TOWN SPORTS INTERNATIONAL HOLDINGS INC
Form 10-K
March 14, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

þ **Annual Report pursuant to Section 13 OR 15(d) of the Securities Exchange Act of 1934**
For the fiscal year ended December 31, 2013

¨ **Transition Report pursuant to Section 13 OR 15(d) of the Securities Exchange Act of 1934**
For the transition period from

Commission file number: 000-52013

Town Sports International Holdings, Inc.

(Exact name of Registrant as specified in its charter)

DELAWARE	**20-0640002**
(State or other jurisdiction of incorporation or organization)	**(I.R.S. Employer Identification No.)**
5 PENN PLAZA 4TH FLOOR NEW YORK, NEW YORK	**10001**
(Address of principal executive offices)	**(Zip code)**

(212) 246-6700

(Registrant s telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $0.001 par value	**The NASDAQ Stock Market LLC**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No þ

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ¨ No þ

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

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part IV of this Form 10-K or any amendment to this Form 10-K. þ

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

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

The aggregate market value of the voting common stock held by non-affiliates of the registrant as of June 28, 2013 (the last business day of the registrant s most recently completed second fiscal quarter) was approximately $194.1 million (computed by reference to the last reported sale price on The Nasdaq National Market on that date). The registrant does not have any non-voting common stock outstanding.

As of February 27, 2014, there were 24,092,016 shares of Common Stock of the Registrant outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive proxy statement for the 2014 Annual Meeting of Stockholders, to be filed not later than April 30, 2014, are incorporated by reference into Items 10, 11, 12, 13 and 14 of Part III of this Form 10-K.

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TOWN SPORTS INTERNATIONAL HOLDINGS, INC.

FORWARD-LOOKING STATEMENTS

This Annual Report on Form 10-K contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, including, without limitation, statements regarding our future expectations regarding the sale of the property located at East 86th Street, New York, future financial results and performance, potential sales revenue, legal contingencies and tax benefits and contingencies, and the existence of adverse litigation and other risks, uncertainties and factors set forth under Item 1A., entitled Risk Factors , of this Annual Report on Form 10-K and in our reports and documents filed with the Securities and Exchange Commission (SEC). You can identify these forward-looking statements by the use of words such as outlook , believes , expects , potential , continues , m should , seeks , approximately , predicts , intends , plans , estimates , anticipates or the negative version of these words or other compara These statements are subject to various risks, and uncertainties, many of which are outside our control, including the level of market demand for our services, competitive pressure, the ability to achieve reductions in operating costs and to continue to integrate club acquisitions, the ability to close the sale of the property located at East 86th Street, New York, environmental initiatives, the application of Federal and state tax laws and regulations, and other specific factors discussed herein and in other SEC filings by us. We believe that all forward-looking statements are based on reasonable assumptions when made; however, we caution that it is impossible to predict actual results or outcomes or the effects of risks, uncertainties or other factors on anticipated results or outcomes and that, accordingly, one should not place undue reliance on these statements. Forward-looking statements speak only as of the date they were made, and we undertake no obligation to update these statements in light of subsequent events or developments. Actual results may differ materially from anticipated results or outcomes discussed in any forward-looking statement.

PART I

Item 1. ***Business***

In this Annual Report, unless otherwise stated or the context otherwise indicates, references to Town Sports , TSI , the Company , we , our and similar references refer to Town Sports International Holdings, Inc. and its subsidiaries, references to TSI Holdings refers to Town Sports International Holdings, Inc., and references to TSI, LLC refer to Town Sports International, LLC, our wholly-owned operating subsidiary.

General

We are the largest owner and operator of fitness clubs in the Northeast and Mid-Atlantic regions of the United States (U.S.) and the third largest fitness club owner and operator in the U.S., in each case based on the number of clubs. As of December 31, 2013, the Company, through its subsidiaries, operated 162 fitness clubs under our four key regional brand names; New York Sports Clubs (NYSC), Boston Sports Clubs (BSC), Philadelphia Sports Clubs (PSC) and Washington Sports Clubs (WSC). As of December 31, 2013, these clubs collectively served approximately 497,000 members, including approximately 41,000 members under our restricted student and teacher membership programs. We owned and operated a total of 108 clubs under the New York Sports Clubs brand name within a 120-mile radius of New York City as of December 31, 2013, including 37 locations in Manhattan where we are the largest fitness club owner and operator. We owned and operated 29 clubs in the Boston region under our Boston Sports Clubs brand name, 16 clubs (two of which are partly-owned) in the Washington, D.C. region under our Washington Sports Clubs brand name and six clubs in the Philadelphia region under our Philadelphia Sports Clubs brand name as of December 31, 2013. In addition, we owned and operated three clubs in Switzerland as of December 31, 2013. We employ localized brand names for our clubs to create an image and atmosphere consistent with the local community and to foster recognition as a local network of quality fitness clubs rather than a national chain.

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We develop clusters of clubs to serve densely populated major metropolitan regions and we service such populations by clustering clubs near the highest concentrations of our target customers areas of both employment and residence. Our clubs are located for maximum convenience to our members in urban or suburban areas, close to transportation hubs or office or retail centers. Our members include a wide age demographic covering the student market to the active mature market. Our members generally have annual income levels of between $50,000 and $150,000. We believe that this mid-value segment is the broadest of the market. Our goal is to be the most recognized health club network in each of the four major metropolitan regions that we serve. We believe that our strategy of clustering clubs provides significant benefits to our members and allows us to achieve strategic operating advantages. In each of our markets, we have developed clusters by initially opening or acquiring clubs located in the more central urban markets of the region and then branching out from these urban centers to suburbs and neighboring communities.

We currently offer three principal types of memberships in our clubs, Passport, which offers access to all clubs at all times, Core, which offers access to a single home club at all times, and Restricted memberships, which is a favorably priced, restricted month-to-month membership offering access to a single home club during all operating hours except 4:30pm to 7:30pm, Monday through Thursday, otherwise a usage fee applies. Members, excluding restricted members, can elect to commit to a minimum contract period of one year in order to benefit from reduced joining fees. Alternatively, our memberships are available on a month-to-month basis. These membership types are described in further detail in the Sales discussion that follows.

Over our 40-year history since 1973, we have developed and refined our club formats, which allows us to cost-effectively construct and efficiently operate our fitness clubs in the different real estate environments in which we operate. Our fitness-only clubs average approximately 21,000 square feet, while our multi-recreational clubs average approximately 37,000 square feet. The aggregate average size of our clubs is approximately 26,000 square feet. Our clubs typically have an open fitness area to accommodate cardiovascular and strength-training equipment, as well as special purpose rooms for group fitness classes and other exercise programs. We seek to provide a broad array of high-quality exercise programs and equipment that are popular and effective, promoting a quality exercise experience for our members. When developing clubs, we carefully examine the potential membership base and the likely demand for supplemental offerings such as swimming, basketball, children s programs, tennis or squash and, provided suitable real estate is available, we will add one or more of these offerings to our fitness-only format. For example, a multi-recreational club in a family market may include Sports Clubs for Kids programs, which can include swim lessons and sports camps for children.

As the fitness industry continues to see a rise in popularity of private studio offerings, we intend to offer our own private studio brand called the Boutique Fitness Experience (BFX Studio) with our first unit opening in the first half of 2014 with expectations to open a total of two to four BFX Studio units during 2014. This three-dimension luxury studio brand will take advantage of the rise in consumer demand for studio experiences. Our BFX Studio will include three unique offerings: Ride Republic, which is indoor cycling, Private Sessions for personal training and Master Class for certain group exercise classes. Our BFX Studio will be staffed with high caliber instructors in each of the three core offerings and the studios will be designed to appeal to all ages and all experience levels of metropolitan, active healthy lifestylers. We estimate that this studio concept will require approximately 7,500 to 10,000 square feet of space per studio which compares to the approximately 26,000 square feet aggregate average size of our traditional clubs.

Industry Overview

According to the most recent information released by the International Health, Racquet and Sportsclub Association (IHRSA), total U.S. fitness club industry revenues increased at a compound annual growth rate of 3.1% from $18.7 billion in 2007 to $21.8 billion in 2012, with a 1.9% increase from 2011 to 2012. Total U.S. fitness club memberships increased at a compound annual growth rate of 3.9% from 41.5 million in 2007 to 50.2 million in 2012, with a 2.3% decline from 2011 to 2012 after reaching an all-time high of 51.4 million members in 2011. Although memberships declined in 2012 compared to 2011, revenue increased slightly due, in

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part, to the impact of non-membership revenue performance from niche and studio concepts. According to the IHRSA, the fitness industry is witnessing a shift in the exercise and preference of health club members. The club landscape now extends beyond the traditional, full-service fitness centers as studio concepts including boxing, yoga, Pilates, group cycling, barre, boot camps, CrossFit, and personal training, also shape the market.

According to the IHRSA, participation in health clubs has been growing over the past five years with 53.4 million Americans utilizing a health club in 2008, as compared to 58.5 million Americans utilizing a health club in 2012. Currently, approximately 17% of the total U.S. population belongs to a health club, leaving room for possible substantial growth in the industry and indicating a significant opportunity to convert these non-members to members. In 2012, the average number of days per year that health club members visited clubs was down 3.4% to 99.0 days after reaching an all time high of 102.5 days in 2011.

According to the IHRSA, demographic trends have helped drive the growth experienced by the fitness industry over the past decade. The average age of a health club member in 2012 was 38 years old and more than one-third of health club members were between the ages of 18 and 34 years old. The greatest membership growth in the past few years has been in the demographic group ages 18 to 34, which has grown 31.4% from 2008 to 2012 and in the group ages 35 to 54, where membership grew 6.1% from 2008 to 2012. These two age groups made up approximately 70.0% of total U.S. health club members in 2012. The industry has also benefited from the aging baby boomer and Eisenhower generations as they place greater emphasis on their health, including a focus on fitness.

According to the Centers for Disease Control and Prevention, during the period from 1990 through 2010**,** there was a dramatic increase in obesity in the U.S. and rates remain high. State prevalence of obesity continues to remain high across the country in 2012, with no state with a prevalence of obesity less than 20.0%. In 2012, 41 states had a prevalence of 25% or more and 13 of these states had a prevalence of 30% or more. As healthcare costs continue to rise in the U.S., some of the focus on combating obesity and other diseases is being directed at prevention. Both government and medical research has shown that exercise and other physical activity plays a critical role in preventing obesity and other health conditions, thereby reducing healthcare costs for treating obesity related sicknesses.

As the focus on exercise and overall healthy lifestyles continue to impact the health club industry, we believe that we are well positioned to benefit from these dynamics as a large operator with recognized brand names, leading regional market shares and an established operating history.

Competitive Strengths

We believe the following competitive strengths are instrumental to our success:

Strong market position with leading brands. Based on number of clubs, we are the third largest fitness club owner and operator in the U.S. and the largest fitness club owner and operator in the Northeast and Mid-Atlantic regions of the U.S. We are the largest fitness club owner and operator in our New York, Boston and Washington, D.C. regions, and the fourth largest owner and operator in our Philadelphia region. We attribute our positions in these markets in part to the strength of our localized owner and operator brand names, which foster recognition as a local network of quality fitness clubs.

Regional clustering strategy provides significant benefits to members and corporations. By operating a network of clubs in a concentrated geographic area, the value of our memberships is enhanced by our ability to offer members access to any of our clubs, which provides the convenience of having fitness clubs near a member s workplace and home. This is also a benefit to our corporate members, as many corporations have employees that will take advantage of multiple gym locations. Approximately 226,000, or 45%, of our members currently have a Passport Membership, including our corporate and group Passport Memberships, and because these memberships offer enhanced privileges and greater convenience, they generate higher monthly dues than our Core Membership in each respective region. Regional clustering also allows us to provide special facilities to all of our members within a local area, such as swimming pools and squash, tennis and basketball courts, without offering them at every location. In the year ended December 31, 2013, 40% of all club usage was by members visiting clubs other than their home clubs.

Regional clustering strategy designed to enhance revenues and achieve economies of scale. We believe our regional clustering strategy allows us to enhance revenue and earnings growth by providing high-quality, conveniently located fitness facilities on a cost-effective basis. We believe that potential new entrants would need to establish or acquire a large number of clubs in a market to compete effectively with us. Our clustering strategy also enables us to achieve economies of scale with regard to sales, marketing, purchasing, general operations and corporate administrative expenses and reduces our capital spending needs. Regional clustering also provides the opportunity for members who relocate within a region to remain members of our clubs, thus aiding in member retention.

Expertise in site selection and development process. We believe that our expertise in site selection and development provides an advantage over our competitors given the complex real estate markets in the metropolitan areas in which we operate and the relative scarcity of suitable sites. Before opening or acquiring a new club, we undertake a rigorous process involving demographic and competitive analysis, financial modeling, site selection and negotiation of lease and acquisition terms to ensure that a potential location meets our criteria for a model club. We believe our flexible club formats are well suited to the challenging real estate environments in our markets. We currently have 162 clubs under operation that can easily adapt and respond to the changing demands of our customers. This flexibility allows us to compete against private studios with unique specialty offerings by adapting the space and formats in our own clubs to match the offerings provided by these private studios. An example of the use of this flexibility is evidenced in the installation of our UXF training zones within our clubs which was introduced in 2012 as part of our UXF launch. This training zone features an array of innovative equipment designed to maximize the member s experience and support growth in personal training. As of December 31, 2013, UXF training zones have been installed in 126 clubs.

