

Registered No 3462675

**Morgans Hotel Group London Limited**

**Annual report**

**For the year ended 31 December 2006**



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# **Morgans Hotel Group London Limited**

## **Annual report for the year ended 31 December 2006**

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## Directors and advisers

### Directors

R Bloom  
J Quicksilver  
E Scheetz  
D Hamamoto

### Secretary and registered office

Bibi Ali  
MacFarlanes  
10 Norwich Street  
London EC4A 1BD

### Solicitors

MacFarlanes  
10 Norwich Street  
London EC4A 1BD

### Registered auditors

BDO Stoy Hayward LLP  
8 Baker Street  
London, W1U 3LL

### Bankers

National Westminster Bank PLC  
135 Bishopsgate  
London EC2M 3UR

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## **Directors' report for the year ended 31 December 2006**

The directors present their report and the audited financial statements of the company for the year ended 31 December 2006

### **Principal activities and future developments**

The principal activity of the company is to operate two five star hotels in central London – St Martin's Lane and Sanderson. There have been no changes in the company's activities in the year under review.

### **Review of the business**

The profit and loss account is set out on page 7 and shows the turnover for the year of £30,118,000 (2005 £26,206,000) and a profit for the year of £2,246,000 (2005 loss £5,678,000).

Turnover has increased by 14.9% and for the full year under review is made up of the following categories: rooms 78%, rental and other income 14% and other operating departments 8%.

The directors are pleased with the growth in revenue during the year and are confident in seeing the increased sales continue for 2007. Room's revenue represents the total revenue achieved through the average room rate by the total number of rooms sold during the year. The key indicators are ADR (Average Daily Room Rate) and Occupancy (The total available rooms divided by the rooms occupied expressed as a percentage), and REVPAR which is a combination of both expressed in £'s.

In the year under review the combined occupancy for the hotels was 78.3% (2005 72.3%) an increase of 6 % points, the ADR achieved was £232.93 (2005 £213.76) and REVPAR of £182.34 (2005 £154.55).

The increase in profit for the year under review is £7,924,000 this can be attributed to a number of key elements, the improvement in performance as detailed in the review of turnover and not having the exceptional interest charges as in 2005.

The directors do not recommend the payment of a dividend for the year (2005 nil).

### **Principal risks and uncertainties**

The hotel market in London has been very buoyant during the year under review and continues to be so into 2007. The 5 star hotel category in particular has shown significant REVPAR increases and Sanderson and St Martins Lane have been well positioned to take full advantage of this upturn in the market. The company seeks to manage the risk of losing customers to key competitors by the provision of higher than ordinary service levels coupled with the exciting environment of the hotel properties. The company engages a full service level sales and account management team to work closely with key clients around the world who are important to the continued success of the hotels.

## Employee Involvement

The company's policy is to give full and fair consideration for applications for employment made by people with disabilities. Wherever possible we will continue the employment of staff that become disabled and provide equal opportunities for the training and development of disabled employees.

The company recognises the importance of the employees within its business and annually provides a communication program under the title Vision at which the company's achievements and goals are expressed, employees are encouraged to participate in the delivery of Vision.

## Post Balance Sheet Events

On 16th February 2007 the company entered into a new joint venture agreement with an affiliate of Walton Street Capital LLC, Walton MG London Hotels Investors V LLC, who acquired the 50% joint venture interest in the company from previous owner Burford Hotels Limited.

## Financial Instruments

The company has a loan facility for £107,056,000 at a fixed rate of 6.28% which falls due on 24th November 2010. The facility is fully utilised.

The company's policy in respect of interest rate risk and liquidity risk is to maintain a mixture of long term and short term debt finance and readily accessible bank deposit accounts to ensure the company has sufficient funds for operations. The cash deposits are held in a mixture of short term deposits and current accounts which earn interest at a floating rate.

The company's credit risk is primarily attributable to its trade debtors. Credit risk is managed by running credit checks on new customers and by monitoring payments against the agreed credit terms for specific corporate entities.

The company monitors cash flow as part of its day to day control procedures. The directors consider cash flow projections on a monthly basis to ensure that appropriate facilities are available to be drawn upon as necessary.

