Promus Hotel Corporation Opens Its Doors

1995 Annual Report

FINANCIAL AND STATISTICAL HIGHLIGHTS

Our vision is to be the premier hotel company in the world by offering high quality, value-based lodging products in well-defined market segments, and by having the best people, trained and empowered to deliver excellent service to every customer, every time... Guaranteed.

(In thousands, except percentages and ratios)	*1995*	*1994*	*1993*	*Compound Annual Growth Rate*
OPERATING RESULTS				
Revenues	$ 236,020	$222,561	$214,565	4.9 %
Operating income before property transactions	101,648	91,762	64,758	25.3 %
Operating income	103,590	92,388	66,103	25.2 %
Income before income taxes and extraordinary items	75,579	63,117	30,795	56.7 %
Net income	46,579	36,319	16,926	65.9 %
EBITDA (a)	118,227	104,644	77,281	23.7 %
FINANCIAL POSITION				
Total assets	$ 519,809	$413,308	$438,016	8.9 %
Current portion of long-term debt	278	533	1,052	(48.6)%
Long-term debt (b)	229,479	188,725	172,326	15.4 %
Total equity	167,367	143,008	180,522	(3.7)%
CASH FLOWS				
Provided by (used in)				
Operating activities	$ 79,035	$ 58,287	$ 54,168	
Investing activities	(104,037)	1,471	(720)	
Financing activities				
Advances from (to) Parent	14,840	(60,975)	(51,367)	
Other	10,609	(219)	(667)	
Capital expenditures	115,714	18,379	20,885	
FINANCIAL PERCENTAGES AND RATIOS				
Operating margin before property transactions	43.1%	41.2%	30.2%	
Operating margin	43.9%	41.5%	30.8%	
Return on revenues	18.5%	16.3%	7.9%	
Return on average invested capital	14.5%	13.7%	8.0%	
Return on average equity	28.2%	22.5%	8.6%	
Ratio of earnings to fixed charges	3.2	3.0	1.9	
Current ratio	0.4	0.7	0.5	
Ratio of book equity to total debt	0.7	0.8	1.0	
Ratio of market equity to total debt	5.0	–	–	
Ratio of EBITDA to interest paid	6.8	6.1	4.1	
Ratio of debt to EBITDA	1.9	1.8	2.2	

(a) EBITDA, consisting of income before extraordinary items plus interest, taxes, depreciation, amortization and net earnings of, or distributions from, nonconsolidated affiliates, is a supplemental financial measurement used by management, as well as by industry analysts, to evaluate Promus Hotel Corporation's operations. However, EBITDA should not be construed as an alternative to operating income (as an indicator of operating performance) or to cash flows from operating activities (as a measure of liquidity) as determined in accordance with generally accepted accounting principles.

(b) Includes debt allocated to Promus Hotel Corporation by its Parent for periods prior to the Spin-Off.

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COMPANY MILESTONES

PROMUS HOTEL CORPORATION ● June 20—CEO Ray Schultz and COO David Sullivan visit the New York Stock Exchange for the first trade of company stock under the symbol PRH. ● June 30—Promus Hotel Corporation is launched with the completion of the spin-off from The Promus Companies Incorporated. ● November 7—CEO Ray Schultz announces a corporate donation of $500,000 to fund creation of the Challenger Learning Center of Memphis at Christian Brothers University. Attending the ceremony is June Scobee Rodgers, founder of the national program and widow of Challenger 7 Commander Dick Scobee. The program honors the memory of the Challenger 7 space shuttle crew by promoting space science education. ● December 11—*Fortune* reports that Promus Hotel Corporation received the number one ranking in the hotel industry in the American Customer Satisfaction Index, a joint study of the University of Michigan School of Business and the American Society for Quality Control.

EMBASSY SUITES ● September 22—FelCor Suite Hotels, Inc., of Irving, Tex., announces the acquisition of the Crown Sterling Suites hotel chain, along with its intention to convert the properties to Embassy Suites hotels. As a result of the transaction, which includes an investment by Promus Hotels in a FelCor equity offering, 16 Crown Sterling Suites hotels are slated to join the Embassy Suites system by mid-1996. ● December 1—The first Promus Hotels property in South America, an Embassy Suites hotel, begins operations in Bogota, Colombia. This international location joins other Promus hotels in Canada, Mexico and Costa Rica.

HAMPTON INN ● September 8—The 500th Hampton Inn hotel, a 121-room property, opens in Wichita, Kan. ● October 1—The largest Hampton Inn hotel, with 408 rooms and 26 stories, opens in Reno, Nev. It is located adjacent to Harrah's casino, with a walkway into the Harrah's property.

HOMEWOOD SUITES ● September 22—Promus Hotels opens a company owned Homewood Suites hotel in the Clear Lake area of Houston, Tex., near NASA headquarters.

HAMPTON INN & SUITES ● June 6—The first Hampton Inn & Suites hotel debuts in Newport News, Va. This franchised property features a blend of Hampton Inn-style rooms and Homewood Suites residential-style suites to provide optimum comfort for both business and leisure travelers.

Raymond E. Schultz   Michael D. Rose

Dear Shareholders:

In 1995, Promus Hotel Corporation opened its doors as a new public company listed on the New York Stock Exchange. Although we're a new entity, our roots in the lodging industry are steeped in a rich heritage.

We continue a great tradition of *People Pledged to Excellence*, delivering to our hotel guests and to you, our shareholders, the same strong performance we produced as part of our predecessor company, The Promus Companies Incorporated.

Every day, at almost 700 hotels, thousands of guests enter our doors for a stay that we guarantee will be satisfying. Our unconditional 100% Satisfaction Guarantee, the first of its kind in our industry, is the cornerstone of our culture and our operations. We offer this assurance to our guests because of our confidence in our employees, products and the franchisees, who are our business partners.

This commitment to product quality, product consistency and service excellence has paid off handsomely. This year we enjoyed a superb performance, earning $46.6 million in net income or $0.90 per share for the year, a 28 percent increase over 1994 results. On a pro forma basis, as if we had operated as a stand-alone public company for both 1994 and 1995, net income before extraordinary items and property transactions increased 31.5 percent, from $32.0 million in 1994 to $42.1 million in 1995. In addition, pro forma operating margin before property transactions grew from 37.3 percent in 1994 to 41.7 percent in 1995. The 1995 return on average equity was 28.2 percent.

A critical element in that performance has been record unit growth in our franchising operations. Demand for our hotel brands is greater than ever, with 105 new hotels opened in 1995 and another 292 in the development pipeline, either in design or under construction at year's end.

Our Hampton Inn brand alone accounted for about 15 percent of all new hotel rooms opened nationally in 1995. On average, we opened a new Hampton Inn hotel every four days. We plan to increase the number of new hotel openings in all of our brands combined in 1996 and 1997 over our 1995 record.

For our newer brands, this level of development will provide the critical mass needed to enhance their attractiveness as a franchise product and deliver strong financial performance to franchisees. Homewood Suites expects to reach more than 60 hotels by the end of 1997, double the number with which we began 1995. For the Hampton Inn & Suites brand introduced in mid-year, we expect to have about 40 hotels open by the end of 1997.

We operate in an industry that is enjoying a strong revival after a significant downturn in the late 1980's and early 1990's. We have worthy competitors, many of whom are trying to emulate the success we have enjoyed with our innovative brands.

To continue as the leader we have become, we know we have to work hard to win our customers every stay, every day.

We believe there are three key reasons why Promus Hotel Corporation will continue to perform well in a competitive environment:

1. We have exciting, value-based products that are designed to provide maximum value and satisfaction for our guests while generating higher operating margins for our owners;
2. We have strong franchise demand for our brands in critical industry segments that are growing. And, we continue to attract the highest quality franchisees as our development partners;
3. We have a proven senior management team with a record of innovation and leadership that is unmatched in the industry—and a wealth of talent both at our hotels and in our Memphis headquarters.

For our guests, we open the doors to our hotels and create a homelike feeling. Almost 10,000 Promus Hotels employees, along with our franchisees, will continue to deliver on our promise — high-quality accommodations, friendly and efficient service, and clean, comfortable surroundings.

For shareholders, the management team will build on the strong financial performance and record franchise growth that made 1995 such a success. The confidence you have placed in us is foremost in our minds.

We thank our franchisees for sharing our commitment to product quality, product consistency and service excellence. Together we have set unmatched standards for the lodging industry. Promus Hotels' ranking as the number one hotel company in the American Customer Satisfaction Index by the University of Michigan School of Business and the American Society for Quality Control clearly underscores that performance.

Finally, we salute and thank our employees for their dedication and commitment to excellence that have made Promus Hotels and each of our brands synonymous with superior quality and service. Management is proud that our people know and understand both hotel operations and franchising. We are lodging people. We live the business every day.

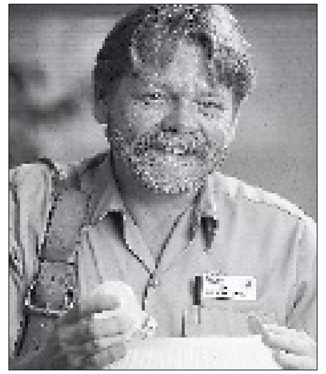
Michael D. Rose, Chairman

Raymond E. Schultz, President and Chief Executive Officer

March 15, 1996

CONCEPT & REALITY It began as a concept. Why not build a hotel that provides only those facilities that guests truly want and will pay for? By eliminating large meeting areas, restaurants, lounges and other amenities used by only a fraction of guests, we created a hotel that meets guests' needs at a price that provides exceptional value. For a single price, we offer guests not only a clean, comfortable room, but also a free continental breakfast, free local phone calls and a free in-room movie channel. The reality that is now Hampton Inn has become one of the fastest-growing hotel chains in industry history. On September 8, 1995, the 500th Hampton Inn opened in Wichita, Kansas, just 11 years after the first one opened its doors in Memphis, Tennessee.

And like all Hampton Inn hotels, the Wichita location backs its quality and consistency with our unconditional 100% Satisfaction Guarantee. If you're not completely satisfied, we don't expect you to pay.

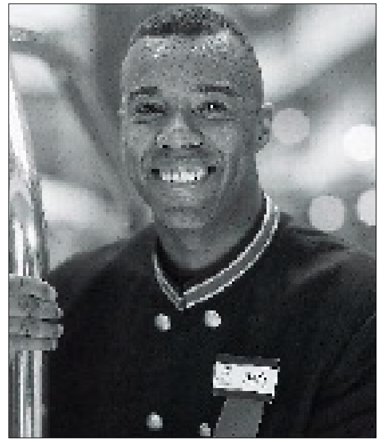


Hampton Inn has achieved a rare level of success in an industry that sees competitors come and go. Franchisees embrace it as the franchise of choice in the mid-scale and upper-economy market segments. In an industry where financing remains difficult, lenders show a clear preference for Hampton Inn projects—another attraction for potential franchisees. Hampton Inn has solidified its position as the brand of choice and the standard our competitors must try to match.

It comes down to performance. Guests appreciate the way Hampton Inn employees provide high-quality accommodations, friendly and efficient service and clean, comfortable surroundings—with satisfaction guaranteed.

In 1995, Hampton Inn opened one new hotel every four days.

THE UNDISPUTED LEADER In just a decade, the Embassy Suites hotel chain has become the undisputed leader in the upscale all-suite hotel market segment, competing very effectively with other suite and upscale full-service hotels as well.