Expertise of senior management. We believe that our senior management s industry expertise, particularly that of our Chief Executive Officer, Robert Giardina, our President, Chief Operating Officer and Chief Financial Officer, Daniel Gallagher, and our Senior Vice President, Chief Information Officer, Paul Barron, provides us with a competitive advantage. Mr. Giardina has extensive knowledge of the fitness industry and over 30 years of experience with the Company. Mr. Giardina was appointed President and Chief Executive Officer in March 2010 and now serves as Chief Executive Officer. He originally joined the Company in 1981 and served as President and Chief Operating Officer from 1992 to 2001, and as Chief Executive Officer from January 2002 through October 2007. Mr. Gallagher joined the Company in February of 1999 as Vice President Finance and served as the Company s Chief Financial Officer since April 2008. Mr. Gallagher was recently promoted to President and Chief Operating Officer in January 2014. Prior to joining the Company, Mr. Gallagher s experience included management roles at large public accounting firms including Coopers & Lybrand and PricewaterhouseCoopers. Mr. Barron joined the Company in February 2011 as Chief Information Officer. Prior to joining the Company, Mr. Barron s experience included a vice president role at Newmarket International, a leading software company for hospitality sales automation and prior to that as a vice president of IT solutions at Starwood Hotels and Resorts. We believe that Mr. Giardina, Mr. Gallagher and Mr. Barron are highly talented and innovative executives who have strong strategic skills and leadership capabilities to lead the Company and execute its strategies.

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Business Strategy

In the long-term, we seek to maximize our net member growth, revenues, earnings and cash flows using the following strategies:

Build and acquire new clubs. We plan to expand our club base through both designing and building clubs and through selective acquisitions. During 2013, we completed the acquisition of the Fitcorp clubs in Boston, which included five clubs and four managed sites. We also completed an acquisition of a single club in Manhattan. In 2014, our expected club openings are concentrated in the urban markets in our New York and Boston regions, with plans to open a combined five to six NYSC and BSC clubs in 2014. We also plan to open two to four new BFX Studio units. This will bring our total unit growth to seven to 10 units when including the BFX Studio units. We expect to fund our club expansion with cash on hand or through internally generated cash flows and, if needed, we can utilize borrowings under our revolving credit facility.

Build on our new Boutique Fitness Experience studio concept. We plan to open a distinctive luxury studio brand in the first half of 2014. This three-product luxury studio brand will take advantage of the rise in consumer demand for studio experiences. Our BFX Studio will include three unique offerings: Ride Republic, which is indoor cycling, Private Sessions for personal training and Master Class for certain group exercise classes. Each BFX Studio is expected to be approximately 7,500 to 10,000 square feet and cost approximately $1.5 million to $2.25 million per studio.

Grow ancillary and other non-membership revenues. We intend to grow our ancillary and other non-membership revenues through a continued focus on increasing the additional value-added services that we provide to our members as well as capitalizing on the opportunities for other non-membership revenues such as in-club advertising and retail sales. Over the past five years, we have expanded the range of ancillary club services provided to members. Non-membership revenues have increased from $85.2 million, or 17.5% of revenues for the year ended December 31, 2009, to $97.1 million, or 20.6% of revenues for the year ended December 31, 2013. Personal training revenue, in particular, increased 16.5% over this five-year period and increased as a percentage of total revenue from 11.7% in 2009 to 14.1% in 2013. Our long-term goal is to generate approximately 20% of revenue from personal training. Our personal training offerings have expanded beyond the prepaid personal training sessions and now also include single or multi-session personal training membership products, originally introduced in 2011 and expanded in 2012 and 2013. We have also expanded our fee-based class offering to generate additional revenue. These offerings include our Ultimate Fitness Experience (UXF) class introduced in 2012. In addition, our fee-based Small Group Training programs include offerings such as Pilates Reformer Technique, Total Body Resistance Exercise (TRX) and Kettlebells, and our Signature Classes which include VBarre and Pilates Tower. We also offer Sports Clubs for Kids programs at select clubs. In 2014, we plan to remain focused on increasing our ancillary programs with continued improvements in training and hiring and building on ancillary programs such as our personal training membership product. These sources of ancillary and other non-membership revenues generate incremental profits with minimal capital investment and assist in attracting and retaining members.

Retain members by focusing on the member experience. Our Company s mission is Improving Lives Through Exercise. We enact our mission through our Ten Essentials, which provide a clear road map for how we want our clubs to look and how we want to serve our members. This is the core of our member experience strategy and allows us to crystallize how we engage our staff to deliver a superior member experience. We tailor the hours of each club to the needs of the specific member demographic utilizing each club and offer a variety of ancillary services, including personal training, group classes, Small Group Training, Sports Clubs for Kids programs, and the XpressLine strength workout which is an eight-station total-body circuit workout designed to be used in 22 minutes and accommodates all fitness levels. We offer a variety of different sports facilities in each regional cluster of clubs; modern, varied and well-maintained exercise and fitness equipment; and an assortment of additional amenities including access to babysitting, sports massage and pro-shops. Through hiring, developing and training a qualified and diverse team that is passionate about fitness and health; maintaining and enhancing our programs and services; and continually increasing our attention to individual member needs, we expect to demonstrate our commitment to increase the quality of the member experience, and thereby increase net membership. To further ensure the member experience remains at a high quality, we provide member surveys to help analyze the areas we can improve upon as well as the areas in which the members are satisfied overall.

Provide state-of-the-art fitness equipment and services. To help members develop and maintain a healthy lifestyle, train for athletic events or lose weight, each of our clubs has a large array of cardiovascular machines and resistance training equipment and free weights. Exercise equipment is positioned to allow for easy movement from machine to machine, facilitating a convenient and efficient workout. Equipment in these areas is generally arranged in long parallel rows that are labeled by muscle group, which allows members to conveniently customize their exercise programs and reduce downtime during their workouts. We have technicians who service and maintain our equipment on a timely basis. In addition, we have personal viewing television screens on most pieces of cardiovascular equipment. Most clubs have between one and three studios used for exercise classes, including at least one large studio used for most group exercise classes, a cycling studio and a mind and body studio used for yoga and Pilates classes. We offer a large variety of group fitness classes at each club and these classes generally are at no additional cost to our members. The volume and variety of activities at each club allow each member to enjoy the club, whether customizing their own workout or participating in group activities and classes.

Marketing

Our marketing campaign, which we believe has increased awareness of our brand names, is directed by our marketing department, which directly reports to the Chief Executive Officer. This team develops advertising strategies to convey each of our regionally branded networks as the premier network of fitness clubs in its region. Our marketing team s goal is to focus on growing our membership base, achieving broad awareness of our regional brand names and be top of mind . We are organized to enable close collaboration between our marketing, sales, fitness and operations staff, which helps to align efforts around operational objectives and new product development while ensuring a primary focus on the member experience.

Brand awareness and preference is aided by a number of factors, including visibility of multiple retail locations and associated signage across each region, word-of-mouth recognition and referrals generated by our membership base of approximately 497,000 as of December 31, 2013, a 40-year operating history and continual advertising investment. All of these factors provide a strong foundation for our ongoing marketing and advertising efforts.

Our regional concentration and clustering strategy creates economies of scale in our marketing and advertising investments which increase their overall efficiency and effectiveness. Clustering enables broader reach and higher frequency for regional advertising campaigns that typically include a mix of traditional media including radio, newspapers, magazines, out-of-home and some television. Geo-targeted and behaviorally targeted digital media, such as paid search, email blasts, online banners and video, as well as other emerging new media vehicles are also utilized. These broader market efforts are bolstered by local marketing plans and tactics, which include direct mail, local sponsorships and co-promotions, as well as community relations and outreach and street-level lead generation activities. Optimization of marketing mix through measurement and modeling of the effectiveness of various media investments and formats continues to be a priority.

Our advertising and marketing message is designed to build our brand while creating an approachable personality that is attractive to prospective members and allows them to feel comfortable with our brand. In contrast to most health club advertising, we generally forego depicting images of hard bodies, facilities and gym equipment. Advertisements generally feature creative slogans that use current events to communicate the serious approach we take toward fitness in a provocative and/or humorous tone. We believe this approach is easily communicated and understood and makes our product more approachable for all consumers regardless of their health club experience.

Promotional marketing campaigns will typically feature opportunities to participate in a variety of value-added services such as personal training, Small Group Training and youth centered sports activities. We also may offer reduced joining fees to encourage enrollment. Additionally, we sponsor member referral incentive programs periodically and other types of member appreciation, acquisition activities and internal promotions to enhance loyalty and to encourage more members to take advantage of our ancillary services.

We engage in public relations, sponsorships and special events to promote our brand image across our network, regionally and in our local communities. We have been featured in national broadcast channels and television shows, such as Good Morning America, The Today Show, Fox & Friends, CNN, MSNBC, CNBC, Fox News Channel, ESPN, The Steve Harvey Show and Access Hollywood; and major newspapers, such as The New York Times, USA Today, Washington Post, Boston Globe, The Wall Street Journal, and Crain s; and seen in magazines, such as Fitness, Self, Shape, New York Magazine, Women s Health, Marie Claire and Prevention Magazines.

Our philosophy of giving back to our communities includes sponsoring company-wide and local charitable efforts. Our club management teams and staff are also encouraged to organize and engage in charitable activities. These events have benefited organizations such as the HealthCorps, ALS Therapy Development Institute, Muscular Dystrophy Association, American Cancer Society, Susan G. Komen Race for the Cure, Wounded Warrior Project, No Kid Hungry, as well as many smaller local and specific charities such as: Boston Children s Hospital, Josephine s Garden for Pediatric Cancer, North Rockland Soccer Association, and The Theatre Offensive of Boston and Verrazano Babe Ruth League.

Sales

We sell our memberships through four channels: direct sales at the club level; through our corporate and group sales division; through our online website; and through our call center which we introduced in September 2010 principally to reach out to former members and to handle specific campaigns. We are constantly reviewing other possible opportunities to sell memberships through the call center. We employ over 400 in-club membership sales consultants who are responsible for new membership sales in and around their designated club locations. Each club generally has either two or three membership sales consultants. These consultants report directly to the club general manager, who, in turn, reports to a business director. Additional incentive-based compensation represents a majority of the compensation for the membership sales consultants. Membership sales consultants must successfully complete an in-house four week training program through which they learn our sales strategy and gain valuable hands-on experience. In our New York, Boston and Washington regions, these trainings primarily occur in our three sales academies which were introduced in August 2011. All membership sales consultants hired and working within these regions attend these training centers where a full time sales training manager is available to them. These academies are hosted within working clubs and the membership sales consultants all have the opportunity to learn and experience the entire sales process (from prospecting to after care) and product knowledge in what we consider a live but supervised environment. There are assessments throughout the training and the membership sales consultants must pass the course prior to being selected and placed in a club. Both the in-house/in-club and sales academy training allows us to achieve consistency in our selling process. Successful completion of our training program allows each membership sales consultant to be consistently trained and exit the training program with a high level of brand standard selling skills, which will assist them in achieving their targeted sales objectives.

Our corporate and group sales division consists of approximately 21 full-time employees located throughout our markets, who concentrate on building long-term relationships with local and regional companies and large groups. Corporate and group members accounted for approximately 18% of our total membership base as of December 31, 2013. We offer numerous programs to meet our corporate and group clients needs. We have developed our club level teams and systems to allow our corporate and group clients the opportunity to join at their convenience at their local club, online or through our call center. Standard & Poors, New York University, Ralph Lauren, Con Edison, Viacom and Citibank are among just a few of the many clients that are currently enrolled in our corporate membership program. We believe this focus on relationship building, providing the corporate and group member with options for enrollment and our clustering strategy will continue to lead to new group participation in the future. Corporate and group membership sales are typically sold under our higher priced Passport Memberships at a discount to our standard rates with corporations sometimes subsidizing the costs of memberships provided to their employees. During 2013, as a means of continuing to grow our corporate and group sales division, we launched the Fitcorp Private Fitness Center Division in June 2013 under the

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leadership of Gary Klencheski who joined TSI as part of the Fitcorp acquisition in May 2013. The Fitcorp Private Fitness Center Division is responsible for managing private fitness centers for both large and small corporations, colleges and universities, and private clubs. We currently manage eight fitness facilities comprised of three university fitness clubs, four managed sites which were acquired as part of the Fitcorp acquisition and one new managed site which was added during the fourth quarter of 2013 under the efforts of our Fitcorp Private Fitness Center Division.

We also sell individual memberships online at www.mysportsclubs.com for our standard membership types and the website also enables us to sell memberships for pre-established corporate and group programs. The website also allows our members to give us direct feedback about our service levels and enables prospective members to sign up for our popular 30 days for 30 dollars web trial membership. The online sales channel offers a high degree of convenience for customers who know and trust our brand and do not require up-front interaction with a membership sales consultant to make their decision. In addition, selling online significantly reduces our cost of sale. Members who joined online accounted for approximately 1.9% of memberships sold in 2013. The web site also provides information about club locations, program offerings, exercise class schedules and sales promotions. Job seekers can also begin the employment application process through the site and investors can access financial information and resources.

