC	143	113.32	81.1	91.90
DoubleTree Resort Surfside Clearwater Beach	Clearwater Beach, FL	426	101.12	70.9	71.72
Ramada Inn Gulfview Clearwater Beach	Clearwater Beach, FL	289	72.85	60.7	44.19
Hilton Hotel Cocoa Beach	Cocoa Beach, FL	296	83.31	72.2	60.11
Holiday Inn Fort Lauderdale Beach	Fort Lauderdale, FL	240	75.95	77.2	58.66
Westin Resort Key Largo	Key Largo, FL	200	126.87	76.8	97.19
Howard Johnson Resort Key Largo	Key Largo, FL	100	86.06	83.4	71.77
Courtyard by Marriott Disney Village	Lake Buena Vista, FL	323	105.41	93.8	98.89
Holiday Inn Madeira Beach	Madeira Beach, FL	149	77.36	55.8	43.16
Radisson Twin Towers Orlando	Orlando, FL	742	81.10	78.5	63.34
Wyndham Safari Resort Lake Buena Vista	Orlando, FL	490	73.67	66.3	48.81
DoubleTree Hotel Tampa Airport	Tampa, FL	496	64.05	68.3	43.73
DoubleTree Guest Suites Atlanta	Atlanta, GA	155	104.90	61.4	64.42
Westin Atlanta Airport	Atlanta, GA	496	79.18	75.5	59.78
Jekyll Inn	Jekyll Island, GA	265	63.15	46.6	29.43
Radisson Hotel Arlington Heights	Arlington Heights, IL	201	81.72	74.5	60.88
Radisson Hotel & Suites	Chicago, IL	341	134.71	81.2	109.38
Holiday Inn Chicago O'Hare International Airport	Rosemont, IL	507	99.15	78.6	77.89
Radisson Hotel	Schaumburg, IL	202	83.59	75.9	63.44

The Participating Leases

Prior to the effective date of the Merger, MeriStar Hotels, operating through Hotels OP, entered into a lease with the REIT or its respective subsidiary (a "Participating Lease") for each CapStar Owned Hotel. In addition, the Company and AGH Leasing entered into amended and restated Participating Leases with the REIT for each of the AGH Owned Hotels that was leased by AGH Leasing, which conformed the Participating Leases for the applicable AGH Owned Hotels with the Participating Leases for the CapStar Owned Hotels, except that (a) the base rent and percentage rent for each Participating Lease of an applicable AGH Owned Hotel was not modified (except as described below with respect to "discounted revenues") and (b) the initial term of each Participating Lease of an applicable AGH Owned Hotel was not modified (though renewal options will be added).

The obligations of Lessee under each Participating Lease are guaranteed by MeriStar Hotels.

Term

Each Participating Lease of an AGH Owned Hotel provides for an initial term of 12 years commencing on the date on which the hotel was acquired. Each Participating Lease of a CapStar Owned Hotel provides for an initial term of 12 years commencing on the effective date of the Merger. Each Participating Lease of an AGH Owned Hotel will be modified to provide, and each Participating Lease of a CapStar Owned Hotel will provide, Lessee with three renewal options of five years each (except in the case of Properties with ground leases having a remaining term of less than 40 years) provided that (a) Lessee will not have the right to a renewal if there shall have occurred a change in the tax law which would permit the REIT to operate the hotel directly; (b) if Lessee shall elect not to renew a Participating Lease for any REIT Owned Hotel, then the REIT shall have the right to reject the exercise of a renewal right on a Participating Lease of a comparable hotel; and (c) the rent for each renewal term shall be adjusted to reflect the then fair market rental value of the hotel. If the REIT and MeriStar Hotels are unable to agree upon the then fair market rental value of the hotel, the Participating Lease will terminate upon the expiration of the then current term and MeriStar Hotels shall thereupon have a right of first refusal to lease the hotel from the REIT on such terms as the REIT may have agreed upon with a third-party lessee.

Base Rent; Participating Rent; Additional Charges

Each Participating Lease requires the lessee to pay (i) fixed monthly base rent, (ii) on a monthly basis, the excess of participating rent over base rent, with participating rent based on certain percentages of room revenue, food and beverage revenue and telephone and other revenue at each hotel, and (iii) certain other amounts, including interest accrued on any late payments or charges ("Additional Charges"). Base rent and participating rent departmental thresholds (departmental revenue on which the rent percentage is based) are increased annually by a percentage equal to the percentage increase in the consumer price index ("CPI") (CPI percentage increase plus 0.75% in the case of the participating rent departmental revenue threshold) compared to the price year. In addition, under certain circumstances a reduced percentage rate will apply to the revenues attributable to certain "discounted rates" that the Lessee may offer. Base rent is payable monthly in arrears. Participating rent is payable in arrears based on a monthly schedule adjusted to reflect the seasonal variations in the hotel's revenue. Participating rent payments during each calendar quarter will be adjusted at the end of each quarter to reflect actual results.

Other than real estate and personal property taxes and assessments, rent payable under ground leases, casualty insurance, including loss of income insurance, capital impositions and capital replacements and refurbishments (determined in accordance with generally accepted accounting principles), which are obligations of the REIT, the Participating Leases require the Lessee to pay rent, liability insurance, all costs and expenses and all utility and other charges incurred in the operation of the hotels. The Participating Leases also provide for rent reductions and abatements in the event of damage or destruction or a partial taking of any hotel.

The Participating Leases also provide for a rental adjustment under certain circumstances in the event of (a) a major renovation of the hotel, or (b) a change in the franchisor of the hotel.

THE RIGHTS OFFERING

MeriStar Hotels is distributing the Rights to holders of record of (a) the REIT Common Stock and/or (b) the REIT OP Units (other than REIT OP Units held by the REIT or any of its subsidiaries) as of the Record Date. Each Rightholder will receive one sixth of a Right for each share of REIT Common Stock and/or each REIT OP Unit so held. Each whole Right will be exercisable for one share of Common Stock. Although fractional Rights will be issued to Rightholders, the Company reserves the right, in its sole discretion, to pay cash in lieu of fractional shares of Common Stock that would otherwise be issued or issuable in respect of fractional Rights exercised by Rightholders, based on a value per whole share of Common Stock equal to the closing price of the Common Stock on the NYSE on the Expiration Date. Any such cash payment will be made to the applicable Rightholder at the same time that shares of Common Stock are issued in respect of whole Rights exercised by Rightholders. Fractional Rights can only be exercised concurrently with the exercise of whole Rights. The Company intends to pay cash in lieu of all such fractional shares of Common Stock.

Expiration Date

The Rights will be exercisable at any time following 5:00 p.m., New York City time, on the last day of the Measurement Period until the Expiration Date. After the Expiration Date, unexercised Rights will be null and void. The Company will not be obligated to honor any purported exercise of Rights received by the Subscription Agent after the Expiration Date, regardless of when the documents relating to such exercise were sent, except pursuant to the Guaranteed Delivery Procedures described below. Notice of any extension of the Expiration Date will be made through a press release issued by the Company.

Subscription Privilege

Each whole Right will entitle the Rightholder (but not a subsequent transferee of the REIT Common Stock and/or REIT OP Units held by such Rightholder on the Record Date) to purchase one share of Common Stock at the Subscription Price. Certificates representing shares of Common Stock purchased pursuant to the Subscription Privilege will be delivered to subscribers as soon as practicable after the fourth business day following the Expiration Date.

Conditions to Sale of Shares

All amounts received by the Subscription Agent pursuant to the exercise of Rights will be held in a non-interest-bearing escrow account until the completion of the Rights Offering. If the Rights Offering is not completed, all funds received by the Subscription Agent in payment of the Subscription Price and held in escrow by the Subscription Agent will be returned by mail without interest or deduction as soon as practicable following the termination or expiration of the Rights Offering.

Exercise of Rights

Rights may be exercised by Rightholders by delivering to the Subscription Agent, at or prior to the Expiration Date, the properly completed and executed Subscription Certificate evidencing such Rights with any required signatures guaranteed, together with payment in full of the Subscription Price for each share subscribed for pursuant to the Subscription Privilege. Such payment in full must be by (a) check or bank draft drawn upon a United States bank or postal, telegraphic or express money order payable to Continental Stock Transfer & Trust Company, as Subscription Agent, or (b) wire transfer of funds to the account maintained by the Subscription Agent for such purpose at 2 Broadway, New York, New York 10004, The Chase Manhattan Bank Account No. 777011379; ABA No. 021000021. Any wire transfer of funds should clearly indicate the identity of the subscriber who is paying the Subscription Price by the wire transfer. The Subscription Price will be deemed to

Rightholders who hold Rights for the account of others, such as brokers, trustees or depositaries for securities, should provide a copy of this Prospectus to the respective beneficial owners of such Rights as soon as possible, ascertain such beneficial owners' intentions and obtain instructions with respect to the Rights. If the beneficial owner so instructs, the record Rightholder should complete Subscription Certificates and submit them to the Subscription Agent with the proper payment. In addition, beneficial owners of Rights held through such a Rightholder should contact the Rightholder and request the Rightholder to effect transactions in accordance with the beneficial owner's instructions. Beneficial holders should be aware that brokers or other record Rightholders may establish deadlines for receiving instructions from beneficial holders significantly in advance of the Expiration Date.

The instructions accompanying the Subscription Certificates should be read carefully and followed in detail.

The Company anticipates that the exercise of the Subscription Privilege may be effected through the facilities of The Depository Trust Company.

DO NOT SEND SUBSCRIPTION CERTIFICATES TO THE COMPANY, AGH, CAPSTAR OR ANY OF THEIR AFFILIATES, BUT RATHER SEND THEM TO THE SUBSCRIPTION AGENT AS REFERENCED ABOVE.

THE METHOD OF DELIVERY OF SUBSCRIPTION CERTIFICATES AND PAYMENT OF THE SUBSCRIPTION PRICE TO THE SUBSCRIPTION AGENT WILL BE AT THE ELECTION AND RISK OF THE Rightholders, BUT IF SENT BY MAIL IT IS RECOMMENDED THAT SUCH CERTIFICATES AND PAYMENTS BE SENT BY REGISTERED MAIL, PROPERLY INSURED, WITH RETURN RECEIPT REQUESTED, AND THAT A SUFFICIENT NUMBER OF DAYS BE ALLOWED TO ENSURE DELIVERY TO THE SUBSCRIPTION AGENT AND CLEARANCE OF PAYMENT AT OR PRIOR TO THE EXPIRATION DATE. BECAUSE UNCERTIFIED, PERSONAL CHECKS MAY TAKE UP TO FIVE BUSINESS DAYS TO CLEAR, Rightholders ARE STRONGLY URGED TO PAY, OR ARRANGE FOR PAYMENT, BY MEANS OF CERTIFIED OR CASHIER'S CHECK, MONEY ORDER OR WIRE TRANSFER OF FUNDS.

All questions concerning the timeliness, validity, form and eligibility of any exercise of Rights will be determined by the Company, whose determinations will be final and binding. The Company in its sole discretion may waive any defect or irregularity, or permit a defect or irregularity to be corrected within such time as it may determine, or reject the purported exercise of any Right. Subscriptions will not be deemed to have been received or accepted until all irregularities have been waived or cured within such time as the Company determines in its sole discretion. The Company reserves the right to reject any purchases not properly submitted or the acceptance of which would, in the opinion of its counsel, be unlawful. Neither the Company nor the Subscription Agent will be under any duty to give notification of any defect or irregularity in connection with the submission of Subscription Certificates, or incur any liability for failure to give such notification.

Any questions or requests for assistance concerning the method of exercising Rights or requests for additional copies of this Prospectus, the Instructions or the Notice of Guaranteed Delivery should be directed to the Subscription Agent.

No Revocation

ONCE A Rightholder HAS EXERCISED THE SUBSCRIPTION PRIVILEGE, SUCH EXERCISE MAY NOT BE REVOKED.

Rights Not Transferable

The Rights may not be transferred. The Rights will entitle only a Rightholder (but not a subsequent transferee of the REIT Common Stock and/or REIT OP Units held by such Rightholder on the Record Date) to purchase shares of Common Stock at the Subscription Price. In the event that Rightholders transfer REIT Common Stock and/or REIT OP Units owned by them as of the Record Date, they will remain the owners of Rights issued in respect of such shares of REIT Common Stock and/or such REIT OP Units.

share of the undistributed earnings and profits of CapStar as of the effective time of the Merger, and any excess will be treated as gain from the exchange of property. Such gain will be capital gain if such shares of CapStar common stock were held as a capital asset at the effective time of the Merger.