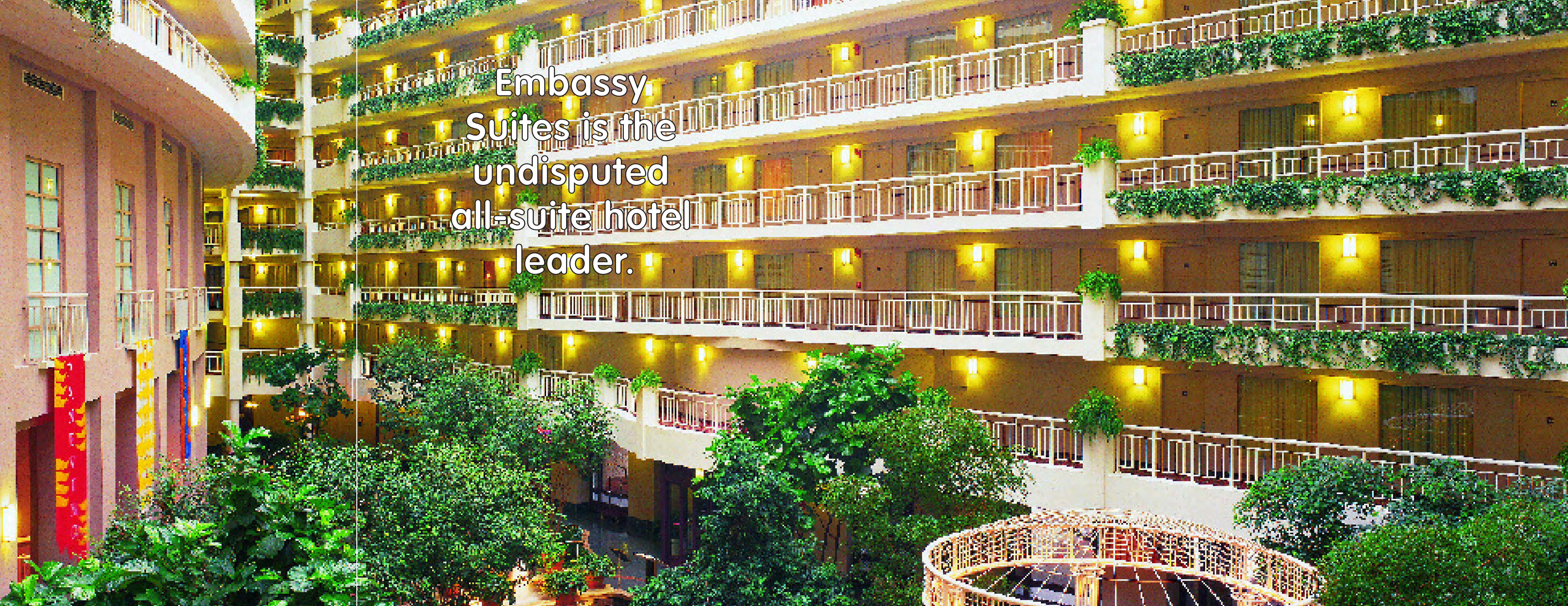


Embassy Suites hotels offer the comfort of a two-room suite for the price of a comparable single hotel room and include a free cooked-to-order breakfast and complimentary evening beverages as part of the value. In a market segment where development has been hampered by a lack of financing, Embassy Suites has experienced exceptional growth. FelCor Suites Hotels, Inc., a leading real estate investment trust (REIT), acquired the Crown Sterling Suites hotel chain and announced that 16 of its hotels will be converted to Embassy Suites. This growth alone will increase the size of the Embassy Suites system by 15 percent

in 1996. The Embassy Suites concept is beginning to attract international attention as well. In 1995, Promus Hotels opened a new Embassy Suites hotel in Bogota, Colombia, its first location in South America. Other Embassy Suites projects are under way in Thailand, Mexico, Chile and Venezuela.

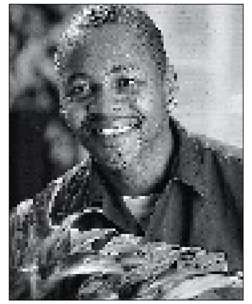
As Embassy Suites grows, so does customer awareness and the room nights booked through our central reservations system. A new 1996 advertising campaign will build even greater recognition. Embassy Suites' superior product offering and its brand-name strength provide value to guests and, in turn, to investors who enjoy revenue and operating premiums over other upscale hotel chains.

For business and leisure travelers, as well as our franchisees, Embassy Suites remains "Twice the Hotel."


Embassy Suites is the undisputed all-suite hotel leader.

A HOTEL LIKE HOME Due to the overwhelmingly positive guest response to the product concept and the proven financial performance, Promus Hotel Corporation decided to devote more resources to growing its extended-stay, residential-style hotel, Homewood Suites. Through an aggressive development plan, the company intends to double the number of Homewood Suites by the end of 1997, with the brand reaching more than 60 properties. Among the new markets that Homewood Suites will enter in 1996 are: Buffalo, Kansas City, Philadelphia, Phoenix, Portland, Salt Lake City, San Antonio and Washington, D.C. Included in the overall brand development during the next two years are hotels that will be developed and operated by Promus Hotels, in addition to strong franchise growth that takes advantage of the brand's solid financial performance.

Homewood Suites hotels offer one- and two-bedroom suites with fully-equipped kitchens and separate living and sleeping areas. The dining area doubles as a workspace, with computer and phone jacks in each suite. Guests enjoy a free breakfast in the central lodge area, social hours on weekdays with a variety of complimentary food and drink, an executive business center, exercise facilities and an on-site convenience store.



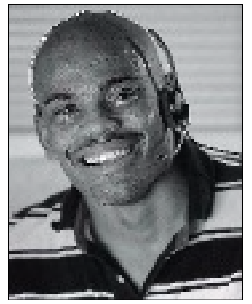
Appealing to both transient and extended-stay travelers with its homelike atmosphere, Homewood Suites hotels produce among the highest guest-satisfaction ratings in the industry and equally strong operating margins for their owners. First-time guests at Homewood Suites come away from their stay knowing that we have created a totally unique lodging experience. And knowing that with their next stay, they'll be "coming home."

Homewood Suites is an industry leader in guest satisfaction.

A FLEXIBLE ALTERNATIVE With the debut of Hampton Inn & Suites in June 1995, Promus Hotels unveiled a new brand concept—a hotel that would offer travelers the choice between a Hampton Inn-style room and the residential-style suites available at Homewood Suites hotels. In doing so, Hampton Inn & Suites became the first hotel product to offer such a combination.

By combining these winning concepts, the company has created an overnight franchising success. Five Hampton Inn & Suites hotels opened in 1995, with the first opening in Newport News, Virginia. Other locations included Pigeon Forge, Tennessee; Nashville, Tennessee; Springdale, Arkansas; and El Paso, Texas. At year's end, 35 new projects were in the development pipeline.

Franchisees, as well as guests, appreciate the flexibility of the brand concept. The typical property can range in size



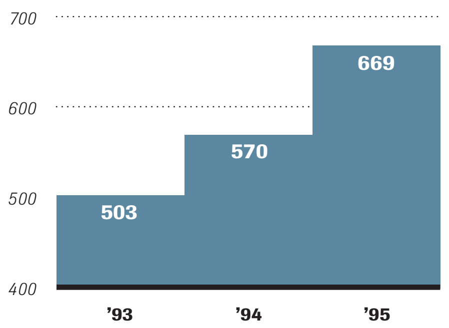
from 60 to 130 rooms, with the mix between rooms and suites running anywhere from a 50-50 ratio to a 75-25 ratio of rooms to suites. Both one- and two-bedroom suites, complete with kitchens, are available.

Like a Hampton Inn hotel, the Hampton Inn & Suites offers guests such amenities as a free continental breakfast, free local phone calls and free in-room movies. Borrowing from the Homewood Suites concept, the new hotel has included the amenities of a convenience shop and a small meeting room. Guests are encouraged to interact in the central lodge area, which is patterned to provide the same relaxed atmosphere found in Homewood Suites hotels. As with the other Promus hotel brands, Hampton Inn & Suites hotels provide the unconditional 100% Satisfaction Guarantee.

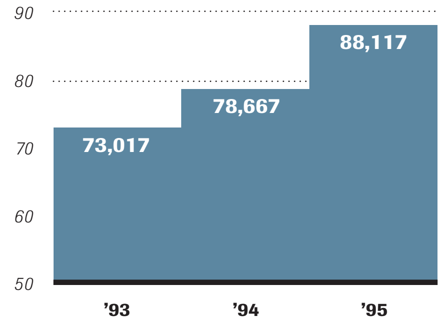
Hampton Inn & Suites debuts an exciting alternative to traditional hotels.

PERFORMANCE STATISTICS

Growth in Number of Hotels



Growth in Number of Hotel Rooms



	Number of Hotels			Compound Annual Growth Rate	Number of Rooms/Suites			Compound Annual Growth Rate
	1995	1994	1993		1995	1994	1993	
Embassy Suites								
Company owned	9	9	9	–	2,025	2,025	2,027	–
Joint venture	23	23	23	–	5,901	5,912	5,913	(0.1)%
Management contract (a)	27	24	23	8.3 %	6,280	6,022	5,835	3.7 %
Franchised	55	51	52	2.8 %	12,529	11,756	12,354	0.7 %
	114	107	107	3.2 %	26,735	25,715	26,129	1.2 %
Hampton Inn								
Company owned	14	15	15	(3.4)%	1,916	2,047	2,048	(3.3)%
Joint venture	19	19	19	–	2,376	2,376	2,376	–
Management contract	4	4	5	(10.6)%	464	464	585	(10.9)%
Franchised (b)	488	399	333	21.1 %	53,531	45,184	39,153	16.9 %
	525	437	372	18.8 %	58,287	50,071	44,162	14.9 %
Homewood Suites								
Company owned	9	8	8	6.1 %	1,024	932	932	4.8 %
Franchised	21	18	16	14.6 %	2,071	1,949	1,794	7.4 %
	30	26	24	11.8 %	3,095	2,881	2,726	6.6 %
Total System								
Company owned	32	32	32	–	4,965	5,004	5,007	(0.4)%
Joint venture	42	42	42	–	8,277	8,288	8,289	(0.1)%
Management contract	31	28	28	5.2 %	6,744	6,486	6,420	2.5 %
Franchised	564	468	401	18.6 %	68,131	58,889	53,301	13.1 %
	669	570	503	15.3 %	88,117	78,667	73,017	9.9 %

(a) Excludes four Crown Sterling Suites properties with 1,076 suites being managed by Promus, but not yet converted to the Embassy Suites brand as of December 31, 1995.

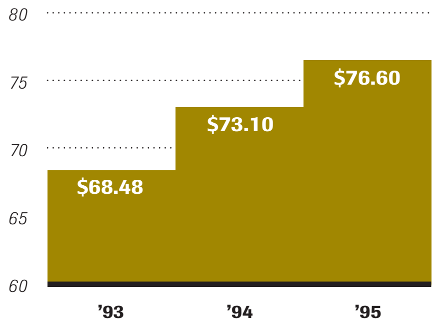
(b) 1995 includes five Hampton Inn & Suites hotels with 573 rooms and suites.