We believe that clustering clubs allows us to sell memberships based upon the opportunity for members to utilize multiple club locations near their workplace and their home. As of December 31, 2013, we currently offer the following three types of memberships:

The Passport Membership is our higher priced membership and entitles members to use any of our clubs in any region at any time and our Regional Passport Membership, offered in our WSC and PSC regions, entitles members to use any of our clubs within one region. These membership plans provide the convenience of having fitness clubs near a member s workplace and home. The current list price of a commit Regional Passport and Passport Memberships generally ranges from $69.99 per month to $99.99 per month, excluding passport restricted members, corporate and group members and premium memberships available at a very limited number of clubs. Our corporate and group memberships are sold as Passport Memberships and averaged approximately $65 per month for those sold in the year ended December 31, 2013. The Passport Membership, excluding our passport restricted members, described below, and including our corporate and group members, was held by approximately 226,000 members, or 45% of our total members as of December 31, 2013. In addition, we have a Passport Premium Membership at two select clubs, which includes a greater array of member services and facilities, with list prices currently ranging from $105.99 per month to $115.99 per month. Further, our Boston Racquet Club, offers a higher level Premium Membership that includes an exclusive Squash membership available only at this club, with pricing ranging from $135.00 to $170.00 per month.

The Core Membership was introduced on November 1, 2010 and enables members to use a specific club at any time. The current list price of a commit Core membership generally ranges from $39.99 per month to $89.99 per month based on club specific facilities and services, the market area of enrollment and length of the membership contract. Core members can also elect to pay a per visit fee ranging from $9.50 to $12.00 per visit to use non-home clubs. The Core Membership, excluding our core restricted members described below, was held by approximately 152,000 members, or 31% of our members as of December 31, 2013.

The Restricted Membership is a favorably-priced, restricted-use month-to-month only membership. In April 2010, this membership was introduced to students and we extended the membership to teachers and first responders in April 2011 and September 2011, respectively. Usage fees ranging from $9.50 to $12.00 per visit are applied if a restricted member chooses to use a club from 4:30pm to 7:30pm, Monday through Thursday. The restricted Passport Membership is currently listed at $39.99 per month and the restricted Core Membership is currently listed at $29.99 per month. Additional groups may also be offered a restricted membership at times through our call center. The Restricted Membership was held by

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approximately 41,000 restricted members, or 8% of our members as of December 31, 2013. Approximately 87% of these restricted members are comprised of our restricted student and teacher memberships.

Prior to November 1, 2010, we also offered The Gold Membership, which is no longer offered to new members. This membership enables members to use a specific club at any time and any of our clubs during off-peak times. Gold members can elect to pay a per visit fee ranging from $9.50 to $12.00 per visit to use non-home clubs during peak hours. This membership was held by approximately 78,000 members, or 16% of our members as of December 31, 2013.

We offer both month-to-month and commit membership options. A member may cancel a month-to-month membership at any time with 30-days notice. Under the commit model, new members commit to a one year membership. In 2013 and 2012, 90% and 89%, respectively, of our newly enrolled members opted for a commit membership. As of December 31, 2013, approximately 20% of our members had originated under a month-to-month non-commit membership and 80% had originated under a commit membership. When the members commit period is over, they retain membership as a month-to-month member until they choose to cancel. As of December 31, 2013, approximately 72% of our total members were on a month-to-month basis. We believe that members prefer to have the flexibility to choose between committing for one year or to join under the month-to-month, non-commit membership.

Prior to the implementation of our rate lock guarantee and maintenance fee in May 2011, we have historically increased our existing member dues annually by between 1% and 3% on average, in line with increases in the cost of living. In May 2011, we implemented a combined rate lock guarantee and maintenance fee to which all members agree at the time of enrollment. This fee, which is currently $39.99, is collected annually in January and is recognized in membership revenue over the subsequent 12 month period following collection. In January 2013 and January 2012, we collected approximately $7.0 million and $3.5 million, respectively, related to this new fee. In 2013, membership dues increases were applied to approximately 10% of our membership base (for those members joining prior to the May 2011 rate lock guarantee) resulting in an overall dues increase of approximately less than 1% on these members.

In joining a club, a new member signs a membership agreement that typically obligates the member to pay one-time joining fees, an annual rate lock guarantee and maintenance fee, and monthly dues on an ongoing basis. Joining fees collected for new monthly electronic funds transfer, or EFT, members averaged approximately $59, $57 and $55 per member for the years ended December 31, 2013, 2012 and 2011, respectively. Monthly EFT of individual membership dues on a per-member basis, including the effect of promotions and memberships with reduced dues, averaged approximately $59, $58 and $59 per month for the years ended December 31, 2013, 2012 and 2011, respectively. Currently, 97.0% of our members pay their membership dues through EFT, with EFT membership revenue constituting approximately 73.5% of consolidated revenue for the year ended December 31, 2013. Substantially all other membership dues are paid in full in advance. Our membership agreements call for monthly dues to be collected by EFT based on credit card or bank account debit authorization contained in the agreement. During the first week of each month, we receive the EFT dues for that month after the payments are initiated by a third-party EFT processor. Discrepancies and insufficient funds incidents are researched and resolved by our in-house account services department.

Usage

Our suburban clubs are generally open 5:00 AM to 10:00 PM on weekdays and 7:00 AM to 7:00 PM on weekends, while our urban clubs are generally open 5:30 AM to 11:00 PM on weekdays and 8:00 AM to 9:00 PM on weekends. We generally consider our peak usage times to be between 6:00 AM and 8:30 AM and 4:30 PM and 7:30 PM on weekdays. Our hours of business are based on usage patterns at each individual club. Our total club usage, based on the number of member visits, was 29.1 million and 29.7 million member visits for

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the years ended December 31, 2013 and 2012, respectively. In the year ended December 31, 2013, approximately 40% of total usage or club visits was to members non-home clubs, indicating that our members take advantage of our network of clubs. Our memberships plans allow for club members to elect to pay a per visit fee ranging from $9.50 to $12.00 to use non-home clubs, subject to peak and non-peak hourly restrictions depending on the membership type. In the aggregate, approximately $2.1 million and $2.2 million of usage fees were generated in 2013 and 2012, respectively, and are reported in membership dues in our consolidated statements of operations.

Non-Membership Revenue

The table below presents non-membership revenue components as a percentage of total revenue for the years ended December 31, 2009 through 2013.

	For the Years Ended December 31, ($ in thousands)									
	2013	**%**	**2012**	**%**	**2011**	**%**	**2010**	**%**	**2009**	**%**
Total revenue	$ 470,225	100.0%	$ 478,981	100.0%	$ 466,941	100.0%	$ 462,387	100.0%	$ 485,392	100.0%
Non-Membership Revenue:										
Personal training revenue(1)	66,367	14.1%	65,641	13.7%	62,394	13.4%	60,875	13.2%	56,971	11.7%
Other ancillary club revenue(2)	24,720	5.3%	29,897	6.3%	28,297	6.1%	24,684	5.3%	23,536	4.8%
Fees and Other revenue(3)	5,985	1.3%	5,804	1.2%	4,890	1.0%	4,761	1.0%	4,661	1.0%
Total non-membership revenue	$ 97,072	20.6%	$ 101,342	21.2%	$ 95,581	20.5%	$ 90,320	19.5%	$ 85,168	17.5%

(1) Personal training revenue in the year ended December 31, 2010 includes $2,697 related to unused and expired sessions in three jurisdictions, of which $570 is related to expired sessions that would have been recognized in 2010.

(2) Other ancillary club revenue primarily consists of Small Group Training, Signature Classes, Sports Clubs for Kids, and racquet sports.

(3) Fees and other revenue primarily consist of rental income, marketing revenue and management fees. The year ended December 31, 2013 includes $424 for the correction of an accounting error related to out of period rental income.

Club Format and Locations

Our clubs are generally located in middle- or upper-income residential, commercial, urban and suburban neighborhoods within major metropolitan areas that are capable of supporting the development of a cluster of clubs. Our clubs typically have high visibility and are easily accessible. In the New York metropolitan, Boston, Washington, D.C. and Philadelphia markets, we have created clusters of clubs in urban areas and their commuter suburban areas aligned with our operating strategy of offering our target members the convenience of multiple locations close to where they live and work, reciprocal use privileges, and standardized facilities and services.

Approximately 66% of our existing clubs are fitness-only clubs and the remaining clubs are multi-recreational. Our fitness-only clubs generally range in size from 15,000 to 25,000 square feet and average approximately 21,000 square feet. Our multi-recreational clubs generally range in size from 25,000 to 65,000 square feet, with one club being approximately 200,000 square feet. The average multi-recreational club size is approximately 37,000 square feet. Memberships for each club generally range from 2,000 to 4,500 members at maturity. Our newly introduced BFX Studio will begin to open in the first half of 2014. The BFX Studio will generally range from 7,500 to 10,000 square feet and will consist of three spaces including a cycling studio, group exercise studio and a personal training area.

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Our existing club base consists of clubs which we have developed and constructed as well as clubs we have acquired. Over the past five years from January 1, 2009 to December 31, 2013, we constructed six new clubs while closing or relocating 16 clubs. Currently, 57 of our clubs, or approximately 35% of our existing club base, were from acquisitions of privately owned single and multi-club businesses. In the year ended December 31, 2013, we acquired six clubs and closed four clubs, ending the year with 162 total clubs under operation. This compares to no club openings or closings during the year ended December 31, 2012. In both 2013 and 2012, we also upgraded certain existing clubs and plan to continue to do so in 2014.

To identify potential new club opportunities, we engage in detailed trade area analyses and selection processes. Target areas are identified based upon population demographics, psychographics, traffic and commuting patterns, availability of sites and competitive market information. As part of our club growth strategy we also evaluate potential targeted acquisitions of both single club and multiple club operators in our core markets that would complement our existing club network. In addition, we evaluate growth opportunities in secondary markets located near our existing markets. In the future, we may explore expansion opportunities in other markets in the U.S. that share similar demographic characteristics to those in which we currently operate. We currently have four signed leases in place for club openings expected in 2014 in our Boston and New York regions. We are currently targeting to open a combined four to six NYSC and BSC clubs and two to four new BFX Studio units in 2014. This will bring our total expected unit growth in 2014 to six to 10 units when including the BFX Studio units. We expect construction cost for the traditional clubs to be approximately $2.5 million per club and the BFX Studio is expected to be approximately $1.5 million to $2.25 million per studio.

Our facilities include a mix of state-of-the-art cardiovascular equipment from some of the best manufacturers including Life Fitness®, Cybex®, Precor®, Star Trac®, Hammer®, Woodway® and Octane®. At certain locations, additional amenities are also offered, including swimming pools, racquet and basketball courts, babysitting services, and pro-shops. Personal training services are offered at all locations for an additional charge. In addition, in our continuing efforts to provide our members with the best tools and equipment to take advantage of the latest exercise techniques, in 2012 we began to outfit our clubs with a new UXF training zone which was further rolled out to the majority of our existing club base in 2013 with 126 clubs installed with the UXF zones as of December 31, 2013. The UXF training zone is a training area within the club that features an array of innovative equipment designed to maximize the member s workout. The UXF training zone is approximately 600 to 800 square feet with AstroTurf flooring, a TRX suspension training frame and a variety of functional training equipment. The UXF training zone is open to members for free self guided workouts and UXF fee-based workout programs. The UXF training zone is also used by our personal trainers for their personal training sessions with our members. Our fee-based programs offered at many of our clubs, include personal training, Small Group Training, children s programs, and other signature classes targeting adult members such as VBarre and Pilates Tower. We also offer our Xpressline strength workout at all of our clubs which is provided for free to our members. Xpressline is an eight-station total-body circuit workout designed to be used in 22 minutes and to accommodate all fitness levels.

Our clubs also feature personal entertainment units. The units are typically mounted on or near individual pieces of cardiovascular equipment and are equipped with a flat-panel color screen for television viewing. We believe our members prefer the flexibility to view and listen to the programs of their choice during their cardiovascular workout.

Club Services and Operations

Our clubs are structured to provide an enhanced member experience through effective execution of our operating plan. Our club and support team members are the key to delivering a valued member experience and our operations are organized to maximize their overall effectiveness. Our club operations include:

Management. We believe that our success is largely dependent on the selection and development of our team members. Our management structure is designed to strike the right balance between consistent execution of

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operational excellence and nurturing a leader s capacity for entrepreneurial decision making. Our learning and development system allows for all club positions to receive training on the key elements of their role as well as development training for growth. We believe a critical component to our growth is our ability to leverage internally-developed management talent.

Functional Support. Functional teams provide technical expertise and support designed to drive the member experience and revenue growth in specific areas of our clubs services, including sales and marketing, fitness and ancillary programming, learning and development, as well as facility management and member service.

Driving excellence in fitness and ancillary programming is critical to our success. Members receive an introductory one-hour assessment session with a fitness manager who helps to develop a customized routine that supports the member s fitness goals. This initial assessment session includes a 30-minute workout evaluation, blood pressure and heart rate measurement, body composition analysis, cardio, strength and endurance testing, and movement screening. Members who elect to receive personal training can benefit from one-on-one coaching and guidance, with refreshed programs that evolve as the members achieve their fitness goals. All of our fitness clubs offer our personal training membership products where members can select from a package of one, four, eight, 12 or 16 personal training sessions per month. These sessions must be used in each respective month they are issued. Members who purchase this product commit to a six month period. Members can also purchase prepaid single sessions or multi-session packages which are sold at a premium to the personal training membership product. The personal training membership product provides members with a certified personal trainer who works with the member to create an individualized goal-based program. Our fitness teams are trained to provide superior fitness solutions to address member needs. We believe the qualifications of the personal training staff help to ensure that members receive a consistent level of quality service throughout our clubs and that our personal training programs provide valuable guidance to our members as well as a significant source of incremental revenue for us. We believe that members who participate in personal training programs typically have a longer membership life.