In general, the determination as to whether the gain recognized by a CapStar stockholder in the Merger will be treated as capital gain or dividend income depends upon whether and to what extent the transactions related to the Merger will be deemed to reduce the stockholder's percentage ownership of the REIT following the Merger. For purposes of that determination, the stockholder is treated as if it first exchanged all of its shares of CapStar common stock solely for REIT Common Stock and then the REIT immediately redeemed (the "deemed redemption") a portion of such REIT Common Stock in exchange for the boot the stockholder actually received. If, under section 302 of the Code, the deemed redemption is "substantially disproportionate" with respect to a CapStar stockholder, the gain recognized will be treated as capital gain. One requirement that must be met in order for the deemed redemption to be "substantially disproportionate" is that the percentage of the outstanding voting stock of the REIT following the Merger and the deemed redemption considered owned by the stockholder is less than 80% of the percentage of the outstanding voting stock of the REIT considered owned by the stockholder following the Merger but immediately before the deemed redemption. Based on calculations of the relative values of the REIT Common Stock, the Common Stock of MeriStar Hotels and the Rights to be received by former holders of CapStar common stock, it is anticipated that the deemed redemption will not be "substantially disproportionate" with respect to holders of CapStar Common Stock. Accordingly, unless a CapStar stockholder qualifies for the exception described below, the gain recognized by such shareholder will be taxed as dividend income to the extent of the accumulated earnings and profits of CapStar at the time of Merger.

However, section 302 of the Code also provides that if the deemed redemption is "not essentially equivalent to a dividend" with respect to the stockholder, then any gain recognized by the stockholder in the transaction will be capital gain. In general, in order for the deemed redemption to be "not essentially equivalent to a dividend", the deemed redemption must result in a "meaningful reduction" in the stockholder's deemed percentage stock ownership of the REIT following the Merger. That determination generally requires a comparison of (i) the percentage of the outstanding stock of the REIT the stockholder is considered to have owned immediately before the deemed redemption and (ii) the percentage of the outstanding stock of the REIT the stockholder owns immediately after the deemed redemption. The Internal Revenue Service has indicated in a published ruling that, in the case of a small minority holder of a publicly-held corporation who exercises no control over corporate affairs, a reduction in the holder's proportionate interest in the corporation from .0001118% to .0001081% would constitute a meaningful reduction.

In applying the foregoing tests, under the attribution rules of section 318 of the Code, a stockholder is deemed to own (i) stock owned and, in some cases, constructively owned by family members, by certain estates and trusts of which the stockholder is a beneficiary and by certain affiliated entities and (ii) stock subject to an option actually or constructively owned by the stockholder or such other persons. As the determination as to whether a former CapStar stockholder has recognized capital gain with respect to the receipt of the Rights is complex, each stockholder that believes that it might qualify for capital gain treatment under the above rules is urged to consult its tax advisor with respect to such determination.

To the extent that the gain recognized by a holder of CapStar common stock "has the effect of the distribution of a dividend", the amount that will be treated as ordinary dividend income will depend on the earnings and profits of CapStar at the effective time of the Merger. Earnings and profits immediately prior to the effective time of the Merger will be increased by an amount equal to the sum of the fair market value of the Rights and the excess of the fair market value of the Common Stock of MeriStar Hotels over CapStar's tax basis in such stock.

If the distribution of the Rights instead was treated as a distribution of property under Section 301 of the Code, an amount equal to the fair market value of the Rights on the date of distribution would be treated as a

302 of the Code, the deemed redemption is "substantially disproportionate" with respect to an AGH stockholder, the gain recognized will be treated as capital gain. One requirement that must be met in order for the deemed redemption to be "substantially disproportionate" is that the percentage of the outstanding voting stock of the REIT following the Merger and the deemed redemption considered owned by the stockholder is less than 80% of the percentage of the outstanding voting stock of the REIT considered owned by the stockholder following the Merger but immediately before the deemed redemption. Although the matter is not free from doubt, in determining whether this test is satisfied, the reduction in percentage interests of the AGH stockholder as a result of the issuance of additional shares of the REIT to former CapStar stockholders in the Merger should be taken into account. Based on calculations of the relative values of the REIT Common Stock, the Rights to be received by former holders of AGH common stock and the amount of stock issued to former CapStar stockholders in the Merger, it is anticipated that the deemed redemption will be "substantially disproportionate" with respect to holders of AGH Common Stock. Accordingly, the gain recognized by such shareholder will be taxed as a capital gain.

In applying the foregoing tests, under the attribution rules of section 318 of the Code, a stockholder is deemed to own (i) stock owned and, in some cases, constructively owned by family members, by certain estates and trusts of which the stockholder is a beneficiary and by certain affiliated entities and (ii) stock subject to an option actually or constructively owned by the stockholder or such other persons. As the determination as to whether a former AGH stockholder has recognized capital gain with respect to the receipt of the Rights is complex, each stockholder that believes that it might qualify for capital gain treatment under the above rules is urged to consult its tax advisor with respect to such determination.

If the distribution of the Rights instead was treated as a distribution of property under Section 301 of the Code, an amount equal to the fair market value of the Rights on the date of distribution would be treated as a dividend to the extent of the current and accumulated earnings and profits of AGH, including earnings and profits resulting from the distribution of the Rights. The earnings and profits of AGH immediately prior to the effective time of the Merger would be increased by an amount equal to the fair market value of the Rights. Any amount in excess of the earnings and profits of AGH would be treated first as a tax-free return of capital, reducing the stockholder's tax basis in its AGH common stock, and any amount in excess of tax basis would be taxable as gain from sale or exchange of such stockholder's shares of AGH common stock. Such gain would be capital gain if such stockholder's shares of AGH common stock were held as a capital asset at the time of the AGH recapitalization.

The tax basis of a former AGH stockholder in the Rights received in the distribution will be the fair market value of such Rights, and the holding period for such Rights will begin on the date of the distribution.

Whether the Rights Offering is treated as a distribution of boot in a reorganization or as a dividend, AGH will recognize gain on the distribution of the Rights in an amount equal to the fair market value of such Rights at the time of the distribution.

Exercise of Rights by Former Holders of AGH Common Stock

Former holders of AGH common stock will not recognize gain or loss upon the exercise of the Rights. Such holders who receive shares of MeriStar Hotels Common Stock upon such exercise will take a tax basis in those shares equal to the sum of the price paid on exercise and the Rightholder's tax basis in the Rights.

Lapse of Rights by Former Holders of AGH Common Stock

Former holders of AGH common stock who fail to exercise their Rights prior to the Expiration Date will be deemed to have sold their Rights on that date for an amount equal to zero. Assuming the Rights are held as capital assets, such holders will recognize a short-term capital loss equal to their adjusted tax basis in the Rights upon failure to exercise such Rights.

MANAGEMENT

MeriStar Hotels was recently formed. The Company has entered into employment agreements with certain executive officers and will pay a salary and/or other compensation to such executive officers for their services in such capacities as set forth below under "Executive Compensation." Options have been, and in the future may be, granted to executive officers. See "Stock Option Grants."

The Board of Directors

The Board of Directors is divided into three classes of directors. The initial term of the first, second and third classes expires in 2001, 2002 and 2003, respectively. Directors of each class will be elected for three-year terms upon the expiration of the initial class terms, and, beginning in 2001 and each year thereafter, each class of directors will be elected by the stockholders. As of the Spin-off and the effective date of the Merger, the following individuals became directors of MeriStar Hotels:

<u>Name, Principal Occupation and Business Experience</u>	<u>Will Serve as a Director of MeriStar Hotels beginning</u>	<u>Age</u>	<u>Class</u>
Daniel L. Doctoroff Daniel L. Doctoroff has been a Director of CapStar since 1996, a Managing Director of Oak Hill Partners, Inc., the investment advisor to several private investment funds (including Acadia Partners, L.P.), and its predecessor since August 1987; Vice President and Director of Acadia Partners MGP, Inc. since March 1992; Vice President of Keystone, Inc. since March 1992; and a Managing Partner of Insurance Partners Advisors, L.P. since February 1994. All of such entities are affiliates of Acadia Partners. Mr. Doctoroff is also a Director of Bell & Howell Holdings Company, Kemper Corporation and Specialty Foods Corporation.	1998	39	I
Kent R. Hance Kent R. Hance has been a director of AGH since July 1996. Since 1994, Mr. Hance has been a law partner in the firm Hance, Scarborough, Woodward & Weisbart, L.L.P., Austin, Texas, and from 1991 to 1994, he was a law partner in the firm of Hance and Gamble. From 1985 to 1987, he was a law partner with Boyd, Viegall and Hance. Mr. Hance also served as a member of the Texas Railroad Commission from 1987 until 1991 and as its Chairman from 1989 until 1990. From 1979 to 1985, he served as a member of the United States Congress. In addition, Mr. Hance served as a State Senator in the State of Texas from 1975 to 1979 and was a professor of business law at Texas Tech University from 1969 to 1973.	1998	55	II
Steven D. Jorns Steven D. Jorns has been the Chairman of the Board of Directors, Chief Executive Officer and President of AGH since April 1996. Mr. Jorns is the founder of, and has served since its formation in 1981 as Chairman of the Board of Directors, Chief Executive Officer and President of, AGHI, a hotel management company. Prior to forming AGHI, Mr. Jorns spent seven years with an affiliate of General Growth Companies overseeing that company's hotel portfolio. Prior to that, Mr. Jorns was associated with Hospitality Motor Inns, a division of Standard Oil of Ohio, and held marketing positions with Holiday Inns, Inc.	1998	49	I

Board Committees

The Board of Directors of MeriStar Hotels will have four committees: an Audit Committee, a Compensation Committee, an Investment Committee and a Leasing Committee.

The Audit Committee will consist of three directors who are not employees of the Company ("Independent Directors"). The Audit Committee will be responsible for making recommendations concerning the engagement of independent auditors, reviewing with the independent auditors the plans and results of the audit engagement, approving professional services provided by the independent auditors, reviewing the independence of the independent auditors, considering the range of audit and non-audit fees and reviewing the adequacy of the Company's internal accounting controls.

The Compensation Committee will consist of four Independent Directors. The Compensation Committee will be responsible for the determination of compensation of the Company's executive officers and the administration of the Company's employee incentive plans.

The Investment Committee of the Company will consist of the Chairman of the Board and directors from each of MeriStar Hotels and the REIT. The Company's Investment Committee will be responsible for the review and approval of investments proposed by the Company.

The Leasing Committee will consist of the Chairman of the Board and three Independent Directors. The Leasing Committee will be responsible for the review and approval of leases to be entered into between the Hotel Parties and the REIT Parties.

The entire Board of Directors of the Company will act as the nominating committee for directors of the Company and will consider nominations by stockholders for directors. The Board of Directors would be pleased to receive suggestions from stockholders about persons it should consider as possible members of the Board of Directors. Any such suggestion should be mailed to the Secretary of the Company by December 31, 1998.

Directors Compensation

Independent Directors of the Company will be paid an annual fee of \$20,000. In addition, each Independent Director will be paid \$1,250 for attendance at each meeting of the Board; \$1,000 for attendance at each meeting of a committee of the Board of Directors of which such director is a member and \$500 for each telephonic meeting of the Board of Directors or a committee thereof of which such director is a member. Directors who are employees of the Company will not receive any fees for their service on the Board of Directors or a committee thereof. The Company will reimburse directors for their out-of-pocket expenses in connection with their service on the Board of Directors.

Options

Pursuant to the MeriStar Hotels & Resorts, Inc. Non-Employee Directors' Incentive Plan (the "MeriStar Hotels Directors' Plan"), each director, who is not an officer or employee of MeriStar or its subsidiaries (each an "Independent Director"), will be awarded an option to purchase 7,500 shares of Common Stock upon initial commencement of service after the Spin-Off, whether by appointment or election. Thereafter, each Independent Director will be granted an option to purchase 5,000 shares of Common Stock on the first business day following the Company's annual meeting of stockholders. The number of shares authorized for issuance under the MeriStar Hotels Directors' Plan is 125,000. The exercise price of option grants will be 100% of the fair market value of the Common Stock on the date of grant, and options will vest in three annual installments. The exercise price may be paid in cash, cash equivalents acceptable to the Compensation Committee, Common Stock or a combination thereof. Options granted under the MeriStar Hotels Directors' Plan, once vested, are exercisable for ten years from the date of grant. Upon termination of service as a director, options which have not vested are forfeited and vested options may be exercised until they expire. All options accelerate upon a change in control of MeriStar Hotels.