	Comparable System Hotels (a)			Compound Annual Growth Rate	Total System Hotels			Compound Annual Growth Rate
	1995	1994	1993		1995	1994	1993	
Embassy Suites								
Occupancy	74.6%	75.4%	73.8%	0.5%	74.2%	74.9%	73.0%	0.8%
ADR	$102.64	$96.96	$92.78	5.2%	$101.90	$97.28	$93.91	4.2%
RevPAS	76.60	73.10	68.48	5.8%	75.61	72.86	68.58	5.0%
Hampton Inn								
Occupancy	75.3%	75.5%	73.6%	1.1%	73.7%	74.3%	73.0%	0.5%
ADR	$ 56.95	$53.51	$50.92	5.8%	$ 56.97	$53.46	$50.81	5.9%
RevPAR	42.87	40.41	37.47	7.0%	42.01	39.74	37.10	6.4%
Homewood Suites								
Occupancy	78.2%	78.9%	76.6%	1.0%	76.9%	78.1%	75.8%	0.7%
ADR	$ 81.82	$75.92	$73.01	5.9%	$ 82.42	$76.38	$72.47	6.6%
RevPAS	64.01	59.89	55.91	7.0%	63.37	59.67	54.91	7.4%
Hampton Inn & Suites								
Occupancy	–	–	–	–	59.4%	–	–	–
ADR	–	–	–	–	$ 70.13	–	–	–
RevPAS	–	–	–	–	41.65	–	–	–

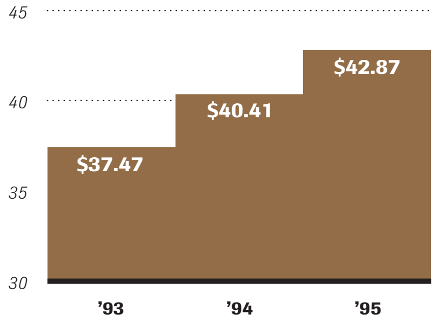
(a) Includes results for only those hotels open for all three years.

(In thousands)	Total System Room Revenues			Compound Annual Growth Rate
	1995	1994	1993	
Hampton Inn	$ 823,247	$ 677,803	$ 565,842	20.6%
Embassy Suites	719,378	687,670	638,115	6.2%
Homewood Suites	68,353	62,080	54,646	11.8%
Hampton Inn & Suites	2,901	–	–	–
	$1,613,879	$1,427,553	$1,258,603	13.2%

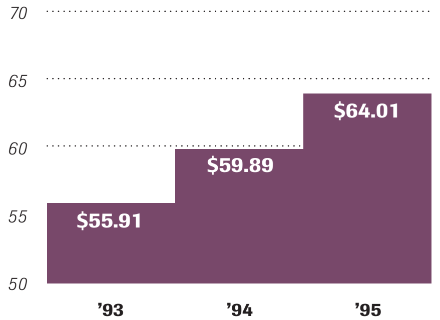
Embassy Suites Comparable RevPAS



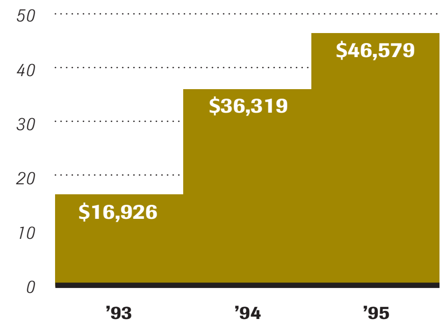
Hampton Inn Comparable RevPAR



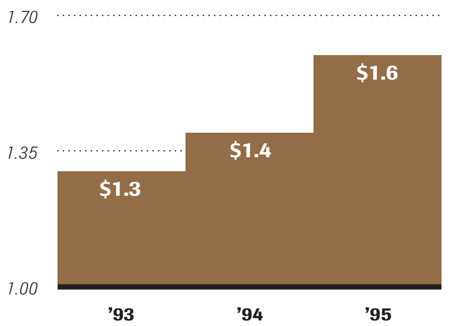
Homewood Suites Comparable RevPAS



Growth in Net Income
(In thousands)



Growth in System Revenues
(In billions)



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

On June 30, 1995, The Promus Companies Incorporated (Parent) completed the transfer of the operations, assets and liabilities of its hotel business (the Hotel Business), composed of three hotel brands targeted at specific market segments: Embassy Suites, Hampton Inn and Homewood Suites, to a new publicly traded entity, Promus Hotel Corporation (Promus or the Company). As approved by Parent's Board of Directors and stockholders on May 26, 1995, this entity was spun-off (the Spin-Off) from the Parent and its stock was distributed to Parent's stockholders on a one-for-two basis effective June 30, 1995 (the Distribution). Concurrent with the Distribution, Parent changed its name to Harrah's Entertainment, Inc. The following is a discussion and analysis of the financial condition and results of operations of Promus as a stand-alone business.

RESULTS OF OPERATIONS

The principal factors affecting Promus' results are: continued growth in the number of hotels; occupancies and room rates achieved by the hotel brands; number and relative mix of owned, managed and franchised hotels; and Promus' ability to manage costs. The number of rooms/suites at franchised and managed properties and revenue per available room/suite (RevPAR/S) significantly affect Promus' results because franchise royalty and management fees are based upon a percentage of rooms/suites revenues. Increases in franchise and management fee revenues have a disproportionate favorable impact on Promus' operating margin due to lower incremental costs associated with these revenues.

As of December 31, 1995, Promus' combined hotel system had grown to 669 properties, resulting in a two-year compound annual growth rate of 15.3%. Total system room revenues have grown to $1.6 billion, which is a two-year compound annual rate of 13.2%. Although comparable system (which includes only those hotels open for all three years) occupancy rates grew at a two-year compound annual rate of approximately 1.0%, increases in the average daily rate (ADR), which contributed to higher RevPAR/S, and the addition of new (primarily franchised) hotels, resulted in significantly improved financial results over the past three years. The continued unit growth of the franchise systems, coupled with a continued focus on rate growth and cost management, were the primary contributors to the Company's higher revenues, margins and operating income.

Actual historical results of operations for all three years were as follows (in millions, except percentages and per share data):

	1995	1994	1993	Percentage Increase/(Decrease) 95 vs 94	94 vs 93
Revenues	$236.0	$222.6	$214.6	6.0%	3.7%
Operating income before property transactions	101.6	91.8	64.8	10.7	41.7
Operating income	103.6	92.4	66.1	12.1	39.8
Net income	46.6	36.3	16.9	28.4	114.8
Operating margin	43.9%	41.5%	30.8%	2.4pts	10.7pts
Earnings per share (a)	$ 0.90	$ 0.70	$ 0.33	28.6%	112.1%
Weighted average shares outstanding (a)	51.6	51.6	51.6	–	–

(a) For purposes of computing earnings per share on a comparable basis, the weighted average shares outstanding for periods prior to the Spin-Off are assumed to be equal to the actual common and common equivalent shares outstanding on June 30, 1995.

Since Promus began operations as a public company on July 1, 1995, comparison of historical results is difficult. The most notable differences between years relate to the incremental stand alone public company costs incurred in the last six months of 1995, and that prior to the Spin-Off, interest was allocated to Promus from Parent at Parent's higher overall borrowing rate. In order to recompute the Company's results of operations on a pro forma basis to achieve better comparability between years, the following adjustments were made (in millions):

	1995	1994	1993
Incremental stand alone public company costs	$(3.2)	$(8.1)	$(8.1)
Net reduction in interest expense	2.2	1.1	1.2
Net revenues and expenses related to the purchase of the corporate office complex	–	0.1	0.1
Decrease in tax provision related to the above adjustments	0.4	2.9	3.1
Total adjustments to net income	$(0.6)	$(4.0)	$(3.7)

Results of operations on a pro forma basis for all three years were as follows (in millions, except percentages and per share data):

	1995	1994	1993	Percentage Increase/(Decrease) 95 vs 94	94 vs 93
Revenues	$236.1	$224.1	$216.1	5.4%	3.7%
Operating income before property transactions	98.4	83.7	56.7	17.6	47.6
Operating income	100.4	84.4	58.1	19.0	45.3
Net income before property transactions and extraordinary items, net of tax	42.1	32.0	12.5	31.6	156.0
Net income	46.0	32.4	13.2	42.0	145.5
Operating margin	42.5%	37.7%	26.9%	4.8pts	10.8pts
Earnings per share	$ 0.89	$ 0.63	$ 0.26	41.3%	142.3%
Weighted average shares outstanding	51.6	51.6	51.6	–	–

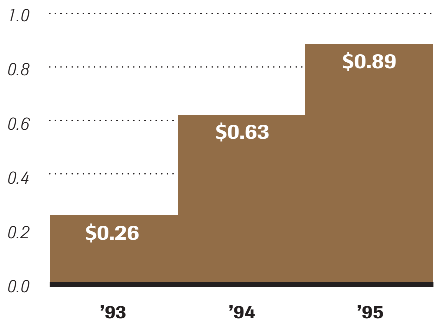
The 1995 increases in operating income and margins are primarily a function of the addition of new franchised hotels, system-wide increases in ADR and cost containment. On a comparable basis, 1995 RevPAR/S increased 4.8%, 6.1% and 6.9% over 1994 at Embassy Suites, Hampton Inn and Homewood Suites hotels, respectively. Company owned hotel revenues for 1995 increased approximately 4.0% or $5.0 million over 1994, while the related operating expenses actually decreased. Excluding the impact of management and franchise terminations and other one-time items, 1995 franchise and management fees increased nearly $9.0 million over 1994, while adding only minimal incremental operating costs.

In 1993, several company owned hotels were sold to a franchisee, contributing to the 1994 decrease in company owned hotel revenues of approximately $11.3 million, and related expenses of approximately $10.0 million. However, the sale of these hotels resulted in an increase in franchise and management fee income, which, along with the addition of other franchise properties, improved operating margins as the increase in operating expenses was not proportionate to the increase in revenues.

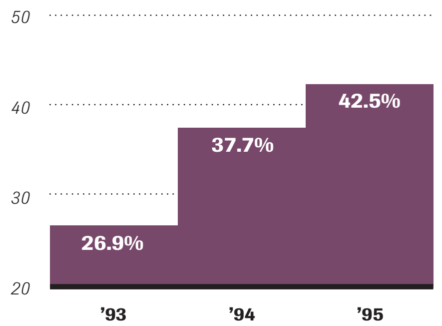
The following comparison of expenses and other items is based on actual historical results (in millions):

	1995	1994	1993	Percentage Increase/(Decrease) 95 vs 94	94 vs 93
Corporate expense	$ 16.7	$ 10.2	$ 13.1	63.7%	(22.1)%
Property transactions	1.9	0.6	1.3	N/M	N/M
Interest expense	(31.1)	(30.8)	(33.1)	1.0	(6.9)
Interest and other income (expense), net	3.1	1.5	(2.2)	N/M	N/M
Extraordinary gains, net of income tax	2.8	–	–	N/M	N/M
Effective tax rate	42.1%	42.5%	45.0%	(0.4)pts	(2.5)pts

Growth in Pro Forma EPS



Growth in Pro Forma Operating Margin



Corporate expense reflects the cost of specific Promus staff functions that support all hotel brands, as well as stand alone public company costs of approximately $5.0 million for the last six months of 1995. The decrease between 1993 and 1994 reflects the 1993 consolidation of all hotel brand management into a single organizational structure.

During 1995, the Company sold a Hampton Inn hotel to a franchisee, which resulted in a pretax property transaction gain of $2.3 million. The property transaction gain recorded in 1994 was primarily the result of the expiration of certain guarantees and contingencies that had caused a portion of prior year's property transaction gains to be deferred, and the sale of a Hampton Inn hotel, both of which were partially offset by the impact of miscellaneous asset write-offs. Property transactions for 1993 included the gain on the sale of an Embassy Suites property. The five other company owned Embassy Suites hotels sold in 1993 referred to herein did not result in the recognition of a property transaction gain or loss.