Our commitment to providing a quality exercise experience to our members also includes group exercise programming. Our instructors teach a variety of classes, including dance, cycling, strength conditioning, boxing, yoga, Pilates and step classes. Instructors report through local club management and are further supported by regional managers responsible for ensuring consistency in class content, scheduling, training and instruction. We also provide Small Group Training offerings to our members, which are fee-based programs that have smaller groups, with a maximum of four to eight members per class, and provide more focused and typically more advanced classes. Our fee-based offerings also include our newly launched UXF classes, as well as our signature classes, including VBarre and Power Pilates Tower.

In addition to group exercise, we offer a variety of ancillary programming for children under our Sports Clubs for Kids brand. As of December 31, 2013, Sports Clubs for Kids was being offered in 36 locations throughout our New York Sports Clubs, Boston Sports Clubs and Philadelphia Sports Clubs regions. Our Sports Clubs for Kids programming positions our multi-recreational clubs as family clubs, which we believe provides us with a competitive advantage. Depending upon the facilities available at a location, Sports Clubs for Kids programming can include traditional youth offerings such as day camps, sports camps, swim lessons, hockey and soccer leagues, gymnastics, dance, and birthday parties. It also can include non-competitive learn-to-play sports programs.

Our facilities and equipment management teams are dedicated to ensuring our clubs and fitness equipment are operating at the highest standard of performance for our members. Local teams are deployed to provide on-site support to clubs as needed.

Our club support and member services groups act as a coordinating point for all departments, supporting excellence in program execution and ensuring consistency of policies and procedures across the entire organization that support the member experience.

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Employee Compensation and Benefits

We provide performance-based incentives to our management. Senior management compensation, for example, is tied to our overall performance. Departmental directors, business directors and club level managers can achieve bonuses tied to meeting specific revenue and member retention targets. We offer our employees various benefits including health, dental and disability insurance; pre-tax healthcare, commuting and dependent care accounts; free gym membership; and a 401(k) plan. We believe the availability of employee benefits provides us with a strategic advantage in attracting and retaining quality managers and staff, program instructors and professional personal trainers and that this strategic advantage in turn translates into a more consistent and higher-quality workout experience for those members who utilize such services.

Centralized Information Systems

Our information technology department and its strategies are led by our Senior Vice President, Chief Information Officer, Paul Barron. The year ended December 31, 2013 was the second year of a three year program to replace the current proprietary Club Management system that is used to process new memberships, bill members, check-in members and to track and analyze sales and membership statistics, the frequency and timing of member workouts, cross-club utilization, member life, value-added services and demographic profiles by member. During 2013, we converted the clubs to the new platform for all club related activities with the exception of processing new memberships and collecting membership dues, which continues to be processed under the legacy Club Management system.

In 2013, we introduced My Club as our first member self service web and mobile site which gives our members the freedom of managing their own schedules and booking into classes conveniently online. In 2014, we will enhance this experience and increase the self service capabilities for our members who book their classes online.

We intend to complete the final phase of the multi-year program to replace the legacy Club Management system over the next two years. The final phase will allow for the processing of memberships in the new system with the objective to have this completed by the end of the year. Once this phase is completed, we would then be in a position to remove our current legacy Club Management system and focus on managing a single Club Management system.

Information Technology

We recognize the value of enhancing and extending the uses of information technology (IT) in virtually every area of our business. Our IT strategy is aligned to support our business strategy and operating plans. We maintain an ongoing comprehensive multi-year program to replace or upgrade key systems and to optimize their performance.

In 2013, we upgraded several business applications and IT infrastructure components. Of note was the upgrade of our Oracle Financials application to a higher and more robust version along with a new and more resilient hardware platform. We continue to leverage our investment made in our Virtual Server infrastructure allowing IT to consolidate and better manage costs associated with the provision of server resources to our internal end users.

In the fourth quarter of 2013, we started the migration of our data and voice network from a traditional private network and fixed voice line service to an internet based Virtual Private Network and Cloud IP Voice service. This migration has already been completed in more than half of our clubs and in our call center and will be completed in the remainder of our clubs during 2014. The migration to an internet based Virtual Private Network and a cloud based IP Voice service will allow us to take full advantage of the applications and content hosted in the cloud and not be subject to the limited bandwidth issues we had with the traditional network design.

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We continuously implement infrastructure changes to accommodate growth, provide network redundancy, better manage telecommunications and data costs, increase efficiencies in operations and improve management of all components of our technical architecture, including disaster recovery. Improvements in the IT infrastructure will continue to be made in the future in order to better serve our business needs.

Intellectual Property

We have registered various trademarks and service marks with the U.S. Patent and Trademark Office, including**, NEW YORK SPORTS CLUBS and NYSC**, **WASHINGTON SPORTS CLUBS and WSC**, **BOSTON SPORTS CLUBS and BSC**, **PHILADELPHIA SPORTS CLUBS and PSC, UXF, SPORTS CLUBS FOR KIDS, COMPANIESGETFIT.COM, BFX STUDIO, RIDE REPUBLIC, MASTER CLASS,** and **PRIVATE SESSIONS.** We continue to register other trademarks and service marks. We believe that our rights to these properties are adequately protected.

Competition

The fitness club industry is highly competitive and continues to become more competitive. The number of health clubs in the U.S. has increased from 29,636 in 2007 to 30,500 in 2012, based on the most recent information available according to the IHRSA. In each of the markets in which we operate, we compete with other fitness clubs, physical fitness and recreational facilities.

We consider the following groups to be our primary competitors in the health and fitness industry:

- commercial, multi-recreational and fitness-only chains, including, among others, Equinox Holdings, Inc., Lifetime Fitness, Inc., Crunch, New York Health and Racquet, LA Fitness International LLC, Sports Club/LA, 24 Hour Fitness Worldwide, Inc., Bally Total Fitness Holding Corporation, Gold s Gym International, Inc., Retro Fitness, Snap Fitness, Anytime Fitness and Planet Fitness;

- private studios, including, among others, Flywheel, Soul Cycle, Barry s Bootcamp and Cross-Fit, as well as other private studios offering cycling, yoga or Pilates;

- the YMCA and similar non-profit organizations;

- physical fitness and recreational facilities established by local governments, hospitals and businesses;

- exercise and small fitness clubs; racquet, tennis and other athletic clubs;
amenity gyms in apartments, condominiums and offices;

- weight-reducing salons;

- country clubs; and

- the home-use fitness equipment industry.

The principal methods of competition include pricing and ease of payment, required level of members contractual commitment, level and quality of services, training and quality of supervisory staff, size and layout of facility and convenience of location with respect to access to transportation and pedestrian traffic.

Competitive Position Measured by Number of Clubs

Market	Number of Clubs	Position
Boston metropolitan	29	Leading owner and operator
New York metropolitan	108	Leading owner and operator
Philadelphia metropolitan	6	#3 owner and operator, #2 in urban center
Washington, D.C. metropolitan	16	#3 owner and operator, #1 in urban center
Switzerland	3	Local owner and operator only

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We consider our traditional service offerings to be in the mid-tier of the value/service proposition and designed to appeal to a large portion of the population who utilize fitness facilities. The number of competitor clubs that offer lower pricing and a lower level of service have continued to grow in our markets over the last few years. These clubs have attracted, and may continue to attract, members away from both our fitness-only clubs and our multi-recreational clubs.

We also face competition from club operators offering comparable or higher pricing with higher levels of service. Larger outer-suburban family fitness centers, in areas where suitable real estate is more likely to be available, could also compete effectively against our suburban formats.

Also, we face competition from the rising popularity and demand for private studios offering niche boutique experiences. As a means of growing and expanding our business, we are planning to launch our own private studio concept, the BFX Studio, set to open in the first half of 2014. This three-dimension luxury studio brand will take advantage of the rise in consumer demand for studio experiences and will have a higher membership pricing point versus our traditional clubs.

We also compete with other entertainment and retail businesses for the discretionary income in our target demographics. There can be no assurance that we will be able to compete effectively in the future in the markets in which we operate. Competitors, who may include companies that are larger and have greater resources than us, may enter these markets to our detriment. These competitive conditions may limit our ability to increase dues without a material loss in membership, attract new members and attract and retain qualified personnel. Additionally, consolidation in the fitness club industry could result in increased competition among participants, particularly large multi-facility operators that are able to compete for attractive acquisition candidates and/or newly constructed club locations. This increased competition could increase our costs associated with expansion through both acquisitions and for real estate availability for newly constructed club locations.

We believe that our market leadership, experience and operating efficiencies enable us to provide the consumer with a superior product in terms of convenience, quality service and affordability. We believe that there are barriers to entry in our metropolitan areas, including restrictive zoning laws, lengthy permit processes and a shortage of appropriate real estate, which could discourage any large competitor from attempting to open a chain of clubs in these markets. However, such a competitor could enter these markets more easily through one, or a series of, acquisitions. These barriers of entry are significant in our four metropolitan regions; however, they are not as challenging in our surrounding suburban locations.

Seasonality of Business

Seasonal trends have a limited effect on our overall business. Generally, we experience greater membership growth at the beginning of each year and experience an increased rate of membership attrition during the summer months. In addition, during the summer months, we experience a slight increase in operating expenses due to our outdoor pool and summer camp operations, generally matched by seasonal revenue recognition from season pool memberships and camp revenue.

Government Regulation

Our operations and business practices are subject to federal, state and local government regulation in the various jurisdictions in which our clubs are located, including general rules and regulations of the Federal Trade Commission, state and local consumer protection agencies and state statutes that prescribe certain forms and provisions of membership contracts and that govern the advertising, sale, financing and collection of such memberships as well as state and local health regulations.

Statutes and regulations affecting the fitness industry have been enacted in jurisdictions in which we conduct business and other states into which we may expand in the future have adopted or may adopt similar legislation. Typically, these statutes and regulations prescribe certain forms and provisions of membership contracts, afford members the right to cancel the contract within a specified time period after signing or in certain circumstances, such as for medical reasons or relocation to a certain distance from the nearest club, require an escrow of funds received from pre-opening sales or the posting of a bond or proof of financial responsibility and may establish maximum prices for membership contracts and limitations on the term of contracts. The specific procedures and reasons for cancellation vary due to differing laws in the respective jurisdictions, but in each instance, the canceling member is entitled to a refund of unused prepaid amounts. In addition, several states have proposed legislation that would prohibit the automatic rollover of membership once a member s commitment period expires. We are also subject to numerous other types of federal and state regulations governing the sale of memberships. These laws and regulations are subject to varying interpretations by a number of state and federal enforcement agencies and courts. We maintain internal review procedures to comply with these requirements and believe that our activities are in substantial compliance with all applicable statutes, rules and decisions.

The tax treatment of membership dues varies by state. Some states in which we operate require sales tax to be collected on membership dues and personal training sessions. Several others states in which we operate have proposed similar tax legislation. These taxes have the effect of increasing the payments by our members, which could impede our ability to attract new members or induce members to cancel their membership.

Changes in any statutes, rules or regulations could have a material adverse effect on our financial condition and results of operations.

Employees

On December 31, 2013, we had approximately 7,800 employees, of whom approximately 3,400 were employed full-time. Approximately 430 of those employees were corporate and other club support personnel. We are not a party to any collective bargaining agreement with our employees. We operate with an open door policy and encourage and welcome the communication of our employees ideas, suggestions and concerns, and believe this strengthens our employee relations. We have never experienced any significant labor shortages or had any difficulty in obtaining adequate replacements for departing employees. We consider our relations with our employees to be good.

Available Information

We make available through our web site at *http://investor.mysportsclubs.com/* in the Investor Relations SEC Filings section, free of charge, all reports and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the Exchange Act), as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission (the SEC). Occasionally, we may use our web site as a channel of distribution of material company information. Financial and other material information regarding the Company is routinely posted on and accessible at http://investor.mysportsclubs.com/. In addition, you may automatically receive email alerts and other information about us by enrolling your email by visiting the E-mail Alerts section at http://investor.mysportsclubs.com/.

The foregoing information regarding our website and its content is for convenience only. The content of our website is not deemed to be incorporated by reference into this report nor should it be deemed to have been filed with the SEC.

Item 1A. ***Risk Factors***

Investors should carefully consider the risks described below and all other information in this Annual Report on Form 10-K. The risks and uncertainties described below are not the only ones that we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also impair our business and operations. If any of the following risks actually occur, our business, financial condition, cash flows or results of operations could be materially adversely affected.

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Risks Related to Our Business

We may be unable to attract and retain members, which could have a negative effect on our business.

The performance of our clubs is highly dependent on our ability to attract and retain members, and we may not be successful in these efforts. Most of our members hold month-to-month memberships and accordingly, most members can cancel their club membership at any time without penalty. In addition, we experience attrition and must continually engage existing members and attract new members in order to maintain our membership levels and ancillary sales. There are numerous factors that have in the past and could in the future lead to a decline in membership levels or that could prevent us from increasing our membership, including a decline in our ability to deliver quality service at a competitive cost, the presence of direct and indirect competition in the areas in which the clubs are located, the public s interest in fitness clubs and general economic conditions. In order to increase membership levels, we may from time to time offer lower membership rates and joining fees. Any decrease in our average membership rates or reductions in joining fees may adversely impact our results of operations.