## Directors

The directors of the company during and after the year are as follows:

B Porter (appointed 24<sup>th</sup> April 2006 resigned 16<sup>th</sup> February 2007)  
J McCarthy (appointed 24<sup>th</sup> April 2006 resigned 16<sup>th</sup> February 2007)  
R Bloom (appointed 16<sup>th</sup> February 2007)  
J Quicksilver (appointed 16<sup>th</sup> February 2007)  
E Scheetz  
D Hamamoto  
R Anderson (resigned 24<sup>th</sup> April 2006)  
J Gleek (resigned 24<sup>th</sup> April 2006)

## Directors interests

According to the register of directors' interests, none of the directors who held office at the end of the year had any interest in the shares of group companies, nor were any rights to subscribe for shares in group companies granted to, or exercised by, any of these directors.

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## Statement of directors' responsibilities

The directors are responsible for preparing the annual report and the financial statements in accordance with applicable law and United Kingdom Generally Accepted Accounting Practice

Company law requires the directors to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgments and estimates that are reasonable and prudent,
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements,
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the company will continue in business

The directors are responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial position of the company and enable them to ensure that the financial statements comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

## Auditors

All of the current directors have taken all the steps that they ought to have taken to make themselves aware of any information needed by the company's auditors for the purposes of their audit and to establish that the auditors are aware of that information. The directors are not aware of any relevant information of which the auditors are unaware.

PricewaterhouseCoopers LLP resigned as auditors during the year and BDO Stoy Hayward LLP were appointed by the Directors. BDO Stoy Hayward LLP have expressed their willingness to continue in office and a resolution to re-appoint them as auditors will be proposed at the next Annual General Meeting.

By order of the board



Edward Scheetz  
Director

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# **Morgans Hotel Group London Limited**

## **Independent auditors' report to the members of Morgans Hotel Group London Limited**

### **To the shareholders of Morgans Hotel Group London Limited**

We have audited the financial statements of Morgans Hotel Group London for the year ended 31 December 2006 which comprise the profit and loss account, the balance sheet, and the related notes. These financial statements have been prepared under the accounting policies set out therein.

#### *Respective responsibilities of directors and auditors*

The directors' responsibilities for preparing the financial statements in accordance with applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice) are set out in the statement of directors' responsibilities.

Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and have been properly prepared in accordance with the Companies Act 1985 and whether the information given in the directors' report is consistent with those financial statements. We also report to you if, in our opinion, the company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the directors' report and consider the implications for our report if we become aware of any apparent misstatements within it.

Our report has been prepared pursuant to the requirements of the Companies Act 1985 and for no other purpose. No person is entitled to rely on this report unless such a person is a person entitled to rely upon this report by virtue of and for the purpose of the Companies Act 1985 or has been expressly authorised to do so by our prior written consent. Save as above, we do not accept responsibility for this report to any other person or for any other purpose and we hereby expressly disclaim any and all such liability.

#### *Basis of audit opinion*

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgments made by the directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the company's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

# Morgans Hotel Group London Limited

## *Opinion*

In our opinion

- the financial statements give a true and fair view, in accordance with United Kingdom Generally Accepted Accounting Practice, of the state of the company's affairs as at 31 December 2006 and of its profit for the year then ended,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the directors' report is consistent with the financial statements



**BDO STOY HAYWARD LLP**

*Chartered Accountants and Registered Auditors*

London

Date 15 March '07



# Morgans Hotel Group London Limited

## Profit and loss account for the year ended 31 December 2006

	Notes	2006 £000	2005 £000
<b>Turnover</b>	1	30,118	26,206
Cost of sales		<u>(7,560)</u>	<u>(7,084)</u>
<b>Gross profit</b>		<b>22,558</b>	19,122
Administrative expenses		<u>(13,988)</u>	<u>(14,441)</u>
<b>Operating profit</b>	3	<b>8,570</b>	4,681
Interest receivable		397	218
Interest payable and similar charges	4	(6,721)	(7,220)
Exceptional Interest Charge	5	<u>-</u>	<u>(3,357)</u>
<b>Net interest payable</b>		<b>(6,324)</b>	(10,359)
<b>Profit / (Loss) on ordinary activities before taxation</b>		<u><b>2,246</b></u>	<u>(5,678)</u>
Tax on profit / (loss) on ordinary activities	6	-	-
<b>Profit / (Loss) for the financial year</b>		<u><b>(2,246)</b></u>	<u>(5,678)</u>