Certain Federal Income Tax Consequences Relating to Options

Generally, an eligible director does not recognize any taxable income, and the Company is not entitled to a deduction upon the grant of an option. Upon the exercise of an option, the eligible director recognizes ordinary

Executive Officers

The following table sets forth the name, age, title and business experience for each person who serves as an executive officer of MeriStar Hotels. For information concerning the business experience of Messrs. Whetsell, Jorns and McCaslin, who are also members of the MeriStar Hotels Board of Directors, see "Management—The Board of Directors."

<u>Name</u>	<u>Age</u>	<u>Position</u>
Paul W. Whetsell	47	Chairman of the Board and Chief Executive Officer
Steven D. Jorns	49	Vice Chairman and Chief Operating Officer
David E. McCaslin	41	President and Director
James A. Calder	35	Chief Financial Officer
John E. Plunket	42	Executive Vice President, Finance and Development

James A. Calder

James A. Calder has served as Senior Vice President of Finance of CapStar since September 1997. From May 1995 to September 1997, he served as Senior Vice President and Corporate Controller of ICF Kaiser International, Inc. Prior to that, from July 1984 to May 1995, he worked for Deloitte & Touche LLP in various capacities, culminating with Audit Senior Manager for the real estate industry. He is a Certified Public Accountant.

John E. Plunket

John E. Plunket has served as Executive Vice President, Finance and Development of CapStar since November 1993. From September 1991 to October 1993, Mr. Plunket served as Vice President and Principal Broker for CIG International, an investment and hotel asset management company. From February 1988 to August 1991, Mr. Plunket served as Managing Director of Cassidy & Pinkard Inc., a commercial real estate services company. From 1985 to 1987, Mr. Plunket served as Senior Vice President for Oxford Development Corporation. Prior to that, from December 1979 to April 1985, Mr. Plunket worked for Marriott Corporation in various capacities, culminating in Director of Project Finance.

Executive Compensation

The following table sets forth the compensation that is expected to be paid by the Company during 1998 with respect to the Chief Executive Officer and the four most highly compensated executive officers (the "Named Executive Officers").

<u>Name and Principal Position</u>	<u>Annual Compensation</u>			<u>Other Annual Compensation</u>	<u>Options to be Granted</u>
	<u>Year</u>	<u>Salary</u>	<u>Bonus</u>		<u>Long-Term Compensation</u>
Paul W. Whetsell	1998	\$190,000	\$ —	\$ —	—
Chief Executive Officer and Chairman of the Board					
Steven D. Jorns	1998	190,000	—	—	250,000
Vice Chairman and Chief Operating Officer					
David E. McCaslin	1998	300,000	—	—	87,500
President and Director					
James A. Calder	1998	200,000	—	—	47,500(1)
Chief Financial Officer					
John E. Plunket	1998	162,000	—	—	10,000(2)
Executive Vice President, Finance and Development					

- (1) Does not include 47,500 options to purchase REIT Common Stock to be granted by the REIT in consideration for services to be rendered by Mr. Calder to the REIT.
- (2) Does not include 12,500 options to purchase REIT Common Stock to be granted by the REIT in consideration for services to be rendered by Mr. Plunket to the REIT.

Termination Due to Death or Disability. Upon termination due to death or disability, the executive or his estate will receive a lump sum payment equal to the executive's base salary, plus the pro rata portion of his bonus for the fiscal year in question, in addition to payment for one year of any other compensation due the executive pursuant to his employment contract. Any unvested portion of such executive's stock options and restricted stock will vest immediately and become exercisable for one year thereafter, and shares of restricted stock previously granted shall become free from all contractual restrictions.

Voluntary Termination or Termination for Cause. Upon voluntary termination or termination for "cause" by the Company, the executive will receive any accrued and unpaid base salary through the termination date. Any unvested options will terminate immediately, and any vested options held by the executive will expire ninety (90) days after the termination date.

Termination Following a Change in Control. If Mr. Whetsell or Mr. Jorns is terminated without cause or voluntarily terminates with "good reason" within 24 months following a "Change in Control," the executive will receive the following benefits: (i) a lump sum payment equal to the product of (x) the sum of (A) his then annual base salary and (B) the amount of his bonus for the preceding year or if the term of the employment agreement is terminated in its initial year his target bonus for such year multiplied by (y) the greater of (A) three (3) and (B) a fraction the numerator of which is the number of days remaining in the Term of the employment agreement, without further extension and the denominator of which is 365; (ii) all unvested stock options held by the executive will immediately vest and be exercisable for the period of one (1) year thereafter and shares of restricted stock previously granted to the executive will become free from all contractual restrictions; and (iii) the continuance of certain benefit under the employment agreement, including, but not limited to, life and health insurance plans, or their equivalent for a period equal to the greater of two years or the remaining term of the employment agreement, without further extension. In the case of the other executives, they would each be entitled to the same type of benefits provided the termination occurred within 18 months of the Change in Control, except their lump sum payment will only be two (2) times the sum of their then annual base salary plus bonus and the total payments would be limited to the amount which is deductible under Section 280G of the Code; but only if, by reason of such limitation, the net after tax benefit of executive shall exceed the net after tax benefit if such limitation were not made.

Change in Control Payments. In the case of Messrs. Whetsell and Jorns, in the event that any accelerated vesting of the executive's rights with respect to stock options, restricted stock or any other payment, benefit or compensation results in the imposition of an excise tax payable by the executive under Section 4999 of the Code, or any successor or other provision with respect to "excess parachute payments" within the meaning of Section 280G(b) of the Internal Revenue Code, the Company will make a cash payment to the executive in the amount of such excise tax (the "Excise Tax Payment") and shall also make a cash payment to the executive in an amount equal to the total of federal, state and local income and excise taxes for which the executive may be liable on account of such Excise Tax Payment.

Termination within 24 Months of Effective Time

Notwithstanding anything to the contrary, if the employment of Messrs. Whetsell or Jorns is terminated for any reason within 24 months after the consummation of the Formation Transactions, any pre-Formation Transaction stock options or other awards will immediately vest and remain exercisable in accordance with their respective terms (with a minimum of one year from the date of termination). If the employment of Messrs. Whetsell and Jorns is terminated other than for cause within 24 months after the consummation of the Formation Transactions, all post-Formation Transactions stock options or other awards made to Messrs. Whetsell and Jorns will continue to vest and remain exercisable following any such termination of employment as if such executive's employment had not terminated.

The MeriStar Hotels Incentive Plan

The Board of Directors adopted the MeriStar Hotels & Resorts, Inc. Incentive Plan (the "MeriStar Hotels Incentive Plan") for the purposes of (i) attracting and retaining employees, directors and other service providers with ability and initiative, (ii) providing incentives to those deemed important to the success of the Company and related entities, and (iii) associating the interests of these individuals with the interests of the Company and its stockholders through opportunities for increased stock ownership.

Incentive Awards

Incentive awards also may be granted under the MeriStar Hotels Incentive Plan. An incentive award is an opportunity to earn a bonus, payable in cash, upon attainment of stated performance objectives. The objectives may be stated with reference to the fair market value of the Common Stock or on the Company's, a subsidiary's, or an operating unit's return on equity, earnings per share, total earnings, earnings growth, return on capital, funds from operations or return on assets or other acceptable performance criteria. The period in which performance will be measured will be at least one year. No Participant may receive an incentive award payment in any calendar year that exceeds the lesser of (i) 100% of the Participant's base salary (prior to any salary reduction or deferral election) as of the date of grant of the incentive award or (ii) \$250,000.

Performance Share Awards

The MeriStar Hotels Incentive Plan also provides for the award of performance shares. A performance share award entitles the Participant to receive a payment equal to the fair market value of a specified number of shares of Common Stock if certain standards are met. The Administrator will prescribe the requirements that must be satisfied before a performance share award is earned. These conditions may include, for example, a requirement that the Participant continue employment with the Company for a specified period or that the Company or the Participant achieve stated, performance-related objectives. The objectives may be stated with reference to the fair market value of the Common Stock or on the Company's, a subsidiary's, or an operating unit's return on equity, earnings per share, total earnings, earnings growth, return on capital, funds from operations or return on assets or other acceptable performance criteria. To the extent that performance shares are earned, the obligation may be settled in cash, in Common Stock, or by a combination of the two. No Participant may be granted performance shares for more than 12,500 shares of Common Stock in any calendar year.

Transferability

Awards granted under the MeriStar Hotels Incentive Plan are generally nontransferable. The Compensation Committee may, however, grant awards other than ISOs, which are transferable to Permitted Family Members.

Share Authorization

At any given time, the maximum number of shares of Common Stock that may be issued pursuant to awards granted under the MeriStar Hotels Incentive Plan will be the total of (i) twelve (12%) percent of the number of shares of Common Stock that were outstanding as of the end of the immediately preceding calendar year (rounded downward if necessary to eliminate fractional shares), minus (ii) the number of shares subject to awards which were granted under the MeriStar Hotels Incentive Plan through the last day of the immediately preceding calendar year, plus (iii) as of the last day of the immediately preceding calendar year, the number of shares with respect to which previously granted awards have expired. For calendar year 1998, the maximum number of shares of Common Stock that may be issued pursuant to the MeriStar Hotels Incentive Plan will be twelve (12%) percent of the number of shares of Common Stock outstanding after the Spin-Off. In addition to the foregoing, in no event may the total number of shares of Common Stock covered by outstanding ISOs granted under the MeriStar Hotels Incentive Plan, plus the number of shares of Common Stock issued pursuant to the exercise of ISOs, whenever granted under the MeriStar Hotels Incentive Plan, exceed approximately 1.4 million shares. All awards made under the MeriStar Hotels Incentive Plan will be evidenced by written agreements between the Company and the Participant. The share limitation and the terms of outstanding awards will be adjusted, as the Compensation Committee deems appropriate, in the event of a stock dividend, stock split, combination, reclassification, recapitalization or other similar event.

Termination and Amendment

No option or stock award may be granted and no performance shares may be awarded under the MeriStar Hotels Incentive Plan more than ten years after the earlier of the date that the MeriStar Hotels Incentive Plan is adopted by the Board of Directors or the date that it is approved by the Company's stockholders. The Board of

does not apply to certain performance-based compensation paid under a plan that meets the requirements of the Code and regulations promulgated thereunder. While the MeriStar Hotels Incentive Plan generally complies with the requirements for performance-based compensation, options granted at less than 100% of fair market value and stock awards granted under the MeriStar Hotels Incentive Plan will not satisfy those requirements.

Stock Options

The following table sets forth for certain executive officers of the Company information regarding the grant of Stock Options as parity awards. See "Management" for information concerning the business experience of the proposed executive officers of the Company.

<u>Name and Position</u>	<u>Number of Stock Options to be Granted(1)</u>
Steven D. Jorns Vice Chairman, Chief Operating Officer	250,000
David E. McCaslin President	87,500
James A. Calder Chief Financial Officer	47,500
John E. Plunket Executive Vice President, Finance and Development	10,000

(1) The awards described herein are parity awards, such that after the Spin-Off similarly situated executives will have the same number of options to purchase Common Stock. Similar parity awards will be made by the REIT. The options will vest in three annual installments beginning on the first anniversary of the consummation of the Formation Transactions.

Except as set forth above, awards granted under the MeriStar Hotels Incentive Plan are discretionary and are therefore not determinable at this time.

DESCRIPTION OF CAPITAL STOCK

The following summary information is qualified in its entirety by the provisions of the Charter and By-laws, copies of which have been filed as exhibits to the Registration Statement of which this Prospectus is a part. See "Available Information."

The authorized capital stock of MeriStar Hotels consists of 100,000,000 shares of Common Stock, par value \$0.01 per share, and 10,000,000 shares of preferred stock ("Preferred Stock"), of which approximately 25,000,000 shares of Common Stock and no shares of Preferred Stock are outstanding. Upon completion of the Rights Offering, a maximum of 34,000,000 shares of Common Stock and no shares of Preferred Stock will be outstanding.

Prior to the Spin-Off, there was no public market for the Common Stock.

Common Stock

Voting Rights. Except as set forth below under "Certain Antitakeover Provisions," the Charter provides that holders of Common Stock are entitled to one vote per share on all matters submitted to a vote of stockholders.

Dividends. Each share of Common Stock is entitled to receive dividends if, as and when declared by the Board. Under Delaware law, a corporation may declare and pay dividends out of surplus, or if there is no surplus, out of net profits for the fiscal year in which the dividend is declared and/or the preceding year. No dividends may be declared out of net profits, however, if the capital of the corporation has been diminished by depreciation in the value of its property, losses or otherwise to an amount less than the aggregate amount of capital represented by any issued and outstanding stock having a preference on the distribution of assets. See "Dividend Policy."