Negative economic conditions, including increased unemployment levels and decreased consumer confidence, have in the past contributed to and in the future could lead to significant pressures and declines in economic growth, including reduced consumer spending. In a depressed economic and consumer environment, consumers and businesses may postpone spending in response to tighter credit, negative financial news and/or declines in income or asset values, which could have a material negative effect on the demand for our services and products and such decline in demand may continue as the economy continues to struggle and disposable income declines. Other factors that could influence demand include increases in fuel and other energy costs, conditions in the residential real estate and mortgage markets, labor and healthcare costs, access to credit, consumer confidence and other macroeconomic factors affecting consumer spending behavior. We believe the challenges to the global economy during the past several years have adversely affected our business and our revenues and profits and continuing challenges may result in additional adverse effects. As a result of these factors, membership levels might not be adequate to maintain our operations at current levels or permit the expansion of our operations.

In addition, to the extent our corporate clients are adversely affected by negative economic conditions, they may decide, as part of expense reduction strategies, to curtail or cancel club membership benefits provided to their respective employees. Any reductions in corporate memberships may lead to membership cancellations as we cannot assure that employees of corporate customers will choose to continue their memberships without employer subsidies. A decline in membership levels may have a material adverse effect on our business, financial condition, results of operations and cash flows.

Low consumer confidence levels, increased competition and decreased spending could negatively impact our financial position and result in club closures and fixed asset and goodwill impairments.

In the year ended December 31, 2013, we closed four clubs, while in 2012 we did not have any club closures. We recognized $714,000 of fixed asset impairments in the year ended December 31, 2013 compared to $3.4 million of fixed asset impairments in the year ended December 31, 2012. The $3.4 million of fixed asset impairments in 2012 included $3.2 million related to fixed asset write-offs at four clubs sustaining damages from Hurricane Sandy. While there were no goodwill impairments in 2013 and 2012, we have experienced goodwill impairments in the past, in part due to decreased membership. Some of our past club closures and impairments were due, in large part, to the economic and consumer environment, and increased competition in areas in which our clubs operate. If the economic and consumer environment were to deteriorate or not improve or if we are unable to improve the overall competitive position of our clubs, our operating performance may experience declines and we may need to recognize additional impairments of our fixed assets and goodwill and may be compelled to close additional clubs. In addition, we cannot ensure that we will be able to replace any of the revenue lost from these closed clubs from our other club operations.

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Our geographic concentration heightens our exposure to adverse regional developments.

As of December 31, 2013, we operated 108 fitness clubs in the New York metropolitan market, 29 fitness clubs in the Boston market, 16 fitness clubs in the Washington, D.C. market, six fitness clubs in the Philadelphia market and three fitness clubs in Switzerland. Our geographic concentration in the Northeast and Mid-Atlantic regions and, in particular, the New York metropolitan area, heightens our exposure to adverse developments in these areas, including those related to economic and demographic changes in these regions, competition and severe weather or other unforeseen events, such as hurricanes. For example, in the year ended December 31, 2012, as a result of flooding and power outages caused by Hurricane Sandy, 131 clubs were closed on October 29, 2012, with one club that closed permanently, 16 clubs that remained closed for over a week and one club that was closed for over a year and recently reopened in December 2013. We cannot predict the impact that any future severe weather events will have on our ability to avoid wide-spread or prolonged club closures. Any such events affecting the areas in which we operate might result in a material adverse effect on our business, financial condition, cash flows and results of operations in the future.

The level of competition in the fitness club industry could negatively impact our revenue growth and profitability.

The fitness club industry is highly competitive and continues to become more competitive. In each of the markets in which we operate, we compete with other fitness clubs, private studios, physical fitness and recreational facilities established by local governments, hospitals and businesses for their employees, amenity and condominium clubs, the YMCA and similar organizations and, to a certain extent, with racquet and tennis and other athletic clubs, country clubs, weight reducing salons and the home-use fitness equipment industry. We also compete with other entertainment and retail businesses for the discretionary income in our target demographics. We might not be able to compete effectively in the future in the markets in which we operate. Competitors include companies that are larger and have greater resources than us and also may enter these markets to our detriment. These competitive conditions may limit our ability to increase dues without a material loss in membership, attract new members and attract and retain qualified personnel. Additionally, consolidation in the fitness club industry could result in increased competition among participants, particularly large multi-facility operators that are able to compete for attractive acquisition candidates or newly constructed club locations, thereby increasing costs associated with expansion through both acquisitions and lease negotiation and real estate availability for newly constructed club locations.

The number of competitor clubs that offer lower pricing and a lower level of service continue to grow in our markets. These clubs have attracted, and may continue to attract, members away from both our fitness-only clubs and our multi-recreational clubs, particularly in the current consumer environment. Furthermore, smaller and less expensive weight loss facilities present a competitive alternative for consumers.

We also face competition from competitors offering comparable or higher pricing with higher levels of service or offerings. Larger outer-suburban, multi-recreational family fitness centers, in areas where suitable real estate is more likely to be available, also compete against our suburban, fitness-only models.

We also face competition from the increased popularity and demand for private studios offering group exercise classes. The prevalence of these smaller studios may compete against our own studio type offerings, such as cycling, Yoga and Pilates, as well as our new BFX Studio, as consumers may opt to use these competing studios to fulfill their fitness needs.

In addition, large competitors could enter the urban markets in which we operate to open a chain of clubs in these markets through one, or a series of, acquisitions.

Our trademarks and trade names may be infringed, misappropriated or challenged by others.

We believe our brand names and related intellectual property are important to our continued success. We seek to protect our trademarks, trade names and other intellectual property by exercising our rights under applicable trademark and copyright laws. If we were to fail to successfully protect our intellectual property rights for any reason, it could have an adverse effect on our business, results of operations and financial condition. Any damage to our reputation could cause membership levels to decline and make it more difficult to attract new members.

If we are unable to identify and acquire suitable sites for new clubs, our revenue growth rate and profits may be negatively impacted.

To successfully expand our business over the long term, we must identify and acquire sites that meet our site selection criteria. In addition to finding sites with the right geographical, demographic and other measures we employ in our selection process, we also need to evaluate the penetration of our competitors in the market. We face competition from other health and fitness center operators for sites that meet our criteria and as a result, we may lose those sites or we could be forced to pay higher prices for those sites. If we are unable to identify and acquire sites for new clubs on attractive terms, our revenue, growth rate and profits may be negatively impacted. Additionally, if our analysis of the suitability of a site is incorrect, we may not be able to recover our capital investment in developing and building the new club.

The opening of new clubs by us in existing markets may negatively impact our comparable club revenue growth and our operating margins.

We currently operate clubs throughout the Northeast and Mid-Atlantic regions of the United States. In the case of existing markets, our experience has been that opening new clubs may attract some memberships away from other clubs already operated by us in those markets and diminish their revenues. In addition, as a result of new club openings in existing markets and because older clubs will represent an increasing proportion of our club base over time, our mature club revenue increases may be lower in future periods than in the past.

Another result of opening new clubs is that our club operating margins may be lower than they have been historically while the clubs build a membership base. We expect both the addition of pre-opening expenses and the lower revenue volumes characteristic of newly opened clubs to affect our club operating margins at these new clubs.

We may experience prolonged periods of losses in our recently opened clubs.

Upon opening a club, we typically experience an initial period of club operating losses. Enrollment from pre-sold memberships typically generates insufficient revenue for the club to initially generate positive cash flow. As a result, a new club typically generates an operating loss in its first full year of operations and substantially lower margins in its second full year of operations than a club opened for more than 24 months. These operating losses and lower margins will negatively impact our future results of operations. This negative impact will be increased by the initial expensing of pre-opening costs, which include legal and other costs associated with lease negotiations and permitting and zoning requirements, as well as depreciation and amortization expenses, which will further negatively impact our results of operations. We may, at our discretion, accelerate or expand our plans to open new clubs, which may adversely affect results from operations.

We are subject to government regulation, and changes in these regulations could have a negative effect on our financial condition and results of operations.

Our operations and business practices are subject to federal, state and local government regulation in the various jurisdictions in which our clubs are located, including, but not limited to the following:

- general rules and regulations of the Federal Trade Commission;
- rules and regulations of state and local consumer protection agencies;
- state statutes that prescribe certain forms and provisions of membership contracts

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- state statutes that govern the advertising, sale, financing and collection of memberships;
- federal and state laws and regulations governing privacy and security of information; and
- state and local health regulations

Any changes in such laws or regulations could have a material adverse effect on our financial condition and results of operations.

We could be subject to claims related to health or safety risks at our clubs.

Use of our clubs poses some potential health or safety risks to members or guests through physical exertion and use of our services and facilities, including exercise equipment. Claims might be asserted against us for injury suffered by, or death of members or guests while exercising at a club. We might not be able to successfully defend such claims. As a result, we might not be able to maintain our general liability insurance on acceptable terms in the future or maintain a level of insurance that would provide adequate coverage against potential claims.

Depending upon the outcome, these matters may have a material effect on our consolidated financial position, results of operations and cash flows.

Security and privacy breaches may expose us to liability and cause us to lose customers.

Federal and state law requires us to safeguard our customers financial information, including credit card information. Although we have established security procedures and protocol, including credit card industry compliance procedures, to protect against identity theft and the theft of our customers financial information, our security and testing measures may not prevent security breaches and breaches of our customers privacy may occur, which could harm our business. For example, a significant number of our users provide us with credit card and other confidential information and authorize us to bill their credit card accounts directly for our products and services. Typically, we rely on encryption and authentication technology licensed from third parties to enhance transmission security of confidential information. Advances in computer capabilities, new discoveries in the field of cryptography, inadequate facility security or other developments may result in a compromise or breach of the technology used by us to protect customer data. Any compromise of our security or noncompliance with privacy or other laws or requirements could harm our reputation or financial condition and, therefore, our business. In addition, a party who is able to circumvent our security measures or exploit inadequacies in our security measures, could, among other effects, misappropriate proprietary information, cause interruptions in our operations or expose members to computer viruses or other disruptions. Actual or perceived vulnerabilities may lead to claims against us. To the extent the measures we have taken prove to be insufficient or inadequate, we may become subject to litigation or administrative sanctions, which could result in significant fines, penalties or damages and harm to our reputation.

Loss of key personnel and/or failure to attract and retain highly qualified personnel could make it more difficult for us to develop our business and enhance our financial performance.

We are dependent on the continued services of our senior management team, including our Chief Executive Officer, Robert Giardina, our President, Chief Operating Officer and Chief Financial Officer, Daniel Gallagher, and our Senior Vice President, Chief Information Officer, Paul Barron. We believe the loss of such key personnel could have a material adverse effect on us and our financial performance. Currently, we do not have any long-term employment agreements with our executive officers, and we may not be able to attract and retain sufficient qualified personnel to meet our business needs.

Terrorism and the uncertainty of armed conflicts may have a material adverse effect on clubs and our operating results.

Terrorist attacks, such as the attacks that occurred in New York City and Washington, D.C. on September 11, 2001, and other acts of violence or war may affect the markets in which we operate, our operating results or the market on which our common stock trades. Our geographic concentration in the major cities in the Northeast and Mid-Atlantic regions and, in particular, the New York City and Washington, D.C. areas, heightens our exposure to any such future terrorist attacks, which may adversely affect our clubs and result in a decrease in our revenues. The potential near-term and long-term effect these attacks may have for our members, the markets for our services and the market for our common stock are uncertain; however, their occurrence can be expected to further negatively affect the U.S. economy generally and specifically the regional markets in which we operate. The consequences of any terrorist attacks or any armed conflicts are unpredictable; and we may not be able to foresee events that could have an adverse effect on our business.

Disruptions and failures involving our information systems could cause customer dissatisfaction and adversely affect our billing and other administrative functions.

The continuing and uninterrupted performance of our information systems is critical to our success. We use a fully-integrated information system to process new memberships, bill members, check-in members and track and analyze sales and membership statistics, the frequency and timing of member workouts, cross-club utilization, member life, value-added services and demographic profiles by member. This system also assists us in evaluating staffing needs and program offerings. We believe that, without investing in enhancements, this system was approaching the end of its life cycle. Thus, in 2011, we began the process of replacing this system with a new system through a multi-year phase in implementation program which is expected to be completed over the next two years. Correcting any disruptions or failures that affect our proprietary system or the new system, as it is implemented, could be difficult, time-consuming and expensive because we would need to use contracted consultants familiar with our system.

Any failure of our current system could also cause us to lose members and adversely affect our business and results of operations. Our members may become dissatisfied by any systems disruption or failure that interrupts our ability to provide our services to them. Disruptions or failures that affect our billing and other administrative functions could have an adverse effect on our operating results.

Infrastructure changes are being undertaken to accommodate our growth, provide network redundancy, better manage telecommunications and data costs, increase efficiencies in operations and improve management of all components of our technical architecture. Fire, floods, earthquakes, power loss, telecommunications failures, break-ins, acts of terrorism and similar events could damage our systems. In addition, computer viruses, electronic break-ins or other similar disruptive problems could also adversely affect our sites. Any system disruption or failure, security breach or other damage that interrupts or delays our operations could cause us to lose members, damage our reputation, and adversely affect our business and results of operations.

Our growth could place strains on our management, employees, information systems and internal controls, which may adversely impact our business.

Future expansion will place increased demands on our administrative, operational, financial and other resources. Any failure to manage growth effectively could seriously harm our business. To be successful, we will need to continue to improve management information systems and our operating, administrative, financial and accounting systems and controls. We will also need to train new employees and maintain close coordination among our executive, accounting, finance, marketing, sales and operations functions. These processes are time-consuming and expensive, increase management responsibilities and divert management attention.

Our cash and cash equivalents are concentrated in a small number of banks.