All income and expenditure arises from continuing operations

The company has no recognised gains or losses other than the profit for the year

The historical cost loss and reported loss are the same

# Morgans Hotel Group London Limited

## Balance sheet At 31 December 2006

	Notes	2006 £000	2006 £000	2005 £000	2005 £000
<b>Fixed assets</b>					
Tangible assets	7		101,828		104,209
<b>Current assets</b>					
Stock	8	209		147	
Debtors	9	15,003		14,572	
Cash at bank and in hand		<u>12,261</u>		<u>8,438</u>	
		27,473		23,157	
<b>Creditors</b> amounts falling due within one year	10	<u>(4,796)</u>		<u>(3,954)</u>	
<b>Net current assets</b>			<u>22,677</u>		<u>19,203</u>
<b>Total assets less current liabilities</b>			124,505		123,412
<b>Creditors</b> amounts falling due after more than one year	11		<u>(103,380)</u>		<u>(104,533)</u>
<b>Net assets</b>			<u>21,125</u>		<u>18,879</u>
<b>Capital and reserves</b>					
Called up share capital	13		-		-
Share premium account	14		35,000		35,000
Profit and loss account	14		<u>(13,875)</u>		<u>(16,121)</u>
<b>Shareholders' funds</b>	15		<u>21,125</u>		<u>18,879</u>

The financial statements on pages 7 to 17 were approved by the board of directors and authorised for issue on 3/15/07

E Scheetz  
Director

R Bloom  
Director

# **Morgans Hotel Group London Limited**

## **Notes to the financial statements for the year ended 31 December 2006**

### **1 Principal accounting policies**

The financial statements have been prepared under the historical cost convention and in accordance with applicable Accounting Standards in the United Kingdom. A summary of the more important accounting policies is set out below.

#### **Cash flow statement**

The company is exempt under FRS1 (revised) from the requirement to prepare a separate cash flow statement on the grounds that its immediate parent, Morgans Hotel Group Europe Limited, incorporates the company's cash flows in its own published consolidated cash flow statements.

#### **Fixed assets and depreciation**

Tangible fixed assets are stated at cost less depreciation and any provision for impairment. Assets are depreciated to their residual values on a straight line basis over their estimated useful lives as follows:

Freehold buildings	50 years
Building surface finishes	25 years
Plant and machinery	15 years
Fixtures, fittings and equipment	5 – 10 years

No depreciation is provided on freehold land. No residual values are ascribed to building surface finishes.

Interest paid on fixed assets purchases is capitalised up until the time the asset is available for use.

#### **Foreign currency transactions**

Translations into sterling are made at the average of rates ruling throughout the period for profit and loss items and at the rate ruling at 31 December 2006 for assets and liabilities. Exchange differences arising in the ordinary course of trading are reflected in the profit and loss account.

#### **Deferred taxation**

Deferred taxation is provided in respect of all timing differences that have originated but not reversed at the balance sheet date, where transactions or events have occurred which result in an obligation to pay more or less tax in the future.

Deferred tax is measured at the average tax rates which apply in the period in which the timing differences are expected to reverse. Deferred tax is measured on a non-discounted basis.

Deferred tax assets are regarded as recoverable and therefore recognised only when, on the basis of all available evidence, it is more likely than not that there will be adequate future taxable profits against which to recover carried forward tax losses.

# Morgans Hotel Group London Limited

## Finance costs

Finance costs are included within the carrying value of the loan and are amortised over the term of the loan

## Stocks

Stocks are stated at the lower of cost and net realisable value. In determining the cost of raw materials and consumables the weighted average purchase price is used.

## Turnover

Turnover represents the amounts (excluding value added tax) derived from the provision of goods and services to customers. Turnover is wholly generated in the United Kingdom.

## Pension scheme

The company operates a defined contribution pension scheme. Contributions are charged to the profit and loss account in the period in which they are incurred.