Other Rights. Stockholders of MeriStar Hotels have no preemptive or other rights to subscribe for additional shares. Subject to any rights of the holders of any Preferred Stock, all holders of Common Stock are entitled to share equally on a share-for-share basis in any assets available for distribution to stockholders on liquidation, dissolution or winding up of MeriStar Hotels. No shares of Common Stock are subject to redemption or a sinking fund. All outstanding shares of Common Stock are, and the Common Stock to be outstanding upon completion of the Rights Offering will be, fully paid and nonassessable.

Preferred Stock

The Board of Directors is authorized to issue, without further authorization from stockholders, up to 10,000,000 shares of Preferred Stock in one or more series and to determine, at the time of creating each series, the distinctive designation of, and the number of shares in, the series, its dividend rate, the number of votes, if any, for each share of such series, the price and terms on which such shares may be redeemed, the terms of any applicable sinking fund, the amount payable upon liquidation, dissolution or winding up, the conversion rights, if any, and such other rights, preferences and priorities of such series as the Board of Directors may be permitted to fix under the laws of the State of Delaware as in effect at the time such series is created. The issuance of Preferred Stock could adversely affect the voting power of the holders of Common Stock and could have the effect of delaying, deferring or preventing a change in control of MeriStar Hotels.

Series A Junior Preferred Stock

The Company reserved 500,000 shares of Series A Junior Preferred Stock for issuance upon exercise of Preferred Rights. The Series A Junior Preferred Stock will not be redeemable and will rank, with respect to the payment of dividends and the distribution of assets, junior to any other series of any other classes of Preferred Stock that may exist from time to time. Generally, each share of Series A Junior Preferred Stock will entitle its holder to 100 votes on all matters submitted to a vote of the Company's stockholders.

CERTAIN ANTITAKEOVER PROVISIONS

The Charter and By-Laws

The Charter and By-laws and applicable sections of the DGCL contain several provisions that may make the acquisition of control of the Company more difficult without the prior approval of the Board of Directors. Certain provisions of the Charter and the By-laws, among other things: (i) classify the Board of Directors into three classes, each of which serves for staggered three-year terms; (ii) provide that a director of Company may be removed by the stockholders only for cause; (iii) provide that the stockholders may amend or repeal any of the foregoing provisions of the Charter only by a vote of 66 $\frac{2}{3}$ % of the stock entitled to vote generally in the election of directors; (iv) provide that only the Chairman of the Board, Vice Chairman, President or the Board of Directors may call special meetings of the stockholders; (v) provide that the stockholders may take action only at a meeting of Company stockholders, not by written consent; (vi) provide that stockholders must comply with certain advance notice procedures in order to nominate candidates for election to the Board of Directors or to place stockholders' proposals on the agenda for consideration at meetings of the stockholders and (vii) provide that the chair of any meeting of stockholders shall have the power to adjourn such meeting. In general, Section 203 of the DGCL prohibits publicly held Delaware corporations from engaging in a "business combination" with an "interested stockholder" for a period of three years following the time of the transaction in which the person or entity became an interested stockholder, unless (i) prior to such time, either the business combination or the transaction which resulted in the stockholder's becoming an interested stockholder is approved by the Board of Directors, (ii) upon consummation of the transaction which resulted in the stockholder's becoming an interested stockholder, the interested stockholder owned at least 85% of the outstanding voting stock of the corporation (excluding for this purpose certain shares owned by persons who are directors and also officers of the corporation and by certain employee benefit plans) or (iii) on or after such date the business combination is approved by the Board of Directors and by the affirmative vote (and not by written consent) of at least 66 $\frac{2}{3}$ % of the outstanding voting stock which is not owned by the interested stockholder. For the purposes of Section 203, a "business combination" is broadly defined to include mergers, asset sales and other transactions resulting in a financial benefit to the interested stockholder. An "interested stockholder" is a person who, together with affiliates and associates, owns (or, in certain cases, within the immediately preceding three years did own) 15% or more of the corporation's voting stock. The Charter authorizes the Board of Directors to issue up to 10 million shares of Preferred Stock in series, and to establish the rights and preferences (including the convertibility of such shares of Preferred Stock into shares of Common Stock) of any series of Preferred Stock so issued. The issuance of Preferred Stock could have the effect of delaying or preventing a change in control of Company, even if such a change in control were in the best interests of some, or a majority, of Company's stockholders. See "Description of Capital Stock".

The Rights Plan

The Board of Directors adopted the Rights Plan prior to the date of the Spin-Off. Pursuant to the Rights Plan, the Board of Directors will cause to be issued one right (a "Preferred Right") for each share of Common Stock outstanding on August 1, 1998 (the "Distribution Date"). Each Preferred Right will entitle the registered holder to purchase from MeriStar Hotels one-hundredth of a share of Series A Junior Preferred Stock, par value \$.01 per share, of MeriStar Hotels at a price of \$35 (the "Purchase Price"), subject to adjustment. The description and terms of the Preferred Rights are set forth in a Rights Agreement (the "Rights Agreement"), between MeriStar Hotels and the designated Rights Agent (the "Rights Agent"). The description set forth below is intended as a summary only and is qualified in its entirety by reference to the form of the Rights Agreement filed as an exhibit to the Registration Statement. See "Available Information."

Until the earlier to occur of (i) 10 days following a public announcement that a person or group of affiliated or associated persons (an "Acquiring Person") has acquired beneficial ownership of 20% or more of the outstanding shares of Common Stock or (ii) 10 business days (or such later date as may be determined by action of the Board of Directors prior to such time as any person becomes an Acquiring Person) following the commencement of, or announcement of an intention to make, a tender offer or exchange offer the consummation

The number of outstanding Preferred Rights and the number of one-hundredths of a share of Series A Junior Preferred Stock issuable upon exercise of each Preferred Right also will be subject to adjustment in the event of a split of the Common Stock, or a stock dividend on the Common Stock payable in Common Stock or subdivisions, consolidations or combinations of the Common Stock occurring, in any such case, prior to the Rights Distribution Effective Date.

The Purchase Price payable, and the number of shares of Series A Junior Preferred Stock or other securities or property issuable, upon exercise of the Preferred Right also will be subject to adjustment from time to time to prevent dilution (i) in the event of a stock dividend on, or a subdivision, combination or reclassification of, the shares of Series A Junior Preferred Stock, (ii) upon the grant to holders of shares of Series A Junior Preferred Stock of certain rights or warrants to subscribe for or purchase shares of Series A Junior Preferred Stock at a price, or securities convertible into shares of Series A Junior Preferred Stock or (iii) upon the distribution to holders of shares of Series A Junior Preferred Stock of evidences of indebtedness or assets (excluding regular periodic cash dividends paid out of earnings or retained earnings or dividends payable in shares of Series A Junior Preferred Stock) or of subscription rights or warrants (other than those referred to above).

With certain exceptions, no adjustment in the Purchase Price will be required until cumulative adjustments require an adjustment of at least one percent in such Purchase Price. No fractional shares of Series A Junior Preferred Stock will be issued (other than fractions which are integral multiples of one-hundredth of a share of Series A Junior Preferred Stock, which may, at the election of the Company, be evidenced by depository receipts) and in lieu thereof, an adjustment in cash will be made based on the market price of shares of Series A Junior Preferred Stock on the last trading day prior to the date of exercise.

Shares of Series A Junior Preferred Stock purchasable upon exercise of the Preferred Rights will not be redeemable. Each share of Series A Junior Preferred Stock will be entitled to a minimum preferential quarterly dividend payment of \$1 per share but will be entitled to an aggregate dividend of 100 times the dividend declared per share of Common Stock. In the event of liquidation, the holders of shares of Series A Junior Preferred Stock will be entitled to a minimum preferential liquidation payment of \$100 per share but will be entitled to an aggregate payment of 100 times the payment made per share of Common Stock. Each share of Series A Junior Preferred Stock will have 100 votes voting together with the Common Stock. Finally, in the event of any merger, consolidation or other transaction in which shares of Common Stock are exchanged, each share of Series A Junior Preferred Stock will be entitled to receive 100 times the amount received per share of Common Stock. These rights are protected by customary anti-dilution provisions.

Due to the nature of the shares of Series A Junior Preferred Stock's dividend, liquidation and voting rights, the value of the one-hundredth interest in a share of Series A Junior Preferred Stock purchasable upon exercise of each Preferred Right should approximate the value of one share of Common Stock.

The Preferred Rights have certain antitakeover effects. The Rights will cause substantial dilution to a person or group of persons that attempts to acquire MeriStar Hotels on terms not approved by the Board of Directors. The Preferred Rights would not interfere with any merger or other business combination approved by the Board of Directors prior to the time that a person or group has acquired beneficial ownership of 20% or more of the Common Stock since the Rights may be redeemed by MeriStar Hotels at the Redemption Price until the tenth day after such time.

The Rights Plan contains certain provisions to exclude the REIT and its affiliates from the operative provisions thereof.

Restrictions on Ownership

The Charter also provides, with certain exceptions, that persons who own or are treated as owning more than 9.8% of the value of the REIT stock may not own, either directly or under the attribution rules set forth in Section 318(a) of the Code, as modified by Section 856(d)(5) of the Code, more than 9.9% of either the voting stock or the total number of outstanding shares of the Company's stock (the "Ownership Limit").

The Dealer Manager

The Company has engaged Lehman Brothers Inc. ("Lehman Brothers") to act as dealer manager in connection with the Rights Offering. In this capacity, Lehman Brothers has agreed to assist in soliciting the Company's shareholders to exercise their Rights. Lehman Brothers has not agreed to any standby or other arrangements to purchase any Rights or any Common Stock underlying the Rights. In addition, Lehman Brothers does not intend to engage in any stabilization activities with respect to any of the Company's securities and Lehman Brothers will not engage in market making activities in the Company's securities subsequent to the date hereof and prior to the Expiration Date.

The Company has agreed to pay the Dealer Manager, in the event the Rights Offering is commenced, a fee equal to the greater of (a) 1% of the aggregate Subscription Price for all Shares sold in the Rights Offering, or (b) \$50,000, regardless of whether the Rights Offering is subsequently withdrawn, terminated or rescinded. The Company has also agreed to reimburse Lehman Brothers for all of its expenses, regardless of whether the Rights Offering is commenced or is subsequently withdrawn, terminated or rescinded, and has agreed to indemnify Lehman Brothers against certain liabilities under the Securities Act. Such fee is not dependent on the exercise of the Rights. Lehman Brothers has provided investment banking services for customary compensation to the Company and its affiliates from time to time in the past and may be engaged to do so in the future.

Other than Lehman Brothers, the Company has not engaged any dealer managers, financial advisors, brokers or dealers in connection with the Rights Offering or solicitation of exercises of the Rights.

EXPERTS

The balance sheet of MeriStar Hotels & Resorts, Inc. as of March 31, 1998 and the combined financial statements of the management and leasing business of CapStar Hotel Company and subsidiaries ("OpCo") as of December 31, 1997 and 1996 and for each of the years in the three-year period ended December 31, 1997, included in this Prospectus, have been included herein in reliance on the report of KPMG Peat Marwick LLP, independent certified public accountants, appearing elsewhere herein, and upon the authority of said firm as experts in accounting and auditing.

The financial statements of AGH Leasing, L.P. as of December 31, 1997 and 1996 and for the year ended December 31, 1997 and for the period from July 31, 1996 through December 31, 1996, the financial statements of American General Hospitality, Inc. as of December 31, 1997 and 1996, and for each of the three years in the period ended December 31, 1997, and the balance sheets of Winston Hospitality, Inc. as of October 31, 1997 and December 31, 1996 and the statements of income, shareholders' equity, and cash flows for the ten months ended October 31, 1997 and each of the two years in the period ended December 31, 1996, included in this registration statement have been audited by PricewaterhouseCoopers LLP, independent accounts, as set forth in their reports thereon. Each of the above referenced financial statements have been included by reference herein in reliance upon the authority of said firm as expert in accounting and auditing.

LEGAL MATTERS

Paul, Weiss, Rifkind, Wharton & Garrison will pass on the validity of the Rights and the Common Stock to be issued in connection with the Rights Offering and certain federal income tax consequences of the Rights Offering.

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MeriStar Hotels & Resorts, Inc.