Interest expense through June 30, 1995 includes the pro rata allocation of corporate interest by Parent related to the debt that was expected to be retired in connection with the Spin-Off using funds drawn on the Company's new $350 million bank credit facility (the Promus Facility), in addition to Promus' share of interest expense attributable to its nonconsolidated affiliates (including joint ventures) and other specific hotel-related debt. 1995 interest expense increased slightly over 1994 due primarily to higher average debt balances and an increase in the interest expense related to deferred compensation balances. This was offset by a decrease attributable to lower actual interest rates obtained under the Promus Facility as compared to Parent's overall borrowing rate used to allocate corporate interest expense before the Spin-Off. The decrease in interest expense between 1994 and 1993 was due largely to the transfer of ownership in five Embassy Suites properties to a third party, which included the assumption of mortgage debt on these properties by the third party.

Interest and other income (expense), net for 1995 increased over 1994 due primarily to interest charged on total net advances to the franchise system funds, as well as increased interest income on mezzanine loans to franchisees and dividend income associated with the Company's investments (see Development and Capital Spending). 1993 included a $3.2 million payment related to the settlement of an issue concerning the guarantee of a land lease associated with an Embassy Suites franchised property.

During 1995, two Embassy Suites hotels in which the Company has a 50 percent interest realized extraordinary gains related to the early payoff and forgiveness of a portion of their existing debt. The cash to fund the early debt payoffs was made available through additional capital contributions to the joint ventures of approximately $10 million from each of its partners. Promus' share of these nonconsolidated affiliates' gains, net of applicable income tax expense, was $2.8 million.

The effective tax rate for all periods is higher than the federal statutory rate primarily due to state income taxes.

DEVELOPMENT AND CAPITAL SPENDING

Hotel Development

There were 99 net hotel additions in the Promus hotel system during 1995, 96 of which were franchised properties, compared to 67 in 1994. This development growth is particularly impressive when one considers that, per Smith Travel Research as of December 31, 1995, Promus hotel brands had a 2.6% share of the entire United States room supply, but accounted for an industry leading 16.6% share of new rooms added to the market from ground-up construction during 1995. This growth occurred primarily in the Hampton Inn brand. As of December 31, 1995, 111 properties were under construction, 109 of which will operate under franchise agreements as Promus brands: 70 Hampton Inn hotels; 23 Embassy Suites hotels; 10 Hampton Inn & Suites hotels and six Homewood Suites hotels. These 111 properties will add 14,284 rooms or suites to the Promus hotel system. The Company had 79 properties under construction at the same time last year. In addition, Promus had 181 hotels in the design phase at December 31, 1995.

Promus opened five Hampton Inn & Suites hotels in 1995. Hampton Inn & Suites is the newest Promus hotel brand and combines, in a single hotel, Hampton-style rooms with two-room suites and a common lodge in the center. Of the 181 hotels in the design phase at December 31, 1995, 25 were Hampton Inn & Suites. To encourage system growth, Promus currently plans to spend approximately $110 million to expand the Homewood Suites hotel brand by developing as many as 14 additional company owned properties over the next three to five years. The Company, however, plans to continue its general strategy of growing its systems primarily through franchise and management contracts. As in the past, company owned hotels and new development projects may be sold to franchisees and the proceeds used to fuel additional system growth, develop new concepts or for other corporate purposes.

FelCor Agreements

In May 1995, Promus entered into a Subscription Agreement with FelCor Suite Hotels, Inc. and FelCor Suites Limited Partnership

(FelCor) whereby Promus agreed to purchase up to $25 million in FelCor limited partnership interests to help fund the partnership's acquisition of all-suite upscale hotels to be converted to the Embassy Suites brand. In September 1995, Promus entered into a second agreement with FelCor in connection with FelCor's agreement to acquire the Crown Sterling Suites hotel chain. FelCor plans to convert up to 16 of the Crown Sterling Suites hotels (over 4,000 suites) to the Embassy Suites brand. In consideration, Promus agreed to make up to $50 million available to FelCor for the conversions through investments in FelCor common stock. Hotels converted to the Embassy Suites brand under either of these agreements will operate under 20-year license agreements, and 10-year management contracts will be awarded to Promus.

Subject to some restrictions, the limited partnership interests may be converted to shares of FelCor common stock on a one-for-one basis and the common stock interests may be sold on the open market.

As of December 31, 1995, Promus had funded approximately $30 million of the total $75 million commitment, and had loaned an additional $7.5 million to FelCor, representing one-half of the deposit required for the Crown Sterling Suites acquisition. The total commitment will be reduced by the amount of such loans outstanding. An additional $30 million was funded in January 1996, and the entire commitment is expected to be funded by the end of the first quarter 1996.

In connection with these agreements, Promus also guaranteed a third party loan to FelCor, not to exceed $25 million. As of December 31, 1995, that facility was not yet in place, and therefore no amounts had been drawn.

As of December 31, 1995, FelCor had acquired nine hotels pursuant to both agreements, eight of which Promus managed, although five had not yet been converted to the Embassy Suites brand. On January 3, 1996, an additional nine Crown Sterling Suites properties were acquired, and are in the process of being converted to Embassy Suites hotels. Effective with the January closing, Promus managed all 18 properties and earned related management fees. However, franchise fees will be earned on these properties only after the conversion to the Embassy Suites brand is complete. Acquisition and conversion of all hotels subject to these agreements is expected to be complete by mid-year 1996.

Mezzanine Financing Program

To encourage growth (primarily in the Hampton Inn & Suites and Homewood Suites brands) in light of the lack of available financing for new hotel construction, Promus developed a mezzanine financing program. Under the program Promus provides conservatively underwritten secondary financing to franchisees. A minimum of 20 percent equity is required by the borrower, and the investment must meet certain defined underwriting criteria. The terms of the mezzanine financing must be consistent with the terms of the first mortgage lender, with whom Promus will enter into an inter-creditor agreement. Promus provided $7.9 million in mezzanine loans during 1995, and anticipates providing an additional $19.6 million during 1996. Outstanding loans bear interest at rates ranging from 10.0% to 10.5%.

Other

Ongoing refurbishment of Promus' existing company owned hotel properties to maintain the quality standards set for those properties will continue in 1996 at an estimated annual cost of approximately $11 million. In early 1995, Promus acquired for $21.7 million an office complex in Memphis, Tennessee, which will serve as its future corporate headquarters.

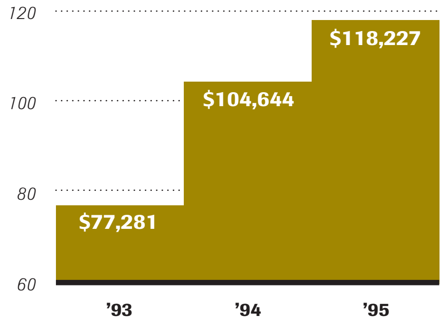
Cash necessary to finance projects currently under development, as well as additional projects to be developed by Promus, will be made available from operating cash flows, the Promus Facility (see "Liquidity and Capital Resources"), joint venture partners, specific project financing, sales of existing hotel assets and, if necessary, Promus debt and equity offerings. Promus' capital expenditures totaled $115.7 million during 1995. The Company expects to spend between $140 million and $160 million during 1996 to fund project development, including those projects discussed above, as well as to refurbish existing facilities and for other corporate related projects.

LIQUIDITY AND CAPITAL RESOURCES

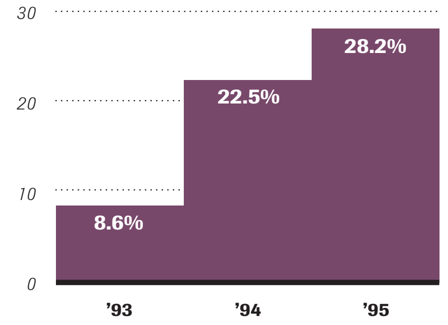
The accompanying financial statements represent the portion of Parent's historical revenues, expenses, assets, liabilities and cash flows associated with the Hotel Business through June 30, 1995, and actual results as a stand-alone company beginning July 1, 1995. The year to date results of operations and cash flows are not necessarily indicative of Promus' future results as a separate corporation. The most significant items that will affect liquidity and capital resources as a result of the Spin-Off are incremental costs associated with operating as a stand-alone company, a decrease in the Company's average borrowing rate, and Promus' payment of state and federal income taxes subsequent to the Distribution (Parent historically paid Promus' taxes).

Cash flows from operating activities for the year ended December 31, 1995 were $79.0 million, compared with $58.3 million for

Growth in EBITDA
(In thousands)



Growth in Return on Average Equity



the same period last year, representing a 35.5% increase. EBITDA, consisting of income before extraordinary items plus interest, taxes, depreciation, amortization and net earnings of, or distributions from, nonconsolidated affiliates, was $118.2 million for 1995, compared with $104.6 million for the comparable period in 1994, representing a 13% increase. EBITDA is a supplemental financial measurement used by management as well as by industry analysts to evaluate operations, but should not be construed as an alternative to operating income (as an indicator of operating performance) or to cash flows from operating activities (as a measure of liquidity) as determined in accordance with generally accepted accounting principles.

On December 31, 1995, the Company had a working capital deficit of $31.4 million, which resulted primarily from Promus' cash management program that calls for the Company to pay down amounts outstanding under the Promus Facility with any excess cash. Therefore, the Company does not believe that the current ratio is an appropriate measure of its short-term liquidity without considering availability under the Promus Facility.

During 1995, Promus entered into the Promus Facility, which is secured by the stock of certain of its material subsidiaries. The Promus Facility consists of two agreements, the significant terms of which are as follows:

	Total Facility	*Maturity Date*	*Interest Rate*	*Facility Fees*
Five-Year Revolver	$300,000,000	June 30, 2000	Base Rate, as defined, or LIBOR +35 basis points	0.20% of the total facility
Extendible Revolver	$ 50,000,000	June 6, 1996	Base Rate, as defined, or LIBOR +40 basis points	0.15% of the total facility

The Extendible Revolver is a 364-day facility with annual renewals and may be converted into a two-year term loan with equal amortizing payments over such two-year period. Facility fees and interest on Base Rate loans are paid quarterly. The agreements contain a tiered scale for facility fees and the applicable LIBOR spread (current rates for both reflected above) that is based on the more favorable of Promus' current credit rating *(Investment Grade* per Standard & Poor's) or leverage ratio, as defined. They also contain provisions that restrict certain investments, limit the Company's ability to incur additional indebtedness and pay dividends, and require that certain performance ratios be maintained. As of December 31, 1995, Promus was in compliance with all such covenants.

The Five-Year Revolver includes a sublimit for letters of credit of $20 million. At December 31, 1995, approximately $9.5 million in letters of credit were outstanding under this agreement (related primarily to the Company's self-insurance reserves). There was approximately $112 million of availability under the Promus Facility as of December 31, 1995. The remaining borrowing capacity available under the Promus Facility is available for working capital, hotel development and other general corporate purposes.

As of December 31, 1995, Promus was a party to several interest rate swap agreements that bear a total notional amount of $100 million. The effect of the swap agreements was to convert a portion of the Company's variable rate debt under the Promus Facility to a fixed rate. The weighted average effective fixed rate pursuant to the agreements, which expire between July 1997 and March 2000, was approximately 7.7% at the end of the year.

RELATIONSHIP WITH PARENT

For the purpose of governing certain of the ongoing relationships between Promus and Parent after the Distribution and to provide mechanisms for an orderly transition, Parent and Promus have entered into various agreements and adopted policies governing their future relationship. Management believes the agreements are fair to both parties and contain terms comparable to those which would have been reached in arm's-length negotiations with unaffiliated parties (although comparisons are difficult with respect to certain agreements that relate to the specific circumstances of the Distribution).