## 2 Staff numbers and costs

The average number of employees in the year was

	2006 Number	2005 Number
Hotel operating staff	141	150
Management/administration	31	30
Sales and marketing	11	12
Maintenance	20	21
Total	<u>203</u>	<u>213</u>

The aggregate payroll costs for these persons were as follows

	2006 £'000	2005 £'000
Wages and salaries	5,730	5,476
Social security costs	444	407
Pension costs	44	47
	<u>6,218</u>	<u>5,930</u>

None of the directors received any remuneration during the year (2005 Nil)

# Morgans Hotel Group London Limited

## Funded defined contribution scheme for employees (group scheme)

Pension costs of £44,000 (2005 £47,000) were charged to the profit and loss account of which £nil (2005 £nil) was outstanding at the balance sheet date

The pension scheme is held with Standard Life and is administered by Inter Alliance

## 3 Operating profit

	2006	2005
	£'000	£'000
<b>This is arrived at after charging</b>		
<b>Auditors' remuneration</b>		
Audit	40	66
Non audit – (Tax compliance)	-	182
Depreciation of tangible fixed assets	2,778	3,267
Loss on disposal of fixed assets	<u>274</u>	<u>-</u>

## 4 Interest payable and similar charges

	2006	2005
	£'000	£'000
On bank loans and overdrafts	<u>6,721</u>	<u>7,220</u>

## 5 Exceptional Interest charge

During 2005 Morgans Hotel Group London undertook a review of their debt structure. In November 2005 Management took advantage of the improvement in the Company's business performance and a favourable capital market and secured new financing at more competitive rates providing a strong, stable financial base from which to operate in the future. Costs of £3,357,000 were incurred in cancelling the previous loan financing in the 2005 financial statements

# Morgans Hotel Group London Limited

## 6 Tax on profit on ordinary activities

No corporation tax has been provided due to losses incurred in the year (2005 nil)

### (a) Factors affecting tax charge for the year

	2006 £'000	2005 £'000
Profit / (Loss) on ordinary activities before tax	<u>2,246</u>	<u>(5,678)</u>
Profit / (Loss) on ordinary activities multiplied by standard rate of corporation tax in the UK of 30% (2005 30%)	674	(1,703)
<i>Effects of</i>		
Expenses not deductible for tax purposes	171	194
Capital allowances in excess of depreciation	695	739
Tax losses	<u>(1,540)</u>	<u>770</u>
Tax charge for the period	<u>-</u>	<u>-</u>

### (b) Factors affecting future tax charges

In respect of the company's tax losses, no deferred tax asset has been recognised due to uncertainty regarding the company's future trading results

# Morgans Hotel Group London Limited

## 7 Tangible Fixed assets

	Land and buildings £000	Plant and machinery £000	Fixtures, fittings and equipment £000	Total £000
<b>Cost</b>				
At 1 January 2006	100,584	7,999	12,992	121,575
Additions	-	346	325	671
Disposal	-	(55)	(1,710)	(1,765)
<b>At 31 December 2006</b>	<b>100,584</b>	<b>8,290</b>	<b>11,607</b>	<b>120,481</b>
<b>Depreciation</b>				
At 1 January 2006	5,870	3,174	8,322	17,366
Charge for the year	1,029	552	1,197	2,778
Disposals	-	(15)	(1,476)	(1,491)
<b>At 31 December 2006</b>	<b>6,899</b>	<b>3,711</b>	<b>8,043</b>	<b>18,653</b>
<b>Net book value</b>				
<b>At 31 December 2006</b>	<b>93,685</b>	<b>4,579</b>	<b>3,564</b>	<b>101,828</b>
At 31 December 2005	94,714	4,825	4,670	104,209

Included in total net book value of land and buildings is £41,955,000 (2005 £42,839,000) of long leasehold property and £4,219,000 (2005 £4,245,000) of capitalised interest (net of accumulated depreciation)

## 8 Stocks

	2006 £'000	2005 £'000
Consumables	<u>209</u>	<u>147</u>

## 9 Debtors: amounts due within one year

	2006 £'000	2005 £'000
Trade debtors	1,471	1,193
Amounts due from immediate parent undertaking	12,634	12,634
Amounts due from related parties (see note 17)	457	341
Prepayments and accrued income	<u>441</u>	<u>404</u>
	<b>15,003</b>	<b>14,572</b>

# Morgans Hotel Group London Limited

## 10 Creditors. amounts falling within one year

	2006	2005
	£'000	£'000
Bank loans and overdrafts	1,500	1,250
Trade creditors	356	338
Amounts due to related parties (see note 17)	520	469
Taxation and social security	676	399
Accruals and deferred income	1,744	1,498
	<u>4,796</u>	<u>3,954</u>

## 11 Creditors amount falling due after more than one year

	2006	2005
	£'000	£'000
Bank loans and overdrafts	<u>103,380</u>	<u>104,533</u>

Bank loans are repayable as follows

	2006	2005
	£'000	£'000
In one year or less, or on demand	1,500	1,250
In more than one year, but not more than two years	2,083	1,500
In more than two years, but not more than five years	101,297	103,033
	<u>104,880</u>	<u>105,783</u>