Balance Sheet
March 31, 1998

Assets

Cash \$100

Stockholder's equity

Common stock \$.01 par value:

1,000 shares authorized; 100 issued and outstanding 1

Additional paid-in-capital 99

Total stockholder's equity \$100

See accompanying notes to balance sheet

INDEPENDENT AUDITORS' REPORT

The Board of Directors
CapStar Hotel Company:

We have audited the accompanying combined balance sheets of the management and leasing business of CapStar Hotel Company and subsidiaries ("OpCo") as of December 31, 1997 and 1996 and the related combined statements of operations, owners' equity and cash flows for each of the years in the three-year period ended December 31, 1997. These combined financial statements are the responsibility of OpCo's management. Our responsibility is to express an opinion on these combined financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of OpCo as of December 31, 1997 and 1996, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 1997, in conformity with generally accepted accounting principles.

/s/ KPMG PEAT MARWICK LLP

Washington, D.C.
March 30, 1998

OPCO
COMBINED STATEMENTS OF OPERATIONS

(In Thousands)

	Three Months Ended March 31,		Years Ended December 31,		
	1998	1997	1997	1996	1995
	(unaudited)				
Revenue:					
Leased hotels' operations:					
Rooms	\$23,404	\$ —	\$ 9,880	\$ —	\$ —
Food and beverage	1,357	—	1,397	—	—
Other operating departments	1,219	—	474	—	—
Hotel management and other revenue	4,150	1,139	12,088	7,050	5,354
Total revenue	<u>30,130</u>	<u>1,139</u>	<u>23,839</u>	<u>7,050</u>	<u>5,354</u>
Leased hotels' operating expenses by department:					
Rooms	5,124	—	2,533	—	—
Food and beverage	995	—	909	—	—
Other operating departments	498	—	261	—	—
Undistributed operating expenses:					
Administrative and general	6,963	2,202	10,473	6,140	4,745
Lease expense	10,655	—	4,135	—	—
Property operating costs	4,142	—	1,917	—	—
Depreciation and amortization	421	96	636	349	84
Total operating expenses	<u>28,798</u>	<u>2,298</u>	<u>20,864</u>	<u>6,489</u>	<u>4,829</u>
Net operating income	1,332	(1,159)	2,975	561	525
Equity in earnings (losses) of affiliates	(521)	—	46	—	—
Interest expense	18	14	56	123	44
Income before minority interests	793	(1,173)	2,965	438	481
Minority interests	35	—	103	—	—
Net income (loss)	<u>\$ 758</u>	<u>\$(1,173)</u>	<u>\$ 2,862</u>	<u>\$ 438</u>	<u>\$ 481</u>

See accompanying notes to combined financial statements.

OPCO
COMBINED STATEMENTS OF CASH FLOWS

(In Thousands)

	Three Months Ended March 31.		Years Ended December 31.		
	1998	1997	1997	1996	1995
	(unaudited)				
Operating activities:					
Net income (loss)	\$ 758	\$(1,173)	\$2,862	\$ 438	\$ 481
Adjustments to reconcile net income (loss) to net cash provided by operating activities:					
Depreciation and amortization	421	96	636	349	84
Equity in earnings of affiliates	521	—	(46)	—	—
Minority interests	35	—	103	—	—
Changes in operating assets and liabilities:					
Accounts receivable, net	493	40	(5,459)	(412)	(1,290)
Prepaid expenses	124	(257)	(320)	(724)	(11)
Deposits, Inventory and other	47	(211)	(645)	(111)	—
Cash and cash equivalents held on behalf of affiliates	649	(120)	(6,702)	(17,843)	—
Accounts payable	(182)	367	1,539	276	267
Due to affiliates, net	(3,915)	484	3,638	18,344	305
Accrued expenses and other liabilities	2,534	1,456	7,250	909	372
Percentage lease payable	1,228	—	1,463	—	—
Advance deposits	47	—	146	—	—
Net cash provided by operating activities	<u>2,760</u>	<u>682</u>	<u>4,465</u>	<u>1,226</u>	<u>208</u>
Investing activities:					
Purchases of fixed assets	(697)	(234)	(2,046)	(382)	(61)
Purchases of intangible assets	(119)	(355)	(924)	(824)	—
Investments in affiliates	—	—	(2,078)	(150)	—
Distributions from investments in affiliates	490	37	147	30	—
Additions to notes receivable	—	(350)	(1,600)	(500)	—
Net cash used in investing activities	<u>(326)</u>	<u>(902)</u>	<u>(6,501)</u>	<u>(1,826)</u>	<u>(61)</u>
Financing activities:					
(Principal payments on) proceeds from long-term debt, net	(205)	(85)	96	662	(38)
Capital contributions	—	—	4,112	—	250
Capital distributions	—	—	—	—	(116)
Loan from (repayments to) affiliate	—	—	—	(950)	950
Repayments from (loans to) management	—	—	—	987	(987)
Net cash provided (used) by financing activities	<u>(205)</u>	<u>(85)</u>	<u>4,208</u>	<u>699</u>	<u>59</u>
Net increase (decrease) in cash and cash equivalents	2,229	(305)	2,172	99	206
Cash and cash equivalents, beginning of period	2,477	305	305	206	—
Cash and cash equivalents, end of period	<u>\$4,706</u>	<u>\$ —</u>	<u>\$2,477</u>	<u>\$ 305</u>	<u>\$ 206</u>

See accompanying notes to combined financial statements.

OPCO

NOTES TO COMBINED FINANCIAL STATEMENTS—(Continued)

December 31, 1997, 1996 and 1995

(Dollars in Thousands)

Cash and Cash Equivalents—OpCo considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

OpCo invests excess cash balances on behalf of the CapStar-owned hotels it manages. This cash is recorded as cash and cash equivalents held on behalf of affiliates with the offsetting liability recorded in due to affiliates, net.

Fixed Assets—Fixed assets are recorded at cost and are depreciated using the straight-line method over lives ranging from five to seven years.

Intangible Assets—Intangible assets consist of the value of goodwill and lease contracts purchased, organization and franchise costs, and costs incurred to obtain management contracts. Goodwill represents the excess of cost over the fair value of the net assets of the acquired businesses. Intangible assets are amortized on a straight-line basis over the estimated useful lives of the underlying assets ranging from five to 40 years.

The carrying values of long-lived intangible assets, which include fixed assets and all intangible assets, are evaluated periodically in relation to the operating performance and expected future undiscounted cash flows of the underlying assets. Adjustments are made if the sum of expected future undiscounted net cash flows is less than book value. The impairment loss to be recognized is measured by the amount by which the carrying amount of the assets exceed the fair value of the assets. No impairment losses were recorded during 1997, 1996 or 1995.

Income Taxes—No provision is made for income taxes as the operations of OpCo are directly owned by a partnership and four limited liability companies, and therefore, any such liability is the liability of the partners and members.

Revenue Recognition—Revenue is earned through the operation and management of the hotel properties and is recognized when earned.

Minority Interests—Minority interests represent OpCo's proportionate share of the value of operating partnership units ("OP Units") of CMC and CMC II issued to third parties in conjunction with CapStar's purchases of certain hotels and CapStar Winston.

Use of Estimates—The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Unaudited interim financial statements—The combined financial statements as of March 31, 1998 and for the three months ended March 31, 1998 and 1997 are unaudited. In the opinion of management, such financial statements reflect all adjustments necessary for a fair presentation of the results of the respective interim periods. All such adjustments are of a normal, recurring nature.

OPCO

NOTES TO COMBINED FINANCIAL STATEMENTS—(Continued)

December 31, 1997, 1996 and 1995

(Dollars in Thousands)

5. INTANGIBLE ASSETS

Intangible assets consist of the following:

	<u>December 31,</u>	
	<u>1997</u>	<u>1996</u>
Goodwill	\$27,605	\$ —
Lease contracts	6,576	—
Organization costs	897	897
Management contracts	867	150
Other	715	—
	<u>36,660</u>	<u>1,047</u>
Less accumulated amortization	(719)	(362)
	<u>\$35,941</u>	<u>\$ 685</u>

6. LONG-TERM DEBT

Long-term debt consists of the following:

	<u>December 31,</u>	
	<u>1997</u>	<u>1996</u>
Note payable	\$ 855	\$ 665
Capital leases	126	220
	981	885
Less current portion	(392)	(336)
	<u>\$ 589</u>	<u>\$ 549</u>

Note Payable—In June 1996, OpCo entered into a note payable to finance liability insurance premiums. This note was amended in December 1997 to increase the principal balance. The principal balance was changed to \$887 and the maturity date was extended to May 2000. The note accrues interest at an annual rate of 6.4% and requires monthly payments of principal and interest. OpCo incurred interest expense of \$33 and \$19 during 1997 and 1996, respectively.

Capital Leases—OpCo has entered into various capital leases for office equipment which expire between 1998 and 2000. The leases require monthly payments of principal and interest. Interest rates on the leases range from 6.4% to 13.3%. The Company incurred interest expense on the leases of \$23 in 1997, \$28 in 1996, and \$18 in 1995.

Future Maturities—Aggregate future maturities of the above obligations are as follows:

1998	\$392
1999	417
2000	<u>172</u>
	<u>\$981</u>

During 1996 and 1995, OpCo incurred interest expense of \$76 and \$26, respectively, on the note payable to an affiliate of OpCo.

OPCO

NOTES TO COMBINED FINANCIAL STATEMENTS—(Continued)

December 31, 1997, 1996 and 1995

(Dollars in Thousands)

9. ACQUISITIONS

In November 1997, CapStar acquired substantially all of the assets of Winston Hospitality, Inc. ("Winston") for a purchase price of \$34,000 and contributed the assets to OpCo. Winston leased 38 and managed 28 of the operating hotels of Winston Hotels, Inc., a real estate investment trust. The acquisition of Winston has been accounted for as a purchase and, accordingly, the operating results of Winston have been included in OpCo's combined financial statements since the date of acquisition. The excess of the aggregate purchase price over the fair market value of net identifiable assets acquired was approximately \$27,605 and is being amortized over 40 years.

The following unaudited pro forma summary presents information as if Winston had been acquired at the beginning of the periods presented. The pro forma information is provided for informational purposes only. It is based on historical information and does not necessarily reflect the actual results that would have occurred nor is it necessarily indicative of future results of operations of OpCo.

PRO FORMA INFORMATION (UNAUDITED)

	1997	1996
Total revenue	\$94,911	\$68,895
Net income before minority interest	3,991	253
Net income	3,698	235

10. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

The following is a summary of the OpCo's quarterly results of operations:

	1997			
	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
Total revenue	\$1,838	\$2,816	\$4,794	\$14,391
Total operating expenses	1,390	2,129	3,911	13,434
Net operating income	448	687	883	957
Net income	424	650	861	927

	1996			
	<u>First Quarter</u>	<u>Second Quarter</u>	<u>Third Quarter</u>	<u>Fourth Quarter</u>
Total revenue	\$1,158	\$1,812	\$1,982	\$ 2,098
Total operating expenses	1,066	1,668	1,824	1,931
Net operating income	92	144	158	167
Net income	72	113	123	130

REPORT OF INDEPENDENT ACCOUNTANTS

The Shareholders
Winston Hospitality, Inc.

We have audited the accompanying balance sheets of Winston Hospitality, Inc. as of October 31, 1997 and December 31, 1996 and the related statements of income, shareholders' equity and cash flows for the 10 months ended October 31, 1997 and the years ended December 31, 1996 and 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Winston Hospitality, Inc. as October 31, 1997 and December 31, 1996 and the results of its operations and its cash flows for the 10 months ended October 31, 1997 and the years ended December 31, 1996 and 1995, in conformity with generally accepted accounting principles.

/s/ COOPERS & LYBRAND L.L.P.

Raleigh, North Carolina
February 6, 1998

WINSTON HOSPITALITY, INC.

STATEMENTS OF INCOME

For the ten months ended October 31, 1997 and 1996 and
the years ended December 31, 1996 and 1995

(\$ in thousands)

	Ten Months Ended October 31.		Years Ended December 31.	
	1997	1996 (unaudited)	1996	1995
Revenue:				
Room	\$67,145	\$49,633	\$58,956	\$39,677
Food and beverage	2,419	1,240	1,685	138
Other operating, net	1,373	1,068	1,191	877
Interest income	152	82	93	85
Total revenue	<u>71,089</u>	<u>52,023</u>	<u>61,925</u>	<u>40,777</u>
Expenses:				
Property and operating	24,112	17,388	21,550	14,124
Property repairs and maintenance	3,193	2,614	3,181	1,909
Food and beverage	1,715	924	1,281	189
General and administrative	2,090	1,603	2,050	1,526
Franchise costs	6,167	4,327	5,361	3,565
Management fees	1,015	1,109	1,126	784
Percentage lease payments	30,980	22,800	26,611	17,148
Total expenses	<u>69,272</u>	<u>50,765</u>	<u>61,160</u>	<u>39,245</u>
Net income	<u>\$ 1,817</u>	<u>\$ 1,258</u>	<u>\$ 765</u>	<u>\$ 1,532</u>

The accompanying notes are an integral part of the financial statements.