Our cash and cash equivalents are held, primarily, in a small number of commercial banks. These deposits are not collateralized. In the event these banks become insolvent, we would be unable to recover most of our cash and cash equivalents deposited at the banks. Cash and cash equivalents held in a small number of commercial banks as of December 31, 2013 totaled $72.9 million. During 2013, in any one month, this amount has been as high as approximately $82.0 million.

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Regulatory changes in the terms of credit and debit card usage, including any existing or future regulatory requirements, could have an adverse effect on our business.

Our business relies heavily on the use of credit and debit cards in sales transactions. Regulatory changes to existing rules or future regulatory requirements affecting the use of credit and debit cards or the fees charged could impact the consumer and financial institutions who provide card services. This may lead to an adverse impact on our business if the regulatory changes result in unfavorable terms to either the consumer or the banking institutions.

Because of the capital-intensive nature of our business, we may have to incur additional indebtedness or issue new equity securities and, if we are not able to obtain additional capital, our ability to operate or expand our business may be impaired and our results of operations could be adversely affected.

Our business requires significant levels of capital to finance the development of additional sites for new clubs and the construction of our clubs. If cash from available sources is insufficient or unavailable due to restrictive credit markets, or if cash is used for unanticipated needs, we may require additional capital sooner than anticipated. In the event that we are required or choose to raise additional funds, we may be unable to do so on favorable terms or at all. Furthermore, the cost of debt financing could significantly increase, making it cost-prohibitive to borrow, which could force us to issue new equity securities. If we issue new equity securities, existing shareholders may experience additional dilution or the new equity securities may have rights, preferences or privileges senior to those of existing holders of common stock. If we cannot raise funds on acceptable terms, we may not be able to execute our current growth plans, take advantage of future opportunities or respond to competitive pressures. Any inability to raise additional capital when required could have an adverse effect on our business plans and operating results.

We may incur rising costs related to construction of new clubs and maintaining our existing clubs. If we are not able to pass these cost increases through to our members, our returns may be adversely affected.

Our clubs require significant upfront investment. If our investment is higher than we had planned, we may need to outperform our operational plan to achieve our targeted return. We cannot assure that we can offset cost increases by increasing our membership dues and other fees and improving profitability through cost efficiencies.

We may be required to remit unclaimed property to states for unused, expired personal training sessions.

We recognize revenue from personal training sessions as the services are performed (i.e., when the session is trained). Unused personal training sessions expire after a set, disclosed period of time after purchase and are not refundable or redeemable by the member for cash. The State of New York has informed us that it is considering whether we are required to remit the amount received by us for unused, expired personal training sessions to the State of New York as unclaimed property. As of December 31, 2013, we had approximately $14.3 million of unused and expired personal training sessions that had not been recognized as revenue and was recorded as deferred revenue. We do not believe that these amounts are subject to the escheatment or abandoned property laws of any jurisdiction, including the State of New York. However, it is possible that one or more of these jurisdictions may not agree with our position and may claim that we must remit all or a portion of these amounts to such jurisdiction. This could have a material adverse effect on our cash flows.

Our growth and profitability could be negatively impacted if we are unable to renew or replace our current club leases on favorable terms, or at all, and we cannot find suitable alternate locations.

We currently lease substantially all of our fitness club locations pursuant to long-term leases (generally 15 to 20 years, including option periods). During the next five years, or the period from January 1, 2014 through December 31, 2018, we have leases for 24 club locations that are due to expire without any renewal options, two of which expire in 2014, and 48 club locations that are due to expire with renewal options. For leases with renewal options, several of them provide for our unilateral option to renew for additional rental periods at

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specific rental rates (for example, based on the consumer price index or stated renewal terms already set in the leases) or based on the fair market rate at the location. Our ability to negotiate favorable terms on an expiring lease or to negotiate favorable terms on leases with renewal options, or conversely for a suitable alternate location, could depend on conditions in the real estate market, competition for desirable properties and our relationships with current and prospective landlords or may depend on other factors that are not within our control. Any or all of these factors and conditions could negatively impact our revenue, growth and profitability.

Failure to complete the sale of the property at East 86th Street in New York may negatively impact the price of our common stock.

We have announced the entry into an agreement to sell our property located at East 86th Street in New York for a price of approximately $82 million, subject to adjustment, and we expect the sale to close on or about March 31, 2014. If we are unable to close the sale of the property on such terms, we may be unable to identify other potential purchasers for such property at a similar price or on terms acceptable to us, which may negatively impact the price of our common stock.

There can be no guarantee that we will continue to declare dividends on our common stock.

In November 2013, we initiated a quarterly cash dividend payment on our common stock. Any determination to continue to declare cash dividends on our common stock will be based primarily upon our financial condition, including availability of cash-on-hand, results of operations, debt repayment requirements and business capital requirements, including capital expenditures and acquisitions, the board of directors continuing determination that the declaration of dividends are in the best interests of our stockholders and are in compliance with all laws and agreements applicable to dividend programs. For example, the ability of our subsidiaries, including TSI, LLC, to make distributions to us is limited by the terms of our existing senior secured credit facility, as described below. Accordingly, our ability to obtain cash to declare dividends is subject, in part, to such limitation. In the event we do not declare a quarterly dividend, our stock price could be adversely affected.

Risks Related to Our Leverage and Our Indebtedness

On November 15, 2013, TSI, LLC entered into a $370.0 million senior secured credit facility (2013 Senior Credit Facility). The 2013 Senior Credit Facility consists of a $325.0 million term loan facility (2013 Term Loan Facility), and a $45.0 million revolving loan facility (2013 Revolving Loan Facility). The 2013 Term Loan Facility matures on November 15, 2020, and the 2013 Revolving Loan Facility matures on November 15, 2018.

We may be negatively affected by economic conditions in the U.S. and key international markets.

We must maintain liquidity to fund our working capital, service our outstanding indebtedness and finance investment opportunities. Without sufficient liquidity, we could be forced to curtail our operations or we may not be able to pursue new business opportunities. The principal sources of our liquidity are funds generated from operating activities, available cash and cash equivalents and borrowings under our $45.0 million 2013 Revolving Loan Facility. If our current resources do not satisfy our liquidity requirements, we may have to seek additional financing.

Economic conditions, both domestic and foreign, may affect our financial performance. Prevailing economic conditions, including unemployment levels, inflation, availability of credit, energy costs and other macro-economic factors, as well as uncertainty about future economic conditions, adversely affect consumer spending and, consequently, our business and results of operations.

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Our leverage may impair our financial condition, and we may incur significant additional debt.

We currently have a substantial amount of debt. As of December 31, 2013, our total outstanding consolidated debt was $325.0 million. In addition, as of December 31, 2013, we had $42.0 million of unutilized borrowings, net of $3.0 million of letters of credit, under our 2013 Revolving Loan Facility. Our substantial debt could have important consequences, including:

- making it more difficult for us to satisfy our obligations with respect to our outstanding indebtedness;

- increasing our vulnerability to general adverse economic and industry conditions;

- limiting our ability to obtain additional financing to fund future working capital, capital expenditures, acquisitions of clubs and other general corporate requirements;

- requiring a substantial portion of our cash flow from operations for the payment of interest on our debt, which is variable on our 2013 Revolving Loan Facility and partially variable on our 2013 Term Loan Facility, and/or principal pursuant to excess cash flow requirements and reducing our ability to use our cash flow to fund working capital, capital expenditures and acquisitions of new clubs and general corporate requirements;

- increasing our vulnerability to interest rate fluctuations in connection with borrowings under our 2013 Senior Credit Facility, some of which are at variable interest rates;

- limiting our ability to refinance our existing indebtedness on favorable terms, or at all; and

- limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate.

These limitations and consequences may place us at a competitive disadvantage to other less-leveraged competitors.

If new debt is added to our and our subsidiaries current debt levels, the related risks that we and they currently face could intensify.

The current debt under the 2013 Senior Credit Facility has a floating interest rate and an increase in interest rates may negatively impact our financial results.

Interest rates applicable to our debt are expected to fluctuate based on economic and market factors that are beyond our control. In particular, the unhedged portion of $165.0 million, of our outstanding debt under our 2013 Senior Credit Facility has a floating interest rate. Any significant increase in market interest rates, and in particular the short-term Eurodollar rates, would result in a significant increase in interest expense on our debt, which could negatively impact our net income and cash flows.

The Company may be unsuccessful in its efforts to effectively hedge against interest rate changes on our variable rate debt .

In its normal operations, the Company is exposed to market risk relating to fluctuations in interest rates. In order to minimize the negative impact of such fluctuations on the Company s cash flows, the Company may enter into derivative financial instruments, such as interest rate swaps. The Company s current interest rate swap arrangement is with one financial institution and covers $160.0 million of our current $325.0 million outstanding term loan principal balance with the swap expiring on May 15, 2018. We are exposed to credit risk if the counterparty to the agreement is not able to perform on its obligations. Additionally, a failure on our part to effectively hedge against interest rate changes may adversely affect our financial condition and results of operations. We are required to record the interest rate swap at its fair value. Changes in interest rates can significantly impact the valuation of the instrument resulting in non-cash changes to our financial position.

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Covenant restrictions under our indebtedness may limit our ability to operate our business and, in such an event, we may not have sufficient assets to settle our indebtedness.

Our 2013 Senior Credit Facility and the agreements related thereto contain, among other things, covenants that may restrict our ability to finance future operations or capital needs or to engage in other business activities and that may impact our ability and the ability of our restricted subsidiaries to:

- incur debt;
- pay dividends or make distributions;
- purchase or redeem stock;
- make investments and extend credit;
- engage in transactions with affiliates;
- engage in sale-leaseback transactions;
- consummate certain asset sales;
- effect a consolidation or merger or sell, transfer, lease or otherwise dispose of all or substantially all of our assets; and
- create liens on our assets.

The 2013 Senior Credit Facility provides for a financial covenant in the situation where the utilization of the revolving loan commitments (other than letters of credit up to $5,500,000 at any time outstanding) exceeds 25% of the commitment. In such event, our subsidiaries are required to maintain a total leverage ratio of no greater than 4.50:1.00. Our subsidiaries were not subject to this covenant as of December 31, 2013 since their total revolving loan commitments, other than letters of credit outstanding, did not exceed 25% of the total revolver. This covenant may require us to take action to reduce our debt or act in a manner contrary to our business objectives.

Events beyond our control, including changes in general economic and business conditions, may affect our ability to meet certain financial ratios under the 2013 Senior Credit Facility. We may be unable to meet those tests and the lenders may decide not to waive any failure to meet those tests. A failure to satisfy these tests could limit our ability to obtain funds to pay dividends or cause a default under the 2013 Senior Credit Facility. If an event of default under the 2013 Senior Credit Facility occurs, the lenders could elect to declare all amounts outstanding thereunder, together with accrued interest, to be immediately due and payable. If any such event should occur, we might not have sufficient assets to pay our indebtedness and meet our other obligations, which would have a material adverse effect on our business, financial condition and results of operations.

Item 1B. *Unresolved Staff Comments*

None

Item 2. *Properties*

We own our 151 East 86th Street, New York location, which houses a fitness club and a retail tenant that generated approximately $2.0 million of rental income for us for the year ended December 31, 2013.

On December 24, 2013 we announced the entry into an agreement to sell the property located at 151 East 86th Street, New York to an affiliate of Stillman Development International, LLC for a price of $82 million, subject to certain adjustments. The transaction is subject to various closing conditions, and the parties expect the transaction to be completed on or about March 31, 2014. In connection with the sale of the property, we will continue to operate our NYSC health and fitness club at this location under a lease with the purchaser of the

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property. After a period of not less than two years, the purchaser, upon prior notice, may exercise its right to terminate the lease in order to commence the demolition of the premises and the currently adjacent property under which the purchaser has entered into a long-term ground lease, and the construction of a new high-rise multi-use property. The parties have agreed to enter into a new lease for a health and fitness club space to be located at the same location as the current fitness club following completion of development of the new high-rise building.

We lease the remainder of our fitness clubs pursuant to long-term leases (generally 15 to 20 years, including options). In the next five years, or the period from January 1, 2014 through December 31, 2018, we have leases for 24 club locations that are due to expire without any renewal options, two which are due to expire in 2014, and 48 club locations that are due to expire with renewal options. Renewal options include terms for rental increases based on the consumer price index, fair market rates or stated renewal terms already set in the lease agreements.

We lease approximately 26,400 square feet of office space in New York City and have smaller regional offices in Fairfax, VA and Boston, MA, for administrative and general corporate purposes.

We lease approximately 82,000 square feet in Elmsford, NY for the operation of a centralized laundry facility for New York Sports Clubs offering towel service, and for construction and equipment storage. This space also serves as corporate office space. Total square footage related to the laundry facility is 42,000 and total square footage related to the corporate office and warehouse space is 40,000.