Bank loans are as follows

	2006	2005
	£'000	£'000
Sterling bank loan Note 6 280%	104,880	105,783
	<u>104,880</u>	<u>105,783</u>

Bank loans are repayable in monthly instalments, are denominated in sterling and bear interest at a fixed rate as noted above

The bank loan is secured by way of a first ranking legal charge over the properties including fixtures, fittings and property management agreements, and an assignment over all revenues due from the operation of the properties



# Morgans Hotel Group London Limited

## 12 Deferred taxation

	2006	2005
	£'000	£'000
Short term timing differences	107	(726)
Losses	3,005	5,003
Total deferred tax asset	<u>3,112</u>	<u>4,277</u>

Deferred tax assets have not been recognised in respect of the losses carried forward or short term timing differences. These assets can only be utilised against future suitable taxable profits and, at present, it is unclear as to the likelihood and timing of sufficient profits in the foreseeable future.

## 13 Called up share capital

	2006	2005
	£	£
<b>Authorised</b>		
100 ordinary shares of £1 each	100	100
<b>Allotted, called up and fully paid</b>		
50 ordinary shares of £1 each	<u>50</u>	<u>50</u>

## 14 Reserves

	Share premium account £000	Profit and loss account £000	Total £000
At 1 January 2006	35,000	(16,121)	18,879
Profit for the year	-	2,246	2,246
At 31 December 2006	<u>35,000</u>	<u>(13,875)</u>	<u>21,125</u>

# Morgans Hotel Group London Limited

## 15 Reconciliation of movements in shareholders' funds

	2006	2005
	£'000	£'000
Profit / (Loss) for the financial year	2,246	(5,678)
Opening shareholders' funds	18,879	24,557
Closing shareholders' funds	21,125	18,879

## 16 Immediate and ultimate controlling parties

The company's immediate and ultimate parent is Morgan Hotel Group Europe Limited a company registered in England and Wales

Morgans Hotel Group Europe Limited was owned 50% by Burford Hotels Limited, whose ultimate holding company is Lehman Brothers Holdings Inc, a company incorporated in the state of Delaware in the USA

The consolidated accounts of Lehman Brothers Holdings Inc are available to the public from 399, Park Avenue, New York, USA and from One Broadgate, London

From the 16<sup>th</sup> February 2007 Morgans Hotel Group Europe Limited is owned 50% by Walton MG Hotels Investors V, LLC, an affiliate of Walton Street Capital LLC, a company incorporated in the state of Delaware in the USA

The other 50% is owned by Royalton Europe Holdings LLC, a wholly owned subsidiary of Morgans Hotel Group Co, a company incorporated in the USA, whose principal place of business is 475 10<sup>th</sup> Avenue New York, NY 10018 USA

# Morgans Hotel Group London Limited

## 17 Related party transactions

### Morgans Hotel Group UK Management Limited

Morgans Hotel Group UK Management Limited is 100% owned by Morgans Hotel Group LLC

Morgans Hotel Group UK Management Limited charged Morgan Hotel Group London Limited a management fee and staff costs relating to hotel management, which totalled £2,865,000 (2005 £2,520,000)

### SC London Limited

SC London Limited is indirectly owned 50% by Morgans Hotel Group LLC and 50% by Chodorow Ventures LLC

SC London Limited pays rent and recharged expenditure to Morgans Hotel Group London Limited, which totalled £3,729,000 (2005 £3,396,000)

<b>Related party balances and transactions</b>	<b>2006</b>	<b>2005</b>
	<b>£'000</b>	<b>£'000</b>
<b>Debtors amounts falling within one year</b>		
SC London Limited	345	246
Other Morgans Hotel Group companies	112	95
	<u>457</u>	<u>341</u>
	<b>2006</b>	<b>2005</b>
	<b>£'000</b>	<b>£'000</b>
<b>Creditors amounts falling within one year</b>		
Morgans Hotel Group UK Management Limited	318	270
SC London Limited	97	197
Other Morgans Hotel Group companies	105	2
	<u>520</u>	<u>469</u>

The directors confirm that there were no related party transactions other than those disclosed in these financial statements and that all transactions were undertaken on an arms length basis