TAX SHARING AGREEMENT

In connection with the Spin-Off, Promus and Parent entered into a tax sharing agreement that defines each company's rights and obligations with respect to deficiencies and refunds of federal, state and other income or franchise taxes relating to Promus' business for tax years prior to the Distribution and with respect to certain tax attributes of Promus after the Distribution. In general, with respect to periods ending on or before December 31, 1995, Parent is responsible for (i) filing federal tax returns for Parent and Promus for the periods such companies were members of the same consolidated group, and (ii) paying the taxes relating to such returns (to include any subsequent adjustments resulting from the redetermination of such tax liabilities by the applicable taxing authorities; Promus will reimburse Parent for the portion of such adjustments relating to the Hotel Business). Promus is responsible for filing returns and paying taxes for periods beginning after the Spin-Off.

EFFECTS OF INFLATION AND CURRENT ECONOMIC CONDITION

Generally, Promus has not experienced any significant negative effect on its hotels and food and beverage operations because of inflation. To date, Promus has been able to increase rates and prices and thereby pass on the effects of inflationary cost increases. Although competitive conditions may limit the industry's future ability to raise room rates at the rate of inflation, management believes that each of its hotel brands has rate growth potential in excess of the inflation rate. Promus will continue to emphasize cost containment and productivity improvement programs. Inflation tends to increase the underlying value of Promus' real estate, and management and franchise contracts.

Although significant growth in the general economy is not expected for 1996, moderate but stable growth is anticipated in the hotel industry, as demand is increasing at a greater rate than supply. Promus hotel brands lead the industry in the percentage of guests who intend to make return visits, and in guest satisfaction, due largely to the 100% Satisfaction Guarantee offered unconditionally throughout the entire Promus hotel system.

ADOPTION OF NEWLY ISSUED ACCOUNTING PRONOUNCEMENT

Effective for fiscal year 1996, Promus will adopt Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation." Management intends to adopt the disclosure-only option provided for by this pronouncement.

CONSOLIDATED BALANCE SHEETS

As of December 31

(In thousands, except share amounts)

	1995	1994
ASSETS		
Current assets		
Cash and cash equivalents	$ 2,668	$ 2,221
Receivables, including notes receivable of $497 and $53, less allowance for doubtful accounts of $1,172 and $855	14,837	12,065
Deferred income taxes (Note 6)	3,492	2,844
Prepayments and other (Note 3)	2,429	1,642
Total current assets	23,426	18,772
Land, buildings, furniture and equipment		
Land	61,651	60,025
Buildings and improvements	264,961	237,044
Furniture, fixtures and equipment	110,275	86,042
	436,887	383,111
Less: accumulated depreciation	(104,993)	(81,368)
	331,894	301,743
Investments in and advances to nonconsolidated affiliates (Note 11)	90,506	35,731
Investment in franchise system (Note 2)	31,652	28,718
Deferred costs and other	42,331	28,344
	$ 519,809	$413,308

	1995	1994
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	$ 18,202	$ 11,124
Accrued expenses (Note 3)	36,371	16,887
Current portion of long-term debt (Note 4)	278	533
Total current liabilities	54,851	28,544
Long-term debt (Note 4)	229,479	188,725
Deferred credits and other	36,282	28,527
Deferred income taxes (Note 6)	31,830	24,504
	352,442	270,300
Commitments and contingencies (Notes 5 through 7)		
Stockholders' equity (Note 9)		
Common stock, $0.10 par value, 360,000,000 shares authorized, 51,371,152 shares outstanding, net of 2,626 shares held in treasury	5,137	–
Capital surplus	136,057	–
Retained earnings	25,349	–
Unrealized gain on marketable equity securities, net of related deferred tax liability of $1,165	1,822	–
Deferred compensation related to restricted stock	(998)	–
Parent company investment	–	143,008
	167,367	143,008
	$519,809	$413,308

The accompanying notes are an integral part of these consolidated balance sheets.

CONSOLIDATED STATEMENTS OF INCOME

For the years ended December 31

(In thousands)	1995	1994	1993
Revenues			
Company owned hotels			
Rooms	$116,094	$110,205	$121,104
Food and beverage	7,180	8,001	8,094
Other	6,805	6,879	7,207
Franchise and management fees	79,935	76,874	60,359
Other	26,006	20,602	17,801
Total revenues	236,020	222,561	214,565
Operating expenses			
Company owned hotels			
Rooms	56,228	56,952	65,529
Food and beverage	6,832	7,760	8,235
Other	12,946	12,547	13,488
Other operating expenses	20,110	24,434	29,419
Depreciation of buildings and equipment	21,582	18,929	20,069
Corporate expense	16,674	10,177	13,067
Total operating expenses	134,372	130,799	149,807
Operating income before property transactions	101,648	91,762	64,758
Property transactions	1,942	626	1,345
Operating income	103,590	92,388	66,103
Interest expense, net of interest capitalized (Note 4)	(31,138)	(30,759)	(33,061)
Interest and other income (expense), net	3,127	1,488	(2,247)
Income before income taxes and extraordinary items	75,579	63,117	30,795
Provision for income taxes (Note 6)	(31,819)	(26,798)	(13,869)
Income before extraordinary items	43,760	36,319	16,926
Extraordinary items, net of income tax of $1,635 (Note 10)	2,819	–	–
Net income	$ 46,579	$ 36,319	$ 16,926

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

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

For the years ended December 31

(Notes 1 and 9)

(In thousands)	*Common Stock* Shares	*Common Stock* Amount	*Capital Surplus*	*Retained Earnings*	*Unrealized Gain on Marketable Equity Securities*	*Deferred Compensation Related to Restricted Stock (Note 8)*	*Parent Company Investment*	*Total*
Balance—December 31, 1992	–	$ –	$ –	$ –	$ –	$ –	$ 212,229	$212,229
Net income	–	–	–	–	–	–	16,926	16,926
Intercompany activity with Parent	–	–	–	–	–	–	(48,633)	(48,633)
Balance—December 31, 1993	–	–	–	–	–	–	180,522	180,522
Net income	–	–	–	–	–	–	36,319	36,319
Intercompany activity with Parent	–	–	–	–	–	–	(73,833)	(73,833)
Balance—December 31, 1994	–	–	–	–	–	–	143,008	143,008
Net income—January 1, 1995 through June 30, 1995	–	–	–	–	–	–	21,230	21,230
Intercompany activity with Parent—January 1, 1995 through June 30, 1995	–	–	–	–	–	–	(24,656)	(24,656)
Spin-Off of the Company	51,352	5,135	135,801	–	–	(1,354)	(139,582)	–
Shares issued under incentive compensation plan	8	1	174	–	–	(175)	–	–
Balance—June 30, 1995	51,360	5,136	135,975	–	–	(1,529)	–	139,582
Net income—July 1, 1995 through December 31, 1995	–	–	–	25,349	–	–	–	25,349
Net shares issued under incentive compensation plans, including income tax benefit of $97	11	1	82	–	–	531	–	614
Unrealized gain on marketable equity securities, net of deferred income tax liability of $1,165	–	–	–	–	1,822	–	–	1,822
Balance—December 31, 1995	51,371	$5,137	$136,057	$25,349	$1,822	$ (998)	$ –	$167,367

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the years ended December 31

(Note 12)

(In thousands)	*1995*	*1994*	*1993*
Cash flows from operating activities			
Net income	$ 46,579	$ 36,319	$ 16,926
Adjustments to reconcile net income to cash flows from operating activities			
Extraordinary items	(4,454)	–	–
Depreciation and amortization	25,263	21,326	25,028
Other noncash items	(2,217)	(2,762)	3,382
Equity in earnings, net of distributions from, nonconsolidated affiliates	(61)	2,969	2,819
Net gains from property transactions	(2,159)	(280)	(1,677)
Net change in long-term accounts	2,089	5,637	2,868
Net change in working capital accounts	13,995	(4,922)	4,822
Cash flows provided by operating activities	79,035	58,287	54,168
Cash flows from investing activities			
Land, buildings, furniture and equipment additions	(55,872)	(13,626)	(12,801)
Investments in and advances to nonconsolidated affiliates	(47,832)	(1,657)	32
Advances under mezzanine loan agreements	(7,899)	(1,000)	(1,545)
Proceeds from property transactions	7,843	19,164	16,921
Net investments in franchise system	(4,111)	(2,096)	(6,571)
Recovery of investment in franchise system	3,049	3,407	2,892
Other	785	(2,721)	352
Cash flows (used in) provided by investing activities	(104,037)	1,471	(720)
Cash flows from financing activities			
Net borrowings under revolving credit facility	10,600	–	–
Debt retirements	(284)	(219)	(667)
Advances from (to) Parent	14,840	(60,975)	(51,367)
Other	293	–	–
Cash flows provided by (used in) financing activities	25,449	(61,194)	(52,034)
Net increase (decrease) in cash and cash equivalents	447	(1,436)	1,414
Cash and cash equivalents, beginning of period	2,221	3,657	2,243
Cash and cash equivalents, end of period	$ 2,668	$ 2,221	$ 3,657

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 1995

NOTE 1—BASIS OF PRESENTATION AND ORGANIZATION

On June 30, 1995, The Promus Companies Incorporated (Parent) completed the transfer of the operations, assets and liabilities of its hotel business (the Hotel Business), composed of three hotel brands targeted at specific market segments: Embassy Suites, Hampton Inn and Homewood Suites, to a new publicly traded entity, Promus Hotel Corporation (Promus or the Company). As approved by Parent's Board of Directors and stockholders on May 26, 1995, this entity was spun-off (the Spin-Off) from the Parent and its stock was distributed to Parent's stockholders on a one-for-two basis effective June 30, 1995 (the Distribution). Concurrent with the Distribution, Parent changed its name to Harrah's Entertainment, Inc.

NOTE 2—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Operations

Promus operates the Embassy Suites, Hampton Inn, Homewood Suites and Hampton Inn & Suites hotel brands primarily through three lines of business: franchise; hotel operations, including management contracts; and hotel real estate and joint venture investments. Embassy Suites is a full-service hotel brand that management believes comprises the largest all-suite upscale hotel system in the United States by number of suites and system revenue. Hampton Inn is a limited-facility hotel and Homewood Suites offers residential-style accommodations designed for the extended stay traveler. Hampton Inn & Suites is the newest Promus hotel brand and combines, in a single hotel, Hampton-style rooms with two-room suites and a common lodge in the center.

Promus' primary focus is to develop, grow and support its franchise business for all brands. Promus hotel brands are located in virtually every state, the District of Columbia and four foreign countries. Promus charges each franchisee royalty fees of generally four percent of suite or room rentals. Royalty fees for 1995, 1994 and 1993 were based on system-wide reported room revenues of $1.6 billion, $1.4 billion and $1.3 billion, respectively. In addition, Promus earns a licensing fee for new licenses granted to franchisees when the franchise is approved.

Promus operates more than 100 Promus-brand hotels. Company operated properties include wholly-owned, partially owned through joint ventures and hotels managed for third parties. Promus has followed an asset strategy to own and manage a mix of Promus hotel brands that can impact profits and enhance its role as franchisor for the respective brands. Management fee income is based on a percentage of gross revenues, profits, or both at the related managed property.

Principles of Consolidation

The accompanying consolidated financial statements include the assets, liabilities, revenues, expenses and cash flows of Parent's Hotel Business on a stand-alone basis for 1993 and 1994, and through the six months ended June 30, 1995, as well as actual results of the Company for the six months ended December 31, 1995. The preparation of these financial statements required the use of certain estimates by management in determining the Company's assets, liabilities, revenues and expenses.