The following table provides information regarding our club locations:

Location	Address	Date Opened or Management Assumed
New York Sports Clubs:		
Manhattan	151 East 86th Street	January 1977
Manhattan	61 West 62nd Street	July 1983
Manhattan	614 Second Avenue	July 1986
Manhattan	151 Reade Street	January 1990
Manhattan	1601 Broadway	September 1991
Manhattan	349 East 76th Street	April 1994
Manhattan	248 West 80th Street	May 1994
Manhattan	502 Park Avenue	February 1995
Manhattan	117 Seventh Avenue South	March 1995
Manhattan	303 Park Avenue South	December 1995
Manhattan	30 Wall Street	May 1996
Manhattan	1635 Third Avenue	October 1996
Manhattan	575 Lexington Avenue	November 1996
Manhattan	278 Eighth Avenue	December 1996
Manhattan	200 Madison Avenue	February 1997
Manhattan	2162 Broadway	November 1997
Manhattan	633 Third Avenue	April 1998
Manhattan	217 Broadway	March 1999
Manhattan	23 West 73rd Street	April 1999
Manhattan	34 West 14th Street	July 1999
Manhattan	503-511 Broadway	July 1999
Manhattan	1372 Broadway	October 1999
Manhattan	300 West 125th Street	May 2000
Manhattan	19 West 44th Street	August 2000
Manhattan	128 Eighth Avenue	December 2000
Manhattan	2527 Broadway	August 2001

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Location	Address	Date Opened or Management Assumed
Manhattan	3 Park Avenue	August 2001
Manhattan	10 Irving Place	November 2001
Manhattan	230 West 41st Street	November 2001
Manhattan	1221 Avenue of the Americas	January 2002
Manhattan	200 Park Avenue	December 2002
Manhattan	232 Mercer Street	September 2004
Manhattan	225 Varick Street	August 2006
Manhattan	885 Second Avenue	February 2007
Manhattan	301 West 145th Street	October 2007
Manhattan	1400 5th Avenue	December 2007
Manhattan	75 West End Avenue	April 2013
Manhattan	28-30 Avenue A	Future opening
Bronx, NY	1601 Bronxdale Avenue	November 2007
Brooklyn, NY	110 Boerum Place	October 1985
Brooklyn, NY	1736 Shore Parkway	June 1998
Brooklyn, NY	179 Remsen Street	May 2001
Brooklyn, NY	324 Ninth Street	August 2003
Brooklyn, NY	1630 E 15th Street	August 2007
Brooklyn, NY	7118 Third Avenue	May 2004
Brooklyn, NY	439 86th Street	April 2008
Brooklyn, NY	242 Bedford Avenue	Future opening
Brooklyn, NY	147 Greenpoint Avenue	Future opening
Queens, NY	69-33 Austin Street	April 1997
Queens, NY	153-67 A Cross Island Parkway	June 1998
Queens, NY	2856-2861 Steinway Street	February 2004
Queens, NY	8000 Cooper Avenue	March 2007
Queens, NY	99-01 Queens Boulevard	June 2007
Queens, NY	39-01 Queens Blvd	December 2007
Staten Island, NY	300 West Service Road	June 1998
Scarsdale, NY	696 White Plains Road	October 1995
Mamaroneck, NY	124 Palmer Avenue	January 1997
Croton-on-Hudson, NY	420 South Riverside Drive	January 1998
Larchmont, NY	15 Madison Avenue	December 1998
Nanuet, NY	58 Demarest Mill Road	May 1998
Great Neck, NY	15 Barstow Road	July 1989
East Meadow, NY	625 Merrick Avenue	January 1999
Commack, NY	6136 Jericho Turnpike	January 1999
Oceanside, NY	2909 Lincoln Avenue	May 1999
Long Beach, NY	265 East Park Avenue	July 1999
Garden City, NY	833 Franklin Avenue	May 2000
Huntington, NY	350 New York Avenue	February 2001
Syosset, NY	49 Ira Road	March 2001
West Nyack, NY	3656 Palisades Center Drive	February 2002
Woodmere, NY	158 Irving Street	March 2002
Hartsdale, NY	208 E. Hartsdale Avenue	September 2004
Somers, NY	Somers Commons, 80 Route 6	February 2005
Port Jefferson Station, NY	200 Wilson Street	July 2005
White Plains, NY	4 City Center	September 2005
Hawthorne, NY	24 Saw Mill River Road	January 2006
Dobbs Ferry, NY	50 Livingstone Avenue	June 2008

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Location	Address	Date Opened or Management Assumed
Smithtown, NY	5 Browns Road	December 2007
Carmel, NY	1880 Route 6	July 2007
Hicksville, NY	100 Duffy Avenue	November 2008
New Rochelle, NY	Trump Plaza, Huguenot Street	March 2008
Deer Park, NY	455 Commack Avenue	March 2009
Garnerville, NY	20 W. Ramapo Road	October 2011
Stamford, CT	106 Commerce Road	January 1998
Danbury, CT	38 Mill Plain Road	January 1998
Stamford, CT	1063 Hope Street	November 1998
Greenwich, CT	6 Liberty Way	May 1999
Westport, CT	427 Post Road, East	January 2002
West Hartford, CT	65 Memorial Road	November 2007
Princeton, NJ	301 North Harrison Street	May 1997
Matawan, NJ	450 Route 34	April 1998
Marlboro, NJ	34 Route 9 North	April 1998
Ramsey, NJ	1100 Route 17 North	June 1998
Mahwah, NJ	7 Leighton Place	June 1998
Springfield, NJ	215 Morris Avenue	August 1998
Colonia, NJ	1250 Route 27	August 1998
Somerset, NJ	120 Cedar Grove Lane	August 1998
Hoboken, NJ	59 Newark Street	October 1998
West Caldwell, NJ	913 Bloomfield Avenue	April 1999
Jersey City, NJ	147 Two Harborside Financial Center	June 2002
Newark, NJ	1 Gateway Center	October 2002
Ridgewood, NJ	129 S. Broad Street	June 2003
Westwood, NJ	35 Jefferson Avenue	June 2004
Livingston, NJ	39 W. North Field Rd.	February 2005
Princeton, NJ	4250 Route 1 North	April 2005
Hoboken, NJ	210 14th Street	December 2006
Englewood, NJ	34-36 South Dean Street	December 2006
Clifton, NJ	202 Main Avenue	March 2007
Montclair, NJ	56 Church Street	January 2008
Butler, NJ	1481 Route 23	January 2009
East Brunswick, NJ	300 State Route 18	March 2009
Bayonne, NJ	550 Route 440 North	December 2011
Boston Sports Clubs:		
Boston, MA	1 Bulfinch Place	August 1998
Boston, MA	201 Brookline Avenue	June 2000
Boston, MA	361 Newbury Street	November 2001
Boston, MA	350 Washington Street	February 2002
Boston, MA	505 Boylston Street	January 2006
Boston, MA	560 Harrison Avenue	February 2006
Boston, MA	695 Atlantic Avenue	October 2006
Boston, MA	One Beacon Street	May 2013
Boston, MA	197 Clarendon Street	May 2013
Boston, MA	800 Boylston Street	May 2013
Boston, MA	100 Summer Street	May 2013
Boston, MA	540 Gallivan Road	Future opening
Allston, MA	15 Gorham Street	July 1997
Weymouth, MA	553 Washington Street	May 1999

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Location	Address	Date Opened or Management Assumed
Wellesley, MA	140 Great Plain Avenue	July 2000
Andover, MA	307 Lowell Street	July 2000
Lynnfield, MA	425 Walnut Street	July 2000
Lexington, MA	475 Bedford Avenue	July 2000
Franklin, MA	750 Union Street	July 2000
Cambridge, MA	625 Massachusetts Avenue	January 2001
West Newton, MA	1359 Washington Street	November 2001
Waltham, MA	840 Winter Street	November 2002
Watertown, MA	311 Arsenal Street	January 2006
Newton, MA	135 Wells Avenue	August 2006
Somerville, MA	1 Davis Square	December 2007
Medford, MA	70 Station Landing	December 2007
Westborough, MA	1500 Union Street	September 2008
Woburn, MA	300 Presidential Way	December 2008
Wayland, MA	Wayland Town Center	Future opening
Providence, RI	131 Pittman Street	December 2008
Providence, RI	10 Dorrance Street	January 2009
Washington Sports Clubs:		
Washington, D.C.	214 D Street, S.E	January 1980
Washington, D.C.	1835 Connecticut Avenue, N.W .	January 1990
Washington, D.C.	2251 Wisconsin Avenue, N.W	May 1994
Washington, D.C.	1211 Connecticut Avenue, N.W	July 2000
Washington, D.C.	1345 F Street, N.W	August 2002
Washington, D.C.	1990 K Street, N.W	February 2004
Washington, D.C.	783 Seventh Street, N.W	October 2004
Washington, D.C.	3222 M Street, N.W	February 2005
Washington, D.C.	14th Street, N.W	June 2008
North Bethesda, MD	10400 Old Georgetown Road	June 1998
Silver Spring, MD	8506 Fenton Street	November 2005
Bethesda, MD	6800 Wisconsin Avenue	November 2007
Alexandria, VA	3654 King Street	June 1999
Fairfax, VA	11001 Lee Highway	October 1999
West Springfield, VA	8430 Old Keene Mill	September 2000
Clarendon, VA	2700 Clarendon Boulevard	November 2001
Philadelphia Sports Clubs:		
Philadelphia, PA	220 South 5th Street	January 1999
Philadelphia, PA	2000 Hamilton Street	July 1999
Chalfont, PA	One Highpoint Drive	January 2000
Philadelphia, PA	1735 Market Street	October 2000
Ardmore, PA	34 W. Lancaster Avenue	March 2002
Radnor, PA	555 East Lancaster Avenue	December 2006
Swiss Sports Clubs:		
Basel, Switzerland	St. Johanns-Vorstadt 41	August 1987
Zurich, Switzerland	Glarnischstrasse 35	August 1987
Basel, Switzerland	Gellerstrasse 235	August 2001
BFX Studio:		
Manhattan	555 Sixth Avenue	Future opening

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Item 3. ***Legal Proceedings***

On or about March 1, 2005, in an action styled Sarah Cruz, et al v. Town Sports International, d/b/a New York Sports Club, plaintiffs commenced a purported class action against TSI, LLC in the Supreme Court, New York County, seeking unpaid wages and alleging that TSI, LLC violated various overtime provisions of the New York State Labor Law with respect to the payment of wages to certain trainers and assistant fitness managers. On or about June 18, 2007, the same plaintiffs commenced a second purported class action against TSI, LLC in the Supreme Court of the State of New York, New York County, seeking unpaid wages and alleging that TSI, LLC violated various wage payment and overtime provisions of the New York State Labor Law with respect to the payment of wages to all New York purported hourly employees. On September 17, 2010, TSI, LLC made motions to dismiss the class action allegations of both lawsuits for plaintiffs failure to timely file motions to certify the class actions. The court granted the motions on January 29, 2013, dismissing the class action allegations in both lawsuits. On March 4, 2013, plaintiffs served notice of their intent to appeal that dismissal. The court has stayed the remaining, individual claims in each action pending resolution of the plaintiffs appeal. The appeal has been fully briefed and the parties expect that oral arguments on the motion will be held in April 2014.

On September 22, 2009, in an action styled Town Sports International, LLC v. Ajilon Solutions, a division of Ajilon Professional Staffing LLC (Supreme Court of the State of New York, New York County, 602911-09), TSI, LLC brought an action in the Supreme Court of the State of New York, New York County, against Ajilon for, among other things, breach of contract seeking, among other things, money damages, in connection with Ajilon s failure to design and deliver to TSI, LLC a new sports club enterprise management system known as GIMS. Subsequently, on October 14, 2009, Ajilon brought a counterclaim against TSI, LLC alleging breach of contract, asserting, among other things, failure to pay outstanding invoices in the aggregate amount of approximately $2.9 million. Following a jury trial, a jury verdict was rendered on January 28, 2013, that awarded TSI, LLC damages against Ajilon in the amount of approximately $3.3 million, plus interest, and also awarded Ajilon damages against TSI, LLC in the amount of approximately $214,000, plus interest. After the Court granted Ajilon s motion to set aside the part of the jury verdict that had rejected the bulk of Ajilon s counterclaim, the Court increased the award of damages against TSI, LLC from approximately $214,000 to approximately $2.9 million, plus interest. The result is a net amount owed to TSI, LLC in the amount of approximately $400,000, plus interest. On April 8, 2013, TSI, LLC filed a notice of appeal, appealing the Court s decision to set aside the jury verdict, and on May 6, 2013, Ajilon filed its notice of appeal, appealing the verdict. On December 3, 2013, the Appellate Division issued its opinion, which vacated the judgments for damages both for and against TSI, LLC but let stand the jury s verdict that Ajilon is liable to TSI, LLC for damages to be determined at a new trial against Ajilon. The new trial, which has not yet been scheduled, will be limited to the damages suffered by TSI, LLC. On January 2, 2014, Ajilon filed a motion to the Appellate Division to both reargue the Appellate Division s decision to deny Ajilon damages as well as appeal the Appellate Division s decision to the New York State Court of Appeals. On February 25, 2014, the Appellate Division denied Ajilon s motion.