WINSTON HOSPITALITY, INC.

STATEMENTS OF CASH FLOWS

For the ten months ended October 31, 1997 and 1996
and the years ended December 31, 1996 and 1995

(\$ in thousands)

	Ten Months Ended October 31,		Years Ended December 31,	
	1997	1996	1996	1995
	(unaudited)			
Cash flows from operating activities:				
Net income	\$ 1,817	\$ 1,258	\$ 765	\$ 1,532
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	67	65	83	63
Changes in assets and liabilities:				
Accounts receivable—trade	(1,137)	(1,525)	(330)	(310)
Prepaid expenses and other assets	38	(137)	(103)	(65)
Accounts payable—trade	659	547	666	132
Percentage lease payable to Lessor	(729)	532	2,064	1,159
Accrued expenses and other liabilities	906	1,045	914	30
Net cash provided by operating activities	<u>1,621</u>	<u>1,785</u>	<u>4,059</u>	<u>2,541</u>
Cash flows from investing activities:				
Purchases of furniture, fixtures and equipment	(76)	(107)	(144)	(67)
Repayments from (advances to) Lessor, affiliates and shareholders, net	518	(265)	(145)	(1,233)
Net cash provided by (used in) investing activities	<u>442</u>	<u>(372)</u>	<u>(289)</u>	<u>(1,300)</u>
Cash flows from financing activities:				
Distributions to shareholders	(600)	(485)	(556)	(1,112)
Net cash used in financing activities	<u>(600)</u>	<u>(485)</u>	<u>(556)</u>	<u>(1,112)</u>
Net increase in cash and cash equivalents	1,463	928	3,214	129
Cash and cash equivalents at beginning of the period	5,463	2,249	2,249	2,120
Cash and cash equivalents at end of the period	<u>\$ 6,926</u>	<u>\$ 3,177</u>	<u>\$ 5,463</u>	<u>\$ 2,249</u>

The accompanying notes are an integral part of the financial statements.

WINSTON HOSPITALITY, INC.
NOTES TO FINANCIAL STATEMENTS—(continued)
(Dollars in Thousands)

3. Commitments:

Under the terms of the Percentage Lease Agreements, Hospitality had future lease commitments to the Company through 2006. As disclosed in Note 6 below, all Percentage Leases were sold as of November 24, 1997.

Hospitality incurred minimum rents of \$13,535, \$11,154 and \$7,853 as well as percentage rents of \$17,445, \$15,457 and \$9,295 for the ten months ended October 31, 1997 and the years ended December 31, 1996 and 1995, respectively.

Hospitality had entered into separate contracts with unrelated parties for the management of 10 of the hotels. The terms of these agreements provided for management fees to be paid based on predetermined formulas for a period of ten years through 2006. The contracts were cancelable under certain circumstances as outlined in the agreements. As disclosed in Note 6 below, all such contracts were sold as of November 24, 1997.

Various legal proceedings against Hospitality have arisen from time to time in the normal course of business. Management believes liabilities arising from these proceedings, if any, will have no material adverse effect on the financial positions or results of operations of Hospitality.

4. Distributions:

Beginning with the year ended December 31, 1996, the shareholders agreed to limit distributions by Hospitality to amounts necessary to pay their income taxes on the net income derived from Hospitality until such time as the tangible net worth of Hospitality reached \$4,000. Thereafter, they agreed to invest at least 75% of their after-tax distributions of net income from Hospitality in Common Stock of the Company. These agreements terminated effective November 24, 1997, due to the sale of the leases to CapStar.

5. Profit Sharing Plan:

On January 1, 1996, Hospitality adopted the Winston 401(k) Plan (the "Plan") for substantially all employees, except any highly compensated employee, as defined in the Plan, who had attained the age of 21 and completed one year of service. Under the Plan, employees were able to contribute from 1% to 15% of compensation, subject to an annual maximum as determined under the Internal Revenue Code. Hospitality made matching contributions of a specified percentage of the employee's contribution currently 3% of the first 6% of the employee's contribution, and may make additional discretionary contributions. Hospitality contributed \$54, \$50 (unaudited) and \$61 during the 10-month periods ended October 31, 1997 and 1996, and the year ended December 31, 1996, respectively.

6. Subsequent Event:

On November 24, 1997, Hospitality completed the sale of substantially all of its assets and all 38 existing Percentage Leases to CapStar Management Company, L.P. ("CMC") for total consideration of \$34,000. The \$34,000 sale price consisted of \$10,000 in cash and 674,236 CMC Partnership Units.

AMERICAN GENERAL HOSPITALITY, INC.

BALANCE SHEETS

ASSETS	<u>December 31, 1997</u>	<u>December 31, 1996</u>	<u>March 31, 1998</u> (unaudited)
Current assets:			
Cash and cash equivalents	\$1,900,176	\$ 455,058	\$3,234,315
Accounts and management fees receivable	1,756,317	1,731,204	1,768,463
Accounts receivable, affiliates	167,621	103,574	35,193
Prepaid expenses	<u>36,010</u>	<u>13,229</u>	<u>34,519</u>
Total current assets	3,860,124	2,303,065	5,072,490
Investments in property and equipment, at cost:			
Furniture and equipment	1,155,220	522,696	1,317,040
Leasehold improvements	<u>88,049</u>	<u>6,960</u>	<u>93,260</u>
	1,243,269	529,656	1,410,300
Less accumulated depreciation	<u>300,362</u>	<u>334,933</u>	<u>327,362</u>
Net investments in property and equipment	<u>942,907</u>	<u>194,723</u>	<u>1,082,938</u>
Deposits	78,860	50	78,860
Goodwill, net of accumulated amortization of \$2,250, \$2,000, and \$2,312 (unaudited) as of December 31, 1997 and 1996 and March 31, 1998, respectively	7,750	8,000	7,688
Other assets	<u>—</u>	<u>1,477</u>	<u>—</u>
Total assets	<u>\$4,889,641</u>	<u>\$2,507,315</u>	<u>\$6,241,976</u>
LIABILITIES AND STOCKHOLDERS' EQUITY			
Accounts payable	\$ 77,499	\$ 474,253	\$2,366,542
Accounts payable, affiliates	1,275,000	42,770	1,275,000
Accrued liabilities	2,795,477	1,268,895	1,507,866
Deferred revenue	<u>48,699</u>	<u>148,586</u>	<u>—</u>
Total current liabilities	<u>4,196,675</u>	<u>1,934,504</u>	<u>5,149,408</u>
Commitments and contingencies (Notes 3 and 5)			
Stockholders' equity:			
Common stock, \$.01 par value, 100,000 shares authorized, 600 shares issued and outstanding	6	6	6
Additional paid-in capital	584,143	584,143	584,143
Retained earnings	<u>108,817</u>	<u>(11,338)</u>	<u>508,419</u>
Total stockholders' equity	<u>692,966</u>	<u>572,811</u>	<u>1,092,568</u>
Total liabilities and stockholders' equity	<u>\$4,889,641</u>	<u>\$2,507,315</u>	<u>\$6,241,976</u>

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

AMERICAN GENERAL HOSPITALITY, INC.

STATEMENTS OF STOCKHOLDERS' EQUITY

For The Years Ended December 31, 1997, 1996, and 1995
and the Three Months Ended March 31, 1998

	Common Stock		Additional Paid-In Capital	Retained Earnings (Deficit)	Total Stockholders' Equity
	Shares	Amount			
Balance, December 31, 1994	600	\$6	\$584,143	\$(223,877)	\$ 360,272
Net loss	—	—	—	(380,883)	(380,883)
Balance, December 31, 1995	600	6	584,143	(604,760)	(20,611)
Net income	—	—	—	593,422	593,422
Balance, December 31, 1996	600	6	584,143	(11,338)	572,811
Net income	—	—	—	120,155	120,155
Balance, December 31, 1997	600	6	584,143	108,817	692,966
Net income (unaudited)	—	—	—	399,602	399,602
Balance, March 31, 1998 (unaudited)	<u>600</u>	<u>\$6</u>	<u>\$584,143</u>	<u>\$ 508,419</u>	<u>\$1,092,568</u>

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

AMERICAN GENERAL HOSPITALITY, INC.
NOTES TO FINANCIAL STATEMENTS

1. ORGANIZATION:

American General Hospitality, Inc. (the "Company"), a Texas corporation, was incorporated in November 1988 and provides hotel management and consulting services to hotels throughout the United States.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

Cash and Cash Equivalents

For the purposes of the statement of cash flows, the Company considers all certificates of deposit and debt instruments with original maturities of three months or less to be cash equivalents. The Company maintains its cash in bank deposit accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash and cash equivalents.

Investments in Property and Equipment

Property and equipment consist of furniture, equipment, computer equipment and leasehold improvements and are stated at cost. Depreciation is provided by using the straight-line method over estimated useful lives of five to seven years for furniture and equipment and three years for leasehold improvements. This is considered reasonable for financial reporting purposes and is not materially different from estimated useful lives.

Maintenance and repairs are charged to operations as incurred; major renewals and improvements are capitalized. Upon the sale or disposition of a fixed asset, the asset and related accumulated depreciation accounts are removed from the accounts and the related gain or loss is included in operations.

Goodwill

Goodwill in the amount of \$10,000 was recorded when the S Corporation was originally formed in 1988. The goodwill is being amortized using the straight line method over a 40 year period.

Revenue Recognition

Revenue is recognized as earned. Ongoing credit evaluations are performed and an allowance for potential credit losses is provided against the portion of accounts receivable which is estimated to be uncollectible.

Advertising Cost

The Company participates in various advertising and marketing programs. All advertising costs are expensed in the period incurred.

Concentrations of Risk

The Company places cash deposits at a major bank. At December 31, 1997, bank account balances exceed Federal Deposit Insurance Corporation limits by approximately \$2,330,000. Management believes credit risk related to these deposits is minimal.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and

AMERICAN GENERAL HOSPITALITY, INC.

NOTES TO FINANCIAL STATEMENTS—(Continued)

Company employs all hotel employees for the properties and is reimbursed by the property owners. At December 31, 1997, there were approximately 7,500 employees.

7. RELATED PARTY TRANSACTIONS:

Accounts receivable-affiliates represents amounts due from affiliates for property renovations, purchases, potential investments, shared expenses and other advances.

Accounts payable-affiliates represents amounts due to affiliates for advances.

During 1997, 1996 and 1995, the Company received fee revenue for management, consulting and accounting services provided in the amount of \$866,969, \$121,087 and \$249,088, respectively, from entities affiliated with the Company through common ownership.

In addition, the Company paid consulting fees of \$2,227,077, \$3,979,446 and \$4,056,477 during 1997, 1996 and 1995, respectively, to an affiliated entity.

8. FAIR VALUE OF FINANCIAL INSTRUMENTS:

Statements of Financial Accounting Standards No. 107 requires all entities to disclose the fair value of certain financial instruments in their financial statements. Accordingly, the Company reports the carrying amounts of cash and cash equivalents, accounts receivable, accounts payable, accrued expenses and other liabilities at cost, which approximates fair value due to the short maturity of these instruments.

9. SUBSEQUENT EVENTS:

On March 15, 1998 American General Hospitality Corporation (the "REIT") and an affiliate and CapStar Hotel Company ("CapStar") entered into a definitive agreement (the "Merger Agreement") pursuant to which the parties agreed, subject to stockholder approval and other conditions and covenants, to merge as equals (the "Proposed Merger"). Accordingly, no assurance can be given that the Proposed Merger will be consummated. Pursuant to the Merger Agreement, CapStar will spin off (the "Spin-Off") in a taxable transaction, its hotel operations and management business to its current stockholders as a new C Corporation to be called MeriStar Hotels & Resorts, Inc. ("MeriStar Resorts"). CapStar will subsequently merge with and into the REIT, which will qualify as a reorganization under Section 368 of the Internal Revenue Code of 1986, as amended (the "Code"). The REIT will be renamed MeriStar Hospitality Corporation after the Proposed Merger. In a separate transaction, which will close immediately after the closing of the Proposed Merger, MeriStar Resorts will acquire AGH Leasing (an affiliate) and the Company which acquisition is a condition to closing the Proposed Merger. If the Proposed Merger is consummated, MeriStar Resorts will become the lessee and manager of all of the Current Hotels currently leased by AGH Leasing and will have a right of first refusal to become the lessee of hotels acquired by the Company in the future except for the Prime Group II Acquisition hotels.