All significant intercompany accounts and transactions have been eliminated. Investments in 50% or less owned companies and joint ventures over which Promus has the ability to exercise significant influence are accounted for using the equity method. Promus reflects its share of income before interest expense and extraordinary gain of these nonconsolidated affiliates in revenues–other. Promus' proportionate share of interest expense and extraordinary gain on forgiveness of debt of such nonconsolidated affiliates is included in interest expense and extraordinary items, respectively, in the consolidated statements of income (see Note 11 for combined summarized financial information regarding these nonconsolidated affiliates). Management believes Promus' inclusion of its proportionate share of the interest expense of its equity investees in interest expense is the preferable presentation due to the nature of its equity investments.

Cash Equivalents

Cash equivalents are highly liquid investments with a maturity of less than three months and are stated at the lesser of cost or market.

Land, Buildings, Furniture and Equipment

Land, buildings, furniture and equipment are stated at cost. Land includes land held for future development or disposition, which totaled $9.6 million at December 31, 1995 and 1994. Improvements and extraordinary repairs that extend the life of the asset are capitalized. Maintenance and repairs are expensed as incurred. Construction in progress, which is reflected in buildings and improvements in the consolidated balance sheets, was $20.2 million and $3.1 million at December 31, 1995 and 1994, respectively.

Interest expense is capitalized on constructed assets at Promus' overall weighted average borrowing rate. The Company capitalized interest of $1.4 million in 1995, due largely to the acquisition of the corporate office complex that is still under construction. No material amounts of capitalized interest were recorded during 1994 or 1993.

Depreciation of buildings, furniture and equipment are calculated using the straight-line method over the estimated useful life of the assets or over the related lease term, as follows:

Buildings and improvements	10 to 40 years
Furniture, fixtures and equipment	2 to 15 years

Investment in Franchise System

Promus' investment in franchise system includes the necessary computer systems to operate the centralized marketing and reservation center, and a property management system that interacts with several operational software packages which are available to each franchised hotel. These costs are reimbursed from the respective brand system fund over their estimated useful lives. Generally, the owner of each hotel, including Promus' company owned hotels, contributes 3.5 to 4.0 percent of suite or room revenues to its brand's fund.

Revenue Recognition

Room revenue represents revenue derived from the rental of rooms and suites for hotels majority owned by Promus. Food and beverage revenues represent revenues from company owned restaurants and lounges.

Amortization

Deferred management and franchise contract costs are amortized on a straight-line basis over the term of the related contract, generally 10 to 20 years. Deferred finance charges are amortized over the term of the related debt (see Note 4).

Property Transactions

Property transactions include gains and losses from asset sales, including sales of joint venture equity interests, write-downs of assets to net realizable value and the ongoing costs of Promus' asset management staff. The operations of properties sold are included in the financial statements through the date of sale.

Reclassifications

Certain amounts for prior years have been reclassified to conform with the presentation for 1995.

NOTE 3—DETAIL OF CERTAIN BALANCE SHEET ACCOUNTS

Prepayments and other consisted of the following (in thousands):

	1995	1994
Prepayments	$1,557	$ 425
Supplies	206	237
Other current assets	666	980
	$2,429	$1,642

Accrued expenses consisted of the following (in thousands):

	1995	1994
Self-insurance reserves	$ 8,934	$ —
Payroll and other compensation	7,424	5,985
Deposits and customer funds	4,794	2,461
Income taxes	4,290	106
Taxes, other than income taxes	3,658	3,690
Other	7,271	4,645
	$36,371	$16,887

NOTE 4—LONG-TERM DEBT

Parent Debt Allocation

The Company's financial position at December 31, 1994, and its results of operations through June 30, 1995, reflect all indebtedness, together with related interest expense, specifically identified with Promus entities, as well as a pro rata portion of Parent's historical corporate debt balance, unamortized deferred finance charges and interest expense. Allocations of those amounts to Promus from Parent were based on the percentage of Parent's historical corporate debt that was expected to be retired using proceeds from Promus' new $350 million bank credit facility (the Promus Facility). The accompanying consolidated balance sheet as of December 31, 1994 reflects corporate debt allocated to Promus from Parent of $187.9 million, together with debt specifically associated with Promus entities of $1.4 million, as well as the unamortized deferred finance charges allocated to Promus of $3.2 million. Parent's corporate interest expense, including amortization of deferred finance costs, allocated to Promus was $17.2 million and $17.0 million, for 1994 and 1993, respectively, and $10.5 million for 1995 (which represents interest allocated from Parent before the Spin-Off).

New Bank Facility

The Promus Facility consists of a $300 million revolving credit arrangement with a maturity of five years (the Five-Year Revolver) and a $50 million annually extendible revolving credit facility with an initial maturity of 364 days (the Extendible Revolver). The Extendible Revolver is convertible into a two-year term loan with equal amortizing payments over such two-year period. Interest on the drawn portion of the Promus Facility is, at the option of the Company, equal to either (i) the Base Rate, as defined, or (ii) LIBOR plus the applicable spread, which was approximately 7.7% (including the LIBOR spread, facility fees and the impact of interest rate swaps) on a weighted average basis for the last six months of 1995. Both agreements incorporate a tiered scale that defines the applicable LIBOR spread and a facility fee based upon the more favorable of the Company's current debt rating or leverage ratio, as defined. Currently, the LIBOR spread on the Five-Year Revolver and the Extendible Revolver is 0.35% and 0.40%, respectively, and the facility fee required on the total amount of the Five-Year Revolver and the Extendible Revolver is 0.20% and 0.15%, respectively. The Promus Facility is secured by the stock of Promus' material subsidiaries and contains provisions that restrict certain investments, limit the Company's ability to incur additional indebtedness and pay dividends, and require that certain performance ratios be maintained. As of December 31, 1995, Promus was in compliance with all such covenants.

The Five-Year Revolver also provides a sublimit for letters of credit of $20 million. At December 31, 1995, approximately $9.5 million in letters of credit were outstanding under this agreement. As of December 31, Promus' indebtedness consisted of the following (in thousands):

	1995	*1994*
Amounts outstanding under the Promus Facility	$228,600	$ –
Notes payable and other-unsecured, 13%, maturities to 1999	776	976
Mortgages, 8.0%–8.75%, maturities to 2005	271	297
Capital lease obligations, 8.2%–13.4%, maturities to 1999	110	125
Corporate debt allocated by Parent	–	187,860
	229,757	189,258
Current portion of long-term debt	(278)	(533)
	$229,479	$188,725

Aggregate annual maturities of long-term debt subsequent to December 31, 1995 were: 1996, $278,000; 1997, $306,000; 1998, $330,000; 1999, $94,000; 2000, $228,636,000, and $113,000 thereafter.

Interest Rate Agreements

As of December 31, 1995, Promus was a party to several interest rate swap agreements that help the Company manage the relative mix of its debt between fixed and variable rate instruments. These agreements effectively modify the interest characteristics of its outstanding debt without an exchange of the underlying principal amount. Pursuant to the agreements, Promus receives a variable interest rate tied to LIBOR in exchange for its payments at a fixed interest rate. The fixed rates to be paid by Promus are summarized in the following table.

Notional Amount (All Associated with The Promus Facility)	*Swap Rate Paid (Fixed)*	*Effective Rate at December 31*	*Next Quarterly Variable Rate Adjustment Date*	*Swap Maturity*
$50.0 million	6.99%	7.54%	3/20/1996	03/20/2000
$25.0 million	7.86%	8.41%	3/15/1996	07/28/1997
$12.5 million	6.92%	7.47%	3/15/1996	12/15/1998
$12.5 million	6.68%	7.23%	3/15/1996	12/15/1999

The differences to be paid or received under the terms of the interest rate swap agreements described above are accrued as an adjustment to interest expense for the related debt. Changes in the effective interest rates to be paid by Promus pursuant to the terms of its interest rate agreements will have a corresponding effect on its future cash flows. On January 22, 1996, the above-mentioned $25 million swap was amended and effectively split into two separate agreements, each with a notional amount of $12.5 million. The amended swaps have effective rates of 7.29% and 7.07% maturing in January 1999 and 2000, respectively. These agreements contain a credit risk that the counterparties may be unable to meet the terms of the agreements. Promus minimizes that risk by evaluating the creditworthiness of its counterparties, which are limited to major banks and financial institutions, and does not anticipate nonperformance by the counterparties.

Fair Market Value

Because the terms of the Promus Facility provide that borrowings outstanding under those agreements bear interest at current market rates, management believes that the related liabilities reflected in the consolidated balance sheet as of December 31, 1995 approximate fair market value. The fair market value of the Company's other material financial instruments as of December 31, 1995 were as follows (in thousands):

	Carrying Value	*Market Value*
Interest rate swaps (used for hedging purposes)	$55	$(5,056)

The amount reflected as the "carrying value" of the interest rate agreements represents the accrual balance as of the date reported. The "market value" represents the estimated amount, considering the prevailing interest rates, that Promus would pay to terminate the agreement as of the date reported.

NOTE 5—COMMITMENTS AND CONTINGENCIES

Contractual Commitments

Promus is liable under certain lease agreements pursuant to which it has assigned the direct obligation to third party interests. Additionally, Promus manages certain hotels for others under agreements that provide for payments or loans to the hotel owners if stipulated levels of financial performance are not maintained. The Company has also provided guarantees for certain loans related to joint venture investments. Promus believes the likelihood is remote that material payments will be required under these agreements. Promus' estimated maximum exposure under such agreements is approximately $39 million over the next 30 years.

FelCor Agreements

In May 1995, Promus entered into a Subscription Agreement with FelCor Suite Hotels, Inc. and FelCor Suites Limited Partnership (FelCor) whereby Promus agreed to purchase up to $25 million in FelCor limited partnership interests to help fund the partnership's acquisition of all-suite upscale hotels to be converted to the Embassy Suites brand. In September 1995, Promus entered into a second agreement with FelCor in connection with FelCor's agreement to acquire the Crown Sterling Suites hotel chain. FelCor plans to convert up to 16 of the Crown Sterling Suites hotels to the Embassy Suites brand. In consideration, Promus agreed to make up to $50 million available to FelCor for the conversions through investments in FelCor common stock. Hotels converted to the Embassy Suites brand under either of these agreements will operate under 20-year license agreements, and 10-year management contracts will be awarded to Promus.

Subject to some restrictions, the limited partnership interests may be converted to shares of FelCor common stock on a one-for-one basis and the common stock interests may be sold on the open market.

As of December 31, 1995, Promus had funded approximately $30 million of the total $75 million commitment, and had loaned an additional $7.5 million to FelCor, representing one-half of the deposit required for the Crown Sterling Suites acquisition. The total commitment will be reduced by the amount of such loans outstanding. An additional $30 million was funded in January 1996, and the entire commitment is expected to be funded by the end of the first quarter 1996.

In connection with these agreements, Promus will guarantee a third party loan to FelCor, not to exceed $25 million. As of December 31, 1995, that facility was not yet in place, and therefore no amounts had been drawn.

Litigation

The Company is a party to various inquiries, administrative proceedings and litigation relating to contracts, sales of property and other matters arising in the normal course of business. While any proceeding or litigation has an element of uncertainty, management believes that the final outcome of these matters will not have a materially adverse effect upon Promus' consolidated financial position or its results of operations.

Employment and Severance Agreements

Promus has severance agreements with 13 senior officers of the Company that provide for a payment of 2.99 times the average annual cash compensation (salary and bonus) paid to each such executive for the five preceding calendar years, including such compensation paid during service with Parent. The agreements also provide for accelerated payment of any compensation or awards payable to such executive under any Promus incentive compensation or stock option plan in the event of termination of an executive's employment, as described in the agreements, subsequent to a change in control of Promus, as defined. The maximum amount of compensation that would be payable under all agreements if a change in control occurred and if such executives were terminated as of December 31, 1995 would be approximately $16.6 million.