The Merger Agreement defines the exchange ratios for both the REIT's and CapStar's stockholders. CapStar stockholders will receive one share each of MeriStar Hospitality Corporation and MeriStar Resorts for each CapStar share owned. The REIT's stockholders will receive 0.8475 shares of MeriStar Hospitality Corporation for each share of common stock owned. Both exchange ratios are fixed, with no adjustment mechanism.

The REIT expects the Proposed Merger to close in June 1998. The Proposed Merger will be submitted for approval at separate meetings of the stockholders of the REIT and CapStar. Prior to such stockholder meetings, the REIT will file a registration statement with the SEC registering under the Securities Act of 1933, as amended, the shares of MeriStar Hospitality Corporation to be issued in the Proposed Merger.

AGH LEASING, L.P.
CONSOLIDATED BALANCE SHEETS

	<u>December 31, 1997</u>	<u>December 31, 1996</u>	<u>March 31, 1998</u> (unaudited)
ASSETS			
Investments in hotel properties, at cost			
Furniture, fixtures and equipment	\$ 315,000	\$ 315,000	\$ 315,000
Less accumulated depreciation	(89,250)	(26,250)	(105,000)
Net investment in hotel properties	225,750	288,750	210,000
Cash and cash equivalents	8,781,329	5,673,232	24,644,714
Accounts receivable, net of allowance for doubtful accounts of \$73,915, \$5,291 and \$80,987 (unaudited) as of December 31, 1997 and 1996 and March 31, 1998, respectively	6,247,083	2,822,936	12,594,508
Inventories	1,007,296	448,234	1,508,406
Prepaid expenses	1,067,384	553,400	1,165,999
Deferred expenses	159,207	194,287	148,859
Other assets	283,997	47,985	457,900
Total assets	<u>\$17,772,046</u>	<u>\$10,028,824</u>	<u>\$40,730,386</u>
LIABILITIES AND PARTNERS' EQUITY (DEFICIT)			
Accounts payable, trade	\$ 2,642,639	\$ 1,054,902	\$ 5,309,072
Participating Lease payable, American General Hospitality Operating Partnership, L.P	7,999,122	3,979,242	17,371,456
Note payable to American General Hospitality Operating Partnership, L.P	234,321	287,684	220,136
Accrued expenses and other liabilities	5,327,522	4,198,035	13,227,644
Deferred income	2,100,000	730,000	2,047,500
Minority interest in Twin Towers Leasing, L.P	1,197,442	—	1,197,442
Total liabilities	<u>19,501,046</u>	<u>10,249,863</u>	<u>39,373,250</u>
Commitments and contingencies (Notes 1 and 2)			
Partner's Capital (deficit)—General Partner	(17,290)	(2,210)	13,571
Partner's Capital (deficit)—Limited Partners	(1,711,710)	(218,829)	1,343,565
Total partners' (deficit)	<u>(1,729,000)</u>	<u>(221,039)</u>	<u>1,357,136</u>
Total liabilities and partners' (deficit)	<u>\$17,772,046</u>	<u>\$10,028,824</u>	<u>\$40,730,386</u>

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

AGH LEASING, L.P.

CONSOLIDATED STATEMENTS OF PARTNERS' DEFICIT

For the Period From July 31, 1996 (Inception of Operations)

Through December 31, 1996

and For The Year Ended December 31, 1997

	General Partner 1%	Limited Partners 99%	Total
Initial capitalization at inception	\$ 5,000	\$ 495,000	\$ 500,000
Net loss for the period from July 31, 1996 through December 31, 1996	(7,210)	(713,829)	(721,039)
Balance at December 31, 1996	(2,210)	(218,829)	(221,039)
Partner distributions	(571)	(56,535)	(57,106)
Net loss for the year ended December 31, 1997	(14,509)	(1,436,346)	(1,450,855)
Balance at December 31, 1997	<u>\$(17,290)</u>	<u>\$(1,711,710)</u>	<u>\$(1,729,000)</u>
Net income for the three months ended March 31, 1998 (unaudited)	30,861	3,055,275	3,086,136
Balance at March 31, 1998 (unaudited)	<u>\$ 13,571</u>	<u>\$ 1,343,565</u>	<u>\$ 1,357,136</u>

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

I. ORGANIZATION

AGH Leasing, L.P. is a Delaware limited partnership which was formed on May 29, 1996, and commenced operations on July 31, 1996. AGH Leasing is owned in part by certain executive officers of American General Hospitality Corporation (the "Company") and American General Hospitality, Inc. ("AGHI"). AGH Leasing, L.P. leases 26 of the 27 Hotels (the "December 31 Hotels") owned by American General Hospitality Operating Partnership, L.P. (the "Operating Partnership") at December 31, 1997, pursuant to operating leases ("Participating Leases") which provide for rent based on the revenues of the December 31 Hotels.

During 1996, the Company acquired two of the December 31 Hotels for an aggregate acquisition price of \$49 million. During 1997, the Company acquired twelve of the December 31 Hotels for an aggregate acquisition price of \$289.7 million. The acquisitions were accounted for by the Company under the purchase method of accounting. Thirteen of the fourteen acquired hotels were subsequently leased to AGH Leasing, L.P. pursuant to the Participating Leases with the remaining hotel being leased to Twin Towers Leasing, L.P. The results of operations of the acquired hotels have been included in the reported results from the date of acquisition.

Twin Towers Leasing, L.P. ("Twin Towers Leasing" and, together with AGH Leasing, L.P., "AGH Leasing") leases the remaining December 31 Hotel, the Radisson Twin Towers Orlando, pursuant to a Participating Lease which is substantially similar in form to the other Participating Leases. Twin Towers Leasing is a Florida limited partnership which was formed on June 1, 1997, and commenced operations on June 25, 1997. AGH Leasing is the 51% sole general partner of Twin Towers Leasing. The remaining 49% is owned by Regent Carolina Corporation ("Regent"), an affiliate of the selling entity. Based on the partnership agreement, Regent is allocated 100% of any losses generated by Twin Towers Leasing up to their capital contribution of \$3 million. The operations of Twin Towers Leasing are consolidated with the operations of AGH Leasing for financial statement purposes.

The consolidated financial statements of AGH Leasing include the results of operations of the December 31 Hotels leased from the Operating Partnership due to AGH Leasing's control over the operations of the December 31 Hotels during the 12-year term of the Participating Leases. AGH Leasing has complete discretion in establishing room rates and all rates for hotel goods and services. Likewise, all operating expenses of the December 31 Hotels are under the control of AGH Leasing. AGH Leasing has the right to manage or to enter into management contracts with other parties to manage the December 31 Hotels. If AGH Leasing elects to enter into management contracts with parties other than AGHI, AGH Leasing must obtain the prior written consent of the Operating Partnership, which consent may not be unreasonably withheld. AGH Leasing has entered into management agreements pursuant to which 26 of the December 31 Hotels are managed by AGHI and the remaining December 31 Hotel is managed by Wyndham Hotel Corporation.

AGH Leasing's results of operations are seasonal. The aggregate room revenues in the second and third quarters of each fiscal year may be higher than room revenues in the first quarter and fourth quarter of each fiscal year. Consequently, AGH Leasing may have net income in some quarters and may have net losses in other quarters of the same year.

Upon consummation of the Company's Initial Public Offering ("IPO"), the partners of AGH Leasing capitalized AGH Leasing with \$500,000 cash and pledged 275,000 units of limited partnership interest in the Operating Partnership ("OP Units") to the Company to collateralize the Lessee's obligations under the Participating Leases. Twin Towers Leasing was capitalized with \$3 million by the 49% limited partner upon commencement of operations.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

3. FAIR VALUE OF FINANCIAL INSTRUMENTS

Statements of Financial Accounting Standards 107 requires all entities to disclose the fair value of certain financial instruments in their financial statements. Accordingly, the Lessee reports the carrying amounts of cash and cash equivalents, accounts receivable, accounts payable, participating lease payable, note payable, accrued expenses and other liabilities at cost, which approximates fair value due to the short maturity of these instruments.

4. COMMITMENTS AND RELATED PARTY TRANSACTIONS

Franchise costs represent the annual expense for franchise royalties and reservation services under the terms of hotel franchise agreements, which expire from 1998 to 2013. Franchise costs are based upon varying percentages of gross room revenue ranging from 2.0% to 5.0%. These fees are paid by the Lessee. No franchise costs were incurred for the Hotel Maison de Ville.

Twenty-six of the December 31 Hotels are managed by AGHI on behalf of AGH Leasing. AGH Leasing pays AGHI a base management fee of 1.5% of total revenue and an incentive fee of up to 2.0% of total revenue. The incentive fee, if applicable, is equal to 0.025% of annual total revenue for each 0.1% increase in annual total revenue over the total revenues for the preceding twelve-month period up to the maximum incentive fee.

The remaining December 31 Hotel, the Wyndham Garden Hotel Marietta, is managed by Wyndham Hotel Corporation ("Wyndham") on behalf of AGH Leasing. AGH Leasing pays Wyndham a base management fee equal to 1.5% of gross revenues at the hotel plus an incentive management fee of up to 1.5% of gross revenues. The incentive fee, if applicable, will be earned if gross revenues exceed certain year over year thresholds.

Each December 31 Hotel, except the Hotel Maison de Ville, is required to remit varying percentages of gross room revenue ranging from 1.0% to 5.0% to the various franchisors for sales and advertising expenses incurred to promote the hotel at the national level. Additional sales and advertising costs are incurred at the local property level. These fees are paid by AGH Leasing.

The Company entered into an agreement for a license and an association membership from one of the sellers of the Wyndham Safari Lake Buena Vista, which the Company immediately assigned to AGH Leasing. Commencing January 1998, in connection with the license and the association membership, the Lessee is required to pay recurring association fees including a base monthly fee equal to 1.0% of the prior month's gross room revenues generated at the Hotel, and an additional fee of 0.5% to 1.0% of gross monthly revenues if the trailing twelve month's gross room revenues at the Hotel exceed a threshold of approximately \$13 million (subject to increase based on the percentage increase in the CPI). In addition, the Lessee is obligated to pay a recurring royalty for the African Safari theme equal to an amount which ranges from 10% to 25% of net operating income in excess of \$6 million (subject to adjustment if the Operating Partnership invests more than \$40 million in the Hotel). AGH Leasing is also obligated to pay a marketing assistance fee equal to .25% of gross room revenues. The marketing and association fees are not expected to exceed 2.25% of gross room revenues for any twelve-month period. The association membership agreement terminates in October 2008; AGH Leasing is obligated to pay liquidated damages if the agreement is terminated earlier.

In order to facilitate compliance with state and local liquor laws and regulations, AGH Leasing subleases those areas of certain of the hotels that comprise the restaurant and other areas where alcoholic beverages are served to the Beverage Corporations, 39 of which are wholly owned by a senior executive of the Company. In accordance with the terms of the Beverage Subleases, each Beverage Corporation is obligated to pay to AGH Leasing rent payments equal to 30% of each such corporation's annual gross revenues generated from the sale of alcoholic beverages generated from such areas. Such sublease income is reported in other revenue. Pursuant to the Participating Leases, such subleases will not reduce the Participating Rent payments to the Operating Partnership, which it is entitled to receive from such beverage sales.

AGH LEASING, L.P.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

6. SUBSEQUENT EVENTS

Proposed Merger

On March 15, 1998 the Company and CapStar Hotel Company ("CapStar") entered into a definitive agreement (the "Merger Agreement") pursuant to which the parties agreed, subject to stockholder approval and other conditions and covenants, to merge as equals (the "Proposed Merger"). Accordingly, no assurance can be given that the Proposed Merger will be consummated. Pursuant to the Merger Agreement, CapStar will spin off (the "Spin-Off") in a taxable transaction, its hotel operations and management business to its current stockholders as a new C-Corporation to be called MeriStar Hotels & Resorts, Inc. ("MeriStar Resorts"). CapStar will subsequently merge with and into the Company, which will qualify as a reorganization under Section 368 of the Internal Revenue Code of 1986, as amended (the "Code"). The Company will be renamed MeriStar Hospitality Corporation after the Proposed Merger. In a separate transaction, which will close immediately after the closing of the Proposed Merger, MeriStar Resorts will acquire AGH Leasing and AGHI which is payable through the issuance of \$11.2 million of units of limited partnership interests of a subsidiary owned by MeriStar Resorts and \$83.8 million in cash. This acquisition is a condition to closing the Proposed Merger. If the Proposed Merger is consummated, MeriStar Resorts will become the lessee and manager of all of the Current Hotels currently leased by AGH Leasing and will have a right of first refusal to become the lessee of hotels acquired by the Company in the future except for the Prime Group II Acquisition hotels.