Self-Insurance Reserves

Promus self-insures various levels of general liability, workers' compensation and employee medical coverage. All self-insurance reserves include accruals of estimated settlements for known claims, as well as accruals of actuarial estimates of incurred but not reported claims. These estimates are based on historical information along with certain assumptions about future events. Changes in assumptions for such things as medical costs and legal expenses, as well as changes in actual experience, could cause these estimates to change in the near term.

NOTE 6—INCOME TAXES

Income tax expense attributable to income before income taxes and extraordinary items consisted of the following (in thousands):

	1995	*1994*	*1993*
Current			
Federal	$22,252	$25,396	$12,087
State	2,889	1,154	1,186
Deferred			
Federal	3,004	248	596
State	3,674	–	–
	$31,819	$26,798	$13,869

In addition to taxes provided for income before income taxes and extraordinary items, during 1995 Promus provided $1.6 million for extraordinary items and $1.2 million for unrealized gains on marketable equity securities. The differences between the statutory federal income tax rate and the effective tax rate expressed as a percentage of income before income taxes were as follows:

	1995	*1994*	*1993*
Statutory tax rate	35.0%	35.0%	35.0%
Increases in tax resulting from			
State taxes, net of federal tax benefit	5.6	1.8	3.9
Other	1.5	5.7	6.1
	42.1%	42.5%	45.0%

Components of Promus' net deferred tax liability included in the consolidated balance sheets were as follows (in thousands):

	1995	*1994*
Deferred tax assets		
Deferred income	$ 4,760	$ 4,643
Compensation	4,581	3,623
State income taxes	1,295	–
Bad debt reserve	703	593
Self-insurance reserves	562	–
Other	270	534
	12,171	9,393
Deferred tax liabilities		
Property and equipment	(23,896)	(19,494)
Investments in nonconsolidated affiliates	(14,430)	(8,813)
Franchise system fund prepayments	(1,333)	(2,746)
Basis difference in other assets	(850)	–
	(40,509)	(31,053)
Net deferred tax liability	$(28,338)	$(21,660)

Tax Sharing Agreement

In connection with the Spin-Off, Promus and Parent entered into a tax sharing agreement that defines each company's rights and obligations with respect to deficiencies and refunds of federal, state and other income or franchise taxes relating to Promus' business for tax years prior to the Distribution and with respect to certain tax attributes of Promus after the Distribution. In general, with respect to periods ending on or before December 31, 1995, Parent is responsible for (i) filing federal tax returns for Parent and Promus for the periods such companies were members of the same consolidated group, and (ii) paying taxes relating to such returns (to include any subsequent adjustments resulting from the redetermination of such tax liabilities by the applicable taxing authorities; Promus will reimburse Parent for the portion of such adjustments relating to the Hotel Business). Promus is responsible for filing returns and paying taxes for periods beginning after the Spin-Off.

NOTE 7—LEASES

Promus leases both real estate and equipment used in its operations through operating and capital leases. Leases that transfer substantially all benefits and risks incidental to ownership of the property are capitalized. In addition to minimum rentals, many leases provide for contingent rents based on percentages of revenue. The average remaining term for operating leases, which generally contain renewal options, extends approximately eight years. The costs of leased assets are amortized over periods not in excess of the lease terms.

Rental expense associated with operating leases included in the consolidated statements of income was as follows (in thousands):

	1995	*1994*	*1993*
Noncancelable rental expense			
Minimum	$3,828	$2,400	$2,286
Contingent	852	740	601
Other	863	790	967
	$5,543	$3,930	$3,854

The future minimum rental commitments as of December 31, 1995 were as follows (in thousands):

	Noncancelable Operating Leases
1996	$ 2,187
1997	1,485
1998	1,100
1999	938
2000	878
Thereafter	10,319
	$16,907

Minimum rental commitments exclude contingent rentals, which may be paid under certain leases based on a percentage of revenues in excess of specified amounts.

NOTE 8—EMPLOYEE BENEFIT PLANS

Savings and Retirement Plan

Promus has a defined contribution savings and retirement plan (Promus S&RP) in which participating employees may elect to make pretax and after-tax contributions of up to 16 percent of their eligible earnings, the first six percent of which Promus will match fully. Amounts contributed to the plan are invested, at the participant's option, in a Promus common stock fund, an aggressive stock fund, a diversified stock fund, a long-term bond fund, an income fund and/or a treasury fund. Participants become vested in Promus' matching contributions over seven years of credited service, including any previous credited service under Parent's plan. Promus recognized contribution expense related to the Promus S&RP of $1.4 million in 1995 (which represents expense incurred subsequent to the Spin-Off).

Restricted Stock

Promus has a restricted stock plan (RSP) under which executives and key employees may be awarded shares of Promus common stock. Shares granted under the Promus RSP are restricted as to transfer, are subject to forfeiture prior to vesting and will generally vest evenly over periods from two to four years. The deferred compensation expense is amortized over the vesting period. This expense totaled $0.5 million in 1995 (which represents expense incurred subsequent to the Spin-Off).

Stock Option Plan

Promus has a stock option plan (SOP) under which options may be granted to Promus key management personnel. Promus' SOP allows an option holder to purchase Promus common stock over specified periods of time, generally ten years, at a fixed price equal to the market value at the date of grant. A summary of stock option transactions during 1995 follows:

	Option Price Range (per share)	*Number of Common Shares*	
		Options Outstanding	*Available for Grant*
Balance—June 30, 1995	$ 2.41–$30.70	1,238,839	2,361,161
1995 grants	$22.56–$24.56	711,150	(711,150)
Exercised	$ 2.41–$ 9.62	(13,763)	–
Canceled	$ 9.62–$30.35	(24,171)	24,171
Balance—December 31, 1995	$ 2.41–$30.70	1,912,055	1,674,182
Exercisable at December 31, 1995	$ 2.41–$30.70	262,660	

Effective for fiscal year 1996, Promus will adopt Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation." Management intends to adopt the disclosure-only option provided for by this pronouncement.

Deferred Compensation Plans

Promus has deferred compensation plans under which certain employees may defer a portion of their compensation. Amounts deposited into these plans are unsecured and earn interest at rates approved by the Human Resources Committee of the Board of Directors. In connection with the administration of the executive deferred compensation plan, company owned life insurance policies insuring the lives of certain directors, officers and key employees have been purchased. As of December 31, 1995, the total liability under these plans was $8.4 million, and the related cash surrender value of life insurance policies was $11.3 million.

Stock Incentive Plan

The Company established a Promus 1996 Non-Management Directors Stock Incentive Plan under which (i) directors will automatically receive each February 1, May 1, August 1 and November 1, in lieu of cash payments, shares of Promus common stock based upon one-half of the meeting and retainer fees earned and the fair market value of Promus common stock and (ii) may elect to receive the remaining one-half of compensation due in the form of a cash payment or as Promus common stock. Shares issued under the plan are restricted as to transfer for at least six months after the date of grant. The plan becomes effective as of the date of the 1996 Promus Annual Meeting of Stockholders.

NOTE 9—STOCKHOLDERS' EQUITY

In addition to its common stock, the Company has the following classes of stock authorized but unissued:

Preferred stock, $100 par value, 150,000 shares authorized
Special stock—Series A, $1.125 par value, 5,000,000 shares authorized

One special right is attached to each outstanding share of common stock. These rights entitle the holders to purchase, under certain conditions, units consisting of fractional shares of Special stock-Series A at a purchase price of $120 per unit, subject to adjustment. The rights also, under certain conditions, entitle certain holders to purchase $240 worth of common stock for $120. These rights expire on May 1, 2005, unless Promus decides to redeem them earlier at $0.01 per right or upon the occurrence of certain other events.

NOTE 10—EXTRAORDINARY ITEMS

During 1995, two Embassy Suites hotels, in which the Company has a 50 percent interest, realized extraordinary gains related to the early payoff and forgiveness of a portion of their existing debt. Promus' share of these nonconsolidated affiliates' gains was $2.8 million, net of income tax expense of $1.6 million. There were no extraordinary items reported in 1994 or 1993.

NOTE 11—NONCONSOLIDATED AFFILIATES

Combined summarized balance sheet and income statement information of nonconsolidated affiliates that Promus accounted for using the equity method as of December 31, 1995 and 1994, and for the three fiscal years ended December 31, 1995, were as follows (in thousands):

	1995	*1994*	*1993*
Combined Summarized Balance Sheet Information			
Current assets	$ 33,578	$ 26,178	
Land, buildings, furniture and equipment, net	366,624	376,480	
Other assets	18,435	26,097	
Total assets	418,637	428,755	
Current portion of long-term debt	187,339	6,019	
Other current liabilities	13,059	15,207	
Long-term debt	86,292	297,537	
Other liabilities	1,696	633	
Total liabilities	288,386	319,396	
Net assets	$130,251	$109,359	
Combined Summarized Income Statements			
Revenues	$157,748	$157,686	$150,431
Operating income	$ 35,161	$ 32,240	$ 27,613
Net income	$ 16,438	$ 5,221	$ 559

Several of Promus' nonconsolidated affiliates have debt maturities in 1996. These affiliates are in the process of renegotiating this nonrecourse debt. Promus management does not anticipate any material cash outlays in connection with these refinancings. Promus' share of its nonconsolidated affiliates' combined net income is reflected in the accompanying consolidated statements of income as follows (in thousands):

	1995	*1994*	*1993*
Pre-interest operating income (included in revenues—other)	$ 19,569	$ 18,077	$ 15,503
Interest expense (included in interest expense)	$(12,899)	$(12,749)	$(12,707)
Pretax extraordinary gain on forgiveness of debt (included in extraordinary items, net)	$ 4,454	$ —	$ —

The components of investments in and advances to nonconsolidated affiliates as of December 31 were as follows (in thousands):

	1995	*1994*
At equity	$39,868	$25,551
At cost	17,622	10,180
At market	33,016	—
	$90,506	$35,731

Certain Promus joint venture investments have been reduced below zero due to Promus' intention to fund its share of operating losses in the future, if needed. The total amount of these negative investments included in deferred credits and other liabilities in the consolidated balance sheets was $5.2 million and $5.0 million at December 31, 1995 and 1994, respectively.

NOTE 12—SUPPLEMENTAL CASH FLOW INFORMATION

The increase (decrease) in cash and cash equivalents due to the changes in long-term and working capital accounts was as follows (in thousands):

	1995	*1994*	*1993*
Long-term accounts			
Deferred credits and other long-term liabilities	$ 4,597	$ 6,792	$ 2,437
Deferred charges and other assets	(2,508)	(1,155)	431
Net change in long-term accounts	$ 2,089	$ 5,637	$ 2,868
Working capital accounts			
Accrued expenses	$ 9,725	$ 744	$ 564
Accounts payable	7,824	(4,410)	672
Receivables	(3,206)	(859)	3,127
Prepayments	(378)	(164)	(2,879)
Supplies	30	133	41
Other current assets	—	(366)	3,297
Net change in working capital accounts	$13,995	$(4,922)	$ 4,822

Supplemental Disclosure of Noncash Investing and Financing Activities

Concurrent with the Spin-Off, the historical assets and liabilities of the Hotel Business were transferred to Promus by Parent, and the issuance of Promus common stock was completed in connection with the Distribution.

During 1993, Promus transferred its ownership interest in five hotel properties to a third party in exchange for cash, the assumption by the third party of the related existing mortgage debt totaling $42.2 million and the issuance of $10 million in notes receivable maturing in three to five years. In an unrelated 1993 transaction, Promus sold a hotel property to a third party for cash and assumption by the third party of the related existing $3.3 million mortgage debt.

These noncash transactions have been excluded from the consolidated statements of cash flows.

Supplemental Disclosure of Cash Paid for Interest and Taxes

The following table reconciles Promus' interest expense, net of interest capitalized, to cash paid for interest (in thousands):

	1995	*1994*	*1993*
Interest expense, net of amount capitalized (Note 4)	$ 31,138	$ 30,759	$ 33,061
Adjustments to reconcile to cash paid for interest			
Promus' share of interest expense of nonconsolidated affiliates (Note 11)	(12,899)	(12,749)	(12,707)
Net change in accruals	(1,117)	—	125
Amortization of deferred finance charges	(785)	(733)	(846)
Net amortization of discounts and premiums	(8)	(45)	(869)
Other	(246)	(143)	(128)
Cash paid for interest, net of amount capitalized	$ 16,083	$ 17,089	$ 18,636
Cash paid for income taxes	$ 15,075	$ —	$ —

For purposes of this presentation, interest expense allocated to Promus by Parent is assumed to have been paid in the year allocated. Parent was responsible for the payment of Promus' income taxes for periods prior to the Spin-Off (Note 6).

NOTE 13—SUMMARIZED FINANCIAL INFORMATION

Promus Hotels, Inc. (PHI) is a wholly-owned subsidiary of Promus and the primary entity through which the operations of Promus are conducted. PHI is also Promus' principal asset. Summarized financial information for PHI, prepared on the same basis as Promus, as of and for the years ended December 31, is as follows (in thousands):

	1995	1994	1993
ASSETS			
Current assets	$ 23,246	$ 18,772	
Land, buildings, furniture and equipment, net	331,894	301,743	
Other assets	163,714	92,793	
	518,854	413,308	
LIABILITIES			
Current liabilities	54,851	28,544	
Long-term debt	229,479	188,725	
Other liabilities	68,112	53,031	
	352,442	270,300	
Net assets	$166,412	$143,008	
Revenues	$236,020	$222,561	$214,565
Operating income	$104,137	$ 92,388	$ 66,103
Net income	$ 46,895	$ 36,319	$ 16,926

NOTE 14—RELATIONSHIP BETWEEN PROMUS AND PARENT AFTER THE DISTRIBUTION

For the purpose of governing certain ongoing relationships between Promus and Parent after the Distribution and to provide mechanisms for an orderly transition, Parent and Promus have entered into various agreements and have adopted policies governing their future relationship. Management believes the agreements are fair to both parties and contain terms comparable to those which would have been reached in arm's-length negotiations with unaffiliated parties (although comparisons are difficult with respect to certain agreements that relate to the specific circumstances of the Distribution).

MANAGEMENT'S REPORT ON FINANCIAL STATEMENTS

Promus is responsible for preparing the financial statements and related information appearing in this report. Management believes that the financial statements present fairly its financial position, its results of operations and its cash flows in conformity with generally accepted accounting principles. In preparing its financial statements, Promus is required to include amounts based on estimates and judgments that it believes are reasonable under the circumstances.

Promus maintains accounting and other control systems designed to provide reasonable assurance that financial records are reliable for purposes of preparing financial statements and that assets are properly accounted for and safeguarded. Compliance with these systems and controls is reviewed through a program of audits by an internal auditing staff. Limitations exist in any internal control system, recognizing that the system's cost should not exceed the benefits derived.

The Board of Directors pursues its responsibility for Promus' financial statements through its Audit Committee, which is composed solely of directors who are not officers or employees of Promus. The Audit Committee meets from time to time with the independent public accountants, management and the internal auditors. Promus' internal auditors report directly to, and the independent public accountants have access to, the Audit Committee, with and without the presence of management representatives.

Michael D. Rose
Chairman of the Board

Jeffery M. Jarvis
Vice President, Controller &
Chief Accounting Officer

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Stockholders and Board of Directors of Promus Hotel Corporation:

We have audited the accompanying consolidated balance sheets of Promus Hotel Corporation (a Delaware corporation) and subsidiaries (Promus) as of December 31, 1995 and 1994, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years ended December 31, 1995. These financial statements are the responsibility of Promus' 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 Promus as of December 31, 1995 and 1994, and the results of its operations and its cash flows for each of the three years ended December 31, 1995, in conformity with generally accepted accounting principles.

Memphis, Tennessee
February 6, 1996.

QUARTERLY RESULTS OF OPERATIONS

(Unaudited)

(In thousands, except per share amounts)	*First Quarter*	*Second Quarter*	*Third Quarter*	*Fourth Quarter*	*Fiscal Year*
1995					
Revenues	$56,487	$61,073	$61,618	$56,842	$236,020
Operating income	24,645	27,725	31,380	19,840	103,590
Net income	9,604	11,626	15,761	9,588	46,579
Earnings per share (a and b)	0.19	0.23	0.31	0.19	0.90
Weighted average shares outstanding (b)	51,573	51,573	51,570	51,579	51,569
1994					
Revenues	$50,915	$58,255	$60,102	$53,289	$222,561
Operating income	19,194	23,761	30,643	18,790	92,388
Net income	6,131	10,207	13,592	6,389	36,319
Earnings per share (a and b)	0.12	0.20	0.26	0.12	0.70
Weighted average shares outstanding (b)	51,573	51,573	51,573	51,573	51,573

(a) The sum of the quarterly per share amounts may not equal the annual amount reported, as per share amounts are computed independently for each quarter while the full year is based on the annual weighted average common equivalent shares outstanding.

(b) For purposes of computing earnings per share on a comparable basis, the weighted average shares outstanding for periods prior to the Spin-Off are assumed to be equal to the actual common and common equivalent shares outstanding on June 30, 1995.

SELECTED FINANCIAL DATA

(In thousands)	*1995*	*1994*	*1993*	*1992*	*1991*
Operating Results					
Revenues	$236,020	$222,561	$214,565	$206,513	$158,004
Operating income before property transactions	101,648	91,762	64,758	49,610	35,206
Operating income	103,590	92,388	66,103	43,897	33,852
Income (loss) before income taxes and extraordinary items	75,579	63,117	30,795	3,242	(6,871)
Net income (loss)	46,579	36,319	16,926	6,361	(4,488)
Total assets	519,809	413,308	438,016	506,111	496,235
Long-term debt (a)	229,479	188,725	172,326	216,386	220,609

(a) Includes debt allocated to Promus Hotel Corporation by its Parent for periods prior to the Spin-Off.

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DIRECTORS AND OFFICERS

Board of Directors

Michael D. Rose[2]
Chairman of the Board,
Promus Hotel Corporation.
Memphis, Tennessee
Director since April 1995.

U. Bertram Ellis, Jr.[1]
President, Chief Executive Officer & Director,
Ellis Communications, Inc.
Atlanta, Georgia
Director since June 1995.

Debra J. Fields[1]
Chairman of the Board,
Mrs. Fields, Inc.
Salt Lake City, Utah
Director since June 1995.

Christopher W. Hart[3]
President,
Spire Group, Ltd.
Brookline, Massachusetts
Director since June 1995.

C. Warren Neel[1,2]
Dean, College of Business Administration,
University of Tennessee.
Knoxville, Tennessee
Director since June 1995.

Ben C. Peternell[2]
Senior Vice President,
Human Resources & Communications,
Harrah's Entertainment, Inc.
Memphis, Tennessee
Director since April 1995.

Michael I. Roth[1]
Chairman of the Board & Chief Executive Officer,
Mutual of New York.
New York, New York
Director since June 1995.

Raymond E. Schultz[2]
President & Chief Executive Officer,
Promus Hotel Corporation.
Memphis, Tennessee
Director since April 1995.

Jay Stein[3]
Chairman of the Board & Chief Executive Officer,
Stein Mart, Inc.
Jacksonville, Florida
Director since June 1995.

David C. Sullivan
Executive Vice President & Chief Operating Officer,
Promus Hotel Corporation.
Memphis, Tennessee
Director since April 1995.

Ronald Terry[2,3]
Former Chairman of the Board,
First Tennessee National Corporation.
Memphis, Tennessee
Director since June 1995.

[1] Audit Committee
[2] Executive Committee
[3] Human Resources Committee

Corporate Executive Officers

Michael D. Rose
Chairman of the Board

Raymond E. Schultz
President & Chief Executive Officer

David C. Sullivan
Executive Vice President & Chief Operating Officer

Donald H. Dempsey
Senior Vice President & Chief Financial Officer

Thomas L. Keltner
Senior Vice President, Development

Ralph B. Lake
Senior Vice President, General Counsel & Secretary

Mark C. Wells
Senior Vice President, Marketing

Other Corporate Officers

Carol G. Champion
Vice President & Treasurer

Vincent C. Ciaramitaro
Vice President, Financial Services

Patricia R. Ferguson
Vice President, Human Resources

M. Ronald Halpern
Vice President & Deputy General Counsel

James T. Harvey
Vice President, Information Technology

Jeffery M. Jarvis
Vice President & Controller

INVESTOR INFORMATION

Stock Listings

Promus Hotel Corporation common stock trades on the New York Stock Exchange under the ticker symbol PRH. The stock is also listed on the Chicago, Philadelphia and Pacific regional stock exchanges.

Annual Meeting Date

Promus Hotel Corporation will conduct its 1996 Annual Meeting of stockholders on April 24, 1996, 11 a.m. (CDT) at the Embassy Hall, Embassy Suites Hotel, 1022 South Shady Grove Road, Memphis, Tennessee.

Shareholder Account Assistance

For address changes, account consolidation, registration changes, lost stock certificates and other shareholder services, contact: Continental Stock Transfer & Trust Company, 2 Broadway, New York, NY 10004 or call 800-509-5586.

Investor Relations

Financial community information requests and requests for financial reports should be directed to: Gregg A. Swearingen, Director, Investor Relations, at 755 Crossover Lane, Memphis, TN 38117, or by calling (901) 680-7222.

Form 10-K

A shareholder may receive without charge a copy of the Form 10-K Annual Report filed with the Securities and Exchange Commission by written request to Investor Relations at the address provided in this section or by calling (901)-680-7222.

Corporate Communications

All media inquiries or requests for copies of this report should be directed to: John C. Hawkins, Director, Corporate Communications, at 755 Crossover Lane, Memphis, TN 38117 or by calling (901) 680-7332.

Corporate Headquarters

755 Crossover Lane
Memphis, TN 38117
(901) 374-5000

Auditors

Arthur Andersen LLP
165 Madison Avenue
Memphis, TN 38103

Reservation Information

Guests wishing to make reservations at our properties may do so by calling the following toll-free numbers:

Embassy Suites Hotels
1-800-EMBASSY

Hampton Inn Hotels
1-800-HAMPTON

Hampton Inn & Suites Hotels
1-800-HAMPTON

Homewood Suites Hotels
1-800-CALL-HOME

Internet Communications

A company overview, financial highlights, statistical data, operating philosophy and reservations information can be found on the Internet by accessing World Wide Web http://www.promus-hotel.com.

Trademarks

The following trademarks are used in this report to identify products and services of Promus Hotel Corporation, its subsidiaries and affiliates: Embassy Suites, Hampton Inn, Hampton Inn & Suites, Homewood Suites, People Pledged to Excellence and 1-800-CALL-HOME.

PROMUS HOTEL CORPORATION

755 Crossover Lane Memphis, TN 38117 901 374-5000