The Merger Agreement defines the exchange ratios for both the Company's and CapStar's stockholders. CapStar stockholders will receive one share each of MeriStar Hospitality Corporation and MeriStar Resorts for each CapStar share owned. The Company's stockholders will receive 0.8475 shares of MeriStar Hospitality Corporation for each share of Common Stock owned. Both exchange ratios are fixed, with no adjustment mechanism.

The Company expects the Proposed Merger to close in June 1998. The Proposed Merger will be submitted for approval at separate meetings of the stockholders of the Company and CapStar. Prior to such stockholder meetings, the Company will file a registration statement with the SEC registering under the Securities Act of 1933, as amended, the shares of MeriStar Hospitality Corporation to be issued in the Proposed Merger.

AGH LEASING, L.P.
PRO FORMA STATEMENT OF OPERATIONS
For The Year Ended December 31, 1997
(Unaudited)

	Historical Year Ended December 31, 1997 (A)	December 31 Hotels Pro Forma Adjustments (B)	Acquired Hotels (C)	Proposed Acquisition Hotel (C)	Management Fees Adjustment (G)	Combined Pro Forma
Revenues						
Room revenue (D)	\$123,965,649	\$27,806,341	\$ 99,361,895	\$1,379,556	\$ —	\$252,513,441
Food and beverage revenue (D)	28,626,625	7,674,974	25,145,757	207,374	—	61,654,730
Other revenue (D)	10,121,833	2,256,516	8,380,871	82,507	—	20,841,727
Minority interest income (E)	1,802,558	(139,150)	—	—	—	1,663,408
Total revenue	\$164,516,665	\$37,598,681	\$132,888,523	\$1,669,437	—	\$336,673,306
Expenses						
Property operating costs and expenses (F) ..	33,894,184	6,754,081	26,658,014	456,500	—	67,762,779
Food and beverage costs and expenses (F) ..	22,768,224	5,297,676	20,218,787	121,170	—	48,405,857
General and administrative (F)	15,871,676	2,978,176	11,792,008	241,768	—	30,883,628
Advertising and promotion (F)	12,792,700	2,489,673	8,638,295	68,533	—	23,989,201
Repairs and maintenance (F)	6,712,883	1,756,796	6,399,372	95,048	—	14,964,099
Utilities (F)	7,258,674	1,532,149	6,198,780	95,716	—	15,085,319
Management fees (G)	1,691,639	1,158,265	2,694,902	42,106	1,767,977	7,354,889
Franchise costs (H)	4,754,285	1,041,672	3,945,161	50,095	—	9,791,213
Depreciation	63,000	—	—	—	—	63,000
Amortization (I)	40,997	—	—	—	—	40,997
Interest expense	26,808	237,256	—	—	—	264,064
Other expense	158,113	173,116	79,997	—	—	411,226
Participating Lease expenses (J)	59,934,337	14,258,118	45,298,537	637,336	—	120,128,328
Total expenses	165,967,520	37,676,978	131,923,853	1,808,272	1,767,977	339,144,600
Net income (loss)	\$ (1,450,855)	\$ (78,297)	\$ 964,670	\$ (138,835)	\$(1,767,977)	\$ (2,471,294)

AGH LEASING, L.P.

NOTES TO PRO FORMA CONSOLIDATED STATEMENTS OF OPERATIONS—(Continued)

- (D) Represents historical room, food and beverage and other revenues of the AGH Hotels.
- (E) Represents the amount of AGH Leasing's minority interest investment in Twin Towers Leasing, L.P. (the "Twin Towers Lessee", together with AGH Leasing, L.P., "AGH Leasing") which leases the Radisson Orlando Twin Towers hotel from the Operating Partnership. The Twin Towers Lessee is owned 51% by AGH Leasing, which is the sole general partner, and 49% by Regent Carolina Corporation, which is the sole limited partner. Regent Carolina Corporation is not affiliated with the Company, the Operating Partnership or AGH Leasing.
- (F) Represents the historical expenses of the AGH Hotels.
- (G) Represents management fees to be incurred under the Management Agreements. The management fees payable to AGHI consist of a base fee of 1.5% of total revenue and an incentive fee of up to 2.0% of total revenue. The incentive fee, if applicable, is equal to 0.025% of annual total revenue for each 0.01% increase in annual total revenues over the total revenues for the preceding twelve month period up to the maximum incentive fee. The payment of the management fees to AGHI by AGH Leasing is subordinate to AGH Leasing's obligations to the Company under the Participating Leases. The full management fee payable during 1997 will be earned only to the extent that AGH Leasing has taxable income equal to or greater than \$50,000. If AGH Leasing's taxable net operating income is below \$50,000 in 1997, management fees are forfeited by AGHI to increase AGH Leasing's taxable net operating income to \$50,000.

	<u>Base management fee</u>	<u>Incentive management fee</u>	<u>Total management fee</u>
December 31 Hotels	\$2,849,904	\$ —	\$2,849,904
Acquired Hotels			
Potomac Portfolio Acquisition Hotels and the Holiday Inn O'Hare International Airport Hotel	738,846	614,955	1,353,801
FSA Portfolio Acquisition Hotels	1,341,101	—	1,341,101
Proposed Acquisition Hotel			
Madison Hotel	25,263	16,843	42,106
Management fee adjustment	—	1,767,977	1,767,977
Total management fees	<u>\$4,955,114</u>	<u>\$2,399,775</u>	<u>\$7,354,889</u>

- (H) Represents the historical franchise fees of the AGH Hotels. Franchise fees associated with the hotel conversions are not included in the pro forma statements of operations since other impacts including possible revenue enhancements and operating expense reductions are also not included.
- (I) Historical deferred loan costs and the related amortization has been eliminated since AGH Leasing is not expected to incur similar costs. Amortization expense relates to the amortization of organization costs which are being amortized over a 60 month period.
- (J) Represents lease payments to the Operating Partnership from AGH Leasing pursuant to the Participating Leases calculated on a pro forma basis by applying the rent provisions of the Participating Leases to the revenues of the AGH Hotels. The departmental thresholds in the Participating Leases are seasonally adjusted for interim periods. The Participating Lease payments for the Acquired Hotels and the Proposed Acquisition Hotel are calculated by applying the rent provisions applicable in the first year of the respective leases executed to the historical operating revenues of the hotels prior to the acquisition by the Company.

AGH LEASING, L.P.

PRO FORMA CONSOLIDATED STATEMENT OF OPERATIONS

FOR THE QUARTER ENDED MARCH 31, 1998

The following unaudited Pro Forma Consolidated Statement of Operations is presented as if the 45 hotels which the Company and its affiliates lease to AGH Leasing (the "AGH Leasing March 31 Hotels") and one of the additional hotels to be acquired by the Company and leased to AGH Leasing (the "Proposed Acquisition Hotel", together with AGH Leasing March 31 Hotels, the "AGH Leasing Hotels") were leased pursuant to Participating Leases as of January 1, 1997. The Proposed Acquisition Hotel is the Madison Hotel Acquisition. The Pro Forma Consolidated Statement of Operations does not include the effects of the Proposed Merger with CapStar.

In management's opinion, all material adjustments necessary to reflect the effect of these transactions have been made.

The following unaudited Pro Forma Consolidated Statement of Operation are derived from AGH Leasing's Consolidated Statements of Operations as of March 31, 1998 and should be read in conjunction with the financial statements filed with American General Hospitality Corporation's Quarterly Report on Form 10-Q for the quarter ended March 31, 1998.

The following Pro Forma Consolidated Statement of Operations are not necessarily indicative of what the actual results of operations would have been assuming such transactions had been completed as of January 1, 1997.

AGH LEASING, L.P.

NOTES TO PRO FORMA CONSOLIDATED STATEMENT OF OPERATIONS

The Pro Forma Consolidated Statement of Operations of AGH Leasing, L.P. ("AGH Leasing") include the results of operations of the 45 hotels leased from the American General Hospitality Operating Partnership, L.P. (the "Operating Partnership") due to AGH Leasing's control over the operations of the hotels during the twelve-year term of the Participating Leases. AGH Leasing has complete discretion in establishing room rates and all rates for hotel goods and services. Likewise, all operating expenses of the hotels are under the control of AGH Leasing. AGH Leasing has the right to manage or to enter into management contracts with other parties to manage the hotels. If AGH Leasing elects to enter into management contracts with parties other than American General Hospitality, Inc. ("AGHI"), AGH Leasing must obtain the prior written consent of the Company, which consent may not be unreasonably withheld.

AGH Leasing's results of operations are seasonal. Generally, hotel revenue is greater in the second and third quarters of a calendar year, although this may not be true for hotels in major tourist destinations. With the Company's acquisition and subsequent leasing of the FSA Portfolio Acquisition Hotels, which include several hotels in tourist destinations, the AGH Hotels may now produce greater revenues in the first and second quarters.

- (A) Represents the Company's historical statement of operations for the year ended March 31, 1998.
- (B) Represents the adjustments to present a statement of operations for the 18 hotels acquired by the Company and leased to AGH Leasing during the first quarter of 1998 prior to their acquisition by the Company based on historical balances of the previous owners. The combination of the historical statement of operations presented in column (A) and the pro forma statement of operation presented in column (B) represent the results of operations of the 45 AGH Leasing March 31 Hotels as if all of the AGH Hotels were acquired on January 1, 1997 and leased to AGH Leasing pursuant to a Participating Lease since that date.
- (C) Proposed Acquisition Hotel represents the acquisition of one hotel, the Madison Hotel, to be acquired by the Company and leased to AGH Leasing pursuant to a Participating Lease. The Madison Hotel was closed for a complete renovation in September 1997 and is expected to reopen in July 1998.
- (D) Represents historical room, food and beverage and other revenues of AGH Hotels.
- (E) Represents the historical expenses of the AGH Hotels.
- (F) Represents management fees to be incurred under the Management Agreements. The management fees payable to AGHI consist of a base fee of 1.5% of total revenue and an incentive fee of up to 2.0% of total revenue. The incentive fee, if applicable, is equal to 0.025% of annual total revenue for each 0.01% increase in annual total revenues over the total revenues for the preceding twelve month period up to the maximum incentive fee. The payment of the management fees to AGHI by AGH Leasing is subordinate to AGH Leasing's obligations to the Company under the Participating Leases.

	<u>Base management fee</u>	<u>Incentive management fee</u>	<u>Total management fee</u>
AGH Leasing March 31 Hotels	\$1,403,965	\$666,408	\$2,070,373
Proposed Acquisition Hotel Madison Hotel	0	0	0
Total management fees	<u>\$1,403,965</u>	<u>\$666,408</u>	<u>\$2,070,373</u>

- (G) Represents the historical franchise fees of the AGH Hotels. Franchise fees associated with the hotel conversions are not included in the pro forma statements of operations since other impacts including possible revenue enhancements and operating expense reductions are also not included.
- (H) Historical deferred loan costs and the related amortization has been eliminated since AGH Leasing is not expected to incur similar costs. Amortization expense relates to the amortization of organization costs which are being amortized over a 60 month period.

No dealer, salesperson or any other person has been authorized to give any information or to make any representation not contained in this Prospectus, and, if given or made, such information or representation must not be relied upon as having been authorized by the Company or the Dealer Manager. This Prospectus does not constitute an offer of any securities other than those to which it relates or an offer to sell, or solicitation of an offer to buy, to any person in any jurisdiction where such offer or solicitation would be unlawful. Neither the delivery of this Prospectus nor any sale made hereunder shall, under any circumstances, create any implication that the information contained herein is correct as of any time subsequent to the date hereof.

MeriStar Hotels & Resorts, Inc.

Shares of Common Stock and
Rights to Acquire
up to 8,400,000 of such shares

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Prospectus
August 12, 1998

Until September 6, 1998 (25 days after the date of this Prospectus), all dealers effecting transactions in the common stock distributed pursuant hereto, whether or not participating in this distribution, may be required to deliver a Prospectus. This is in addition to the obligation of dealers to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.

LEHMAN BROTHERS

Dealer Manager