On February 7, 2007, in an action styled White Plains Plaza Realty, LLC v. TSI, LLC et al., the landlord of one of TSI, LLC s former health and fitness clubs filed a lawsuit in state court against it and two of its health club subsidiaries alleging, among other things, breach of lease in connection with the decision to close the club located in a building owned by the plaintiff and leased to a subsidiary of TSI, LLC, and take additional space in the nearby facility leased by another subsidiary of TSI, LLC. The trial court granted the landlord damages against its tenant in the amount of approximately $700,000, including interest and costs (Initial Award). TSI, LLC was held to be jointly liable with the tenant for the amount of approximately $488,000, under a limited guarantee of the tenant s lease obligations. The landlord subsequently appealed the trial court s award of damages, and on December 21, 2010, the appellate court reversed, in part, the trial court s decision and ordered the case remanded to the trial court for an assessment of additional damages, of approximately $750,000 plus interest and costs (the Additional Award). On February 7, 2011, the landlord moved for re-argument of the appellate court s decision, seeking additional damages plus attorneys fees. On April 8, 2011, the appellate court denied the landlord s motion. On August 29, 2011, the Additional Award (amounting to approximately $900,000), was entered against the tenant. TSI, LLC does not believe it is probable that TSI, LLC will be held liable to pay for any amount of the Additional

Award. Separately, TSI, LLC is party to an agreement with a third-party developer, which by its terms provides indemnification for the full amount of any liability of any nature arising out of the lease described above, including attorneys fees incurred to enforce the indemnity. In connection with the Initial Award (and in furtherance of the indemnification agreement), TSI, LLC and the developer have entered into an agreement pursuant to which the developer has agreed to pay the amount of the Initial Award in installments over time. The indemnification agreement also covers the Additional Award. The developer did not pay the amount of the Additional Award to the landlord, and on October 13, 2011 the landlord commenced a special proceeding in the Supreme Court of the State of New York, Westchester County, to collect the Additional Award directly from the developer. A motion to dismiss the special proceeding made by the developer was denied by the court on March 13, 2012. An appeal of that decision by the developer was rejected. On March 14, 2013, the landlord moved for summary judgment on its claim to recover the Additional Award directly from the developer and on March 25, 2013, the developer cross-moved for summary judgment to dismiss the special proceeding. In May 2013, the court granted summary judgment to the landlord and denied the cross-motion for summary judgment of the developer. Judgment was entered against the developer on June 5, 2013 in the amount of $1.0 million, plus interest. On June 13, 2013, the developer filed a notice of its intent to appeal the judgment. The appeal remains pending.

On or about October 4, 2012, in an action styled James Labbe, et al. v. Town Sports International, LLC, plaintiff commenced a purported class action in New York State court on behalf of personal trainers employed in New York State. Labbe is seeking unpaid wages and damages from TSI, LLC and alleges violations of various provisions of the New York State labor law with respect to payment of wages and TSI, LLC s notification and record-keeping obligations. On December 18, 2012, TSI, LLC filed a motion to stay the class action pending a decision on class certification in the Cruz case and to dismiss the Labbe action if the Cruz case is certified. On January 29, 2013, Labbe responded to the motion to stay and filed a cross-motion to consolidate the Labbe case with the Cruz case. On February 11, 2013, following the dismissal of the class claims in Cruz, Labbe withdrew the cross-motion to consolidate. Oral argument to stay the action until a decision is made on the appeal in the Cruz case was heard on April 10, 2013. On December 17, 2013, the Court granted TSI, LLC s motion to stay the Labbe action pending a resolution of the Cruz appeal. By the terms of the order, the stay lasts as long as the appeal of the dismissal of the class claims in the Cruz case remains pending.

In addition to the litigation discussed above, we are involved in various other lawsuits, claims and proceedings incidental to the ordinary course of business, including personal injury and employee relations claims. The results of litigation are inherently unpredictable. Any claims against us, whether meritorious or not, could be time consuming, result in costly litigation, require significant amounts of management time and result in diversion of significant resources. The results of these other lawsuits, claims and proceedings cannot be predicted with certainty. While it is not feasible to predict the outcome of such proceedings, in the opinion of the Company, either the likelihood of loss is remote or any reasonably possible loss associated with the resolution of such proceedings is not expected to be material either individually or in the aggregate.

Item 4. ***Mine Safety Disclosures***

Not applicable.

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PART II

Item 5. ***Market for Registrant s Common Equity and Related Stockholder Matters and Issuer Purchases of Equity Securities***

Price Range of Common Stock

Our common stock currently trades on The NASDAQ Global Market, under the symbol CLUB. The following table sets forth, for each quarterly period in the last two fiscal years, the high and low sales prices (in dollars per share) of our common stock as quoted or reported on The NASDAQ Global Market:

	High	Low
Year ended December 31, 2013:		
First Quarter	$ 11.11	$ 8.91
Second Quarter	$ 11.37	$ 9.31
Third Quarter	$ 13.03	$ 10.83
Fourth Quarter	$ 14.96	$ 11.50
Year ended December 31, 2012:		
First Quarter	$ 13.44	$ 7.37
Second Quarter	$ 13.48	$ 10.63
Third Quarter	$ 13.88	$ 9.31
Fourth Quarter(a)	$ 13.55	$ 9.32

(a) Pursuant to NASDAQ Exchange rules, the ex-dividend date with respect to the $3.00 per share special cash dividend was set as November 28, 2012. Accordingly, prior to the commencement of trading on November 28, 2012, the Company s stock price was reduced by $3.00 to reflect the payment of the cash dividend. The closing price per share on November 27, 2012 and November 28, 2012 was $12.39 and $9.85, respectively.

Holders

As of February 27, 2014, there were approximately 101 holders of record of our common stock. There are additional holders who are not holders of record but who beneficially own stock through nominee holders such as brokers and benefit plan trustees.

Dividends Policy

Prior to December 11, 2012, we had not paid dividends since becoming a publicly traded company. On November 16, 2012, as a means of returning value to our shareholders, the board of directors declared a special cash dividend of $3.00 per share to common stock holders of record as of November 30, 2012, paid on December 11, 2012. The special dividend was funded by borrowings of $60.0 million under our 2011 Senior Credit Facility (as defined below), as amended, together with available cash on hand. Actual dividends paid on December 11, 2012 were $70.3 million with an additional $1.1 million of dividends to be paid as restricted shares vest.

On November 15, 2013, the board of directors declared a regular quarterly cash dividend of $0.16 per share to common stock holders of record as of November 26, 2013, paid on December 5, 2013. The regular cash dividend was funded by available cash on hand. Actual dividends paid on December 5, 2013 were $3.8 million with an additional $58,000 of dividends to be paid as restricted shares vest. On February 12, 2014, the board of directors declared the second quarterly cash dividend of $0.16 per share payable on March 5, 2014 to common stock holders of record as of February 24, 2014. The aggregate amount to be paid will be approximately $3.9 million.

The board of directors currently intends to pay a quarterly cash dividend as a means of returning value to our stockholders. The declaration and payment of dividends to holders of our common stock by us, if any, are subject to the discretion of our board of directors. Our board of directors will take into account such matters as general economic and business conditions, our strategic plans, our financial results and condition, contractual, legal and regulatory restrictions on the payment of dividends by us and our subsidiaries and such other factors as our board of directors may consider to be relevant. We will rely on cash on hand at TSI Holdings, which was $43.6 million at December 31, 2013, and distributions received from our subsidiaries to provide the funds necessary to pay dividends on our common stock. The existing credit agreement of TSI, LLC restricts the ability of our subsidiaries to pay cash distributions to TSI Holdings in order for TSI Holdings to pay cash dividends except (a) in an amount, when combined with certain prepayments of indebtedness, of up to $35.0 million, subject to pro forma compliance with a total leverage ratio of no greater than 4.50:1.00 and no default or event of default existing or continuing under the credit agreement, and (b) an additional amount based on excess cash flow, such additional amounts subject to pro forma compliance with a total leverage ratio of less than 4.00:1.00 and no default or event of default existing or continuing under the credit agreement.

Issuer Purchases of Equity Securities

We did not purchase any equity securities during the fourth quarter ended December 31, 2013.

Recent Sales of Unregistered Securities

We did not sell any securities during the year ended December 31, 2013 that were not registered under the Securities Act of 1933, as amended.

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Stock Performance Graph

The graph depicted below compares the annual percentage change in our cumulative total stockholder return with the cumulative total return of the Russell 2000 and the NASDAQ composite indices.

* $100 invested on 12/31/08 in stock or index, including reinvestment of dividends. Fiscal year ending December 31.

	December 31,					
	2008	2009	2010	2011	2012	2013
Town Sports International Holdings, Inc	$ 100.00	$ 73.04	$ 127.27	$ 230.41	$ 435.90	$ 610.51
NASDAQ Composite	$ 100.00	$ 144.88	$ 170.58	$ 171.30	$ 199.99	$ 283.39
Russell 2000	$ 100.00	$ 127.17	$ 161.32	$ 154.59	$ 179.86	$ 249.69

Notes :

(1) The graph covers the period from December 31, 2008 to December 31, 2013.

(2) The graph assumes that $100 was invested at the market close on December 31, 2008 in our common stock, in the Russell 2000 and in the NASDAQ composite indexes and that all dividends were reinvested.

(3) A special cash dividend of $3.00 per share of common stock was declared by our board of directors on November 16, 2012 to shareholders of record on November 30, 2012, paid on December 11, 2012. A quarterly cash dividend of $0.16 per share was declared by our board of directors on November 15, 2013 to shareholders of record on November 26, 2013, paid on December 5, 2013.

(4) Stockholder returns over the indicated period should not be considered indicative of future stockholder returns.

(5) We include a comparison against the Russell 2000 because there is no published industry or line-of-business index for our industry and we do not have a readily definable peer group that is publicly traded.

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Notwithstanding anything to the contrary set forth in any of our previous or future filings under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, that might incorporate by reference this Annual Report on Form 10-K or future filings made by the Company under those statutes, the Stock Performance Graph is not deemed filed with the Securities and Exchange Commission, is not deemed soliciting material and shall not be deemed incorporated by reference into any of those prior filings or into any future filings made by the Company under those statutes, except to the extent that the Company specifically incorporates such information by reference into a previous or future filing, or specifically requests that such information be treated as soliciting material, in each case under those statutes.

Item 6. ***Selected Financial Data***

SELECTED CONSOLIDATED FINANCIAL AND OTHER DATA

(In thousands, except share, per share, club and membership data)

The selected consolidated balance sheet data as of December 31, 2013 and 2012 and the selected consolidated statement of operations and cash flow data for the years ended December 31, 2013, 2012 and 2011 have been derived from our audited consolidated financial statements included elsewhere herein. The selected consolidated balance sheet data as of December 31, 2011, 2010 and 2009 and the selected consolidated statement of operations and cash flow data for the years ended December 31, 2010 and 2009 have been derived from our audited consolidated financial statements not included herein. Other data and club and membership data for all periods presented have been derived from our unaudited books and records. Our historical results are not necessarily indicative of results for any future period. You should read these selected consolidated financial and other data, together with the accompanying notes, in conjunction with the Management s Discussion and Analysis of Financial Condition and Results of Operations section of this Annual Report and our consolidated financial statements and the related notes appearing at the end of this Annual Report.

	Year Ended December 31,				
	2013	**2012**	**2011**	**2010**	**2009**
Statement of Operations Data:					
Revenues	$ 470,225	$ 478,981	$ 466,941	$ 462,387	$ 485,392
Operating expenses:					
Payroll and related(1)	174,894	181,632	177,528	185,583	193,891
Club operating	179,683	178,950	176,463	174,135	178,854
General and administrative	28,431	24,139	25,799	28,773	31,587
Depreciation and amortization	49,099	49,391	51,536	52,202	56,533
Insurance recovery related to damaged property(2)	(3,194)				
Impairment of fixed assets	714	3,436		3,254	6,708
Impairment of internal-use software					10,194
Operating income	40,598	41,433	35,615	18,440	7,625
Loss on extinguishment of debt(3)	750	1,010	4,865		
Interest expense, net of interest income	22,616	24,597	24,127	21,013	20,969
Equity in the earnings of investees and rental income	(2,459)	(2,461)	(2,391)	(2,139)	(1,876)
Net income before provision (benefit) for corporate income taxes	19,691	18,287	9,014	(434)	(11,468)
Provision (benefit) for corporate income taxes(4)	7,367	6,321	2,699	(144)	(5,800)
Net income (loss)	$ 12,324	$ 11,966	$ 6,315	$ (290)	$ (5,668)
Earnings (loss) per weighted average number of shares:					
Basic	$ 0.51	$ 0.51	$ 0.28	$ (0.01)	$ (0.25)
Diluted	$ 0.50	$ 0.50	$ 0.27	$ (0.01)	$ (0.25)
Dividends declared per common share(5)	$ 0.16	$ 3.00	$	$	$

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	As of December 31,				
	2013	2012	2011	2010	2009
Balance Sheet Data:					
Cash and cash equivalents	$ 73,598	$ 37,758	$ 47,880	$ 38,803	$ 10,758
Working capital surplus (deficit)(6)	27,830	(11,825)	(18,311)	(11,926)	(35,166)
Total assets(7)	413,792	404,770	450,402	474,693	467,466
Long-term debt, including current installments	314,909	310,339	288,994	316,513	318,363
Total stockholders (deficit) equity	(43,516)	(55,496)	354	(6,945)	(8,233)
Net debt(8)	251,402	277,985	243,870	277,710	307,605

	Year Ended December 31,				
	2013	2012	2011	2010	2009
Cash Flow Data:					
Cash provided by (used in):					
Operating activities	$ 67,388	$ 60,053	$ 74,885	$ 51,238	$ 76,241
Investing activities	(30,606)	(22,490)	(30,907)	(22,035)	(49,277)
Financing activities	(975)	(47,722)	(35,349)	(1,765)	(26,763)
Other Data:					
Non-cash rental expense, net of non-cash rental income	(5,692)	(4,037)	(3,663)	(5,552)	(2,494)
Non-cash share-based compensation expense	2,204	1,306	1,412	1,336	1,704

	Year Ended December 31,				
	2013	2012	2011	2010	2009
Club and Membership Data:					
New clubs opened			2		4
Clubs acquired	6				
Clubs closed	(4)		(2)	(1)	(9)
Wholly-owned clubs operated at end of period	160	158	158	158	159
Total clubs operated at end of period(9)	162	160	160	160	161
Total members at end of period(10)	497,000	510,000	523,000	493,000	486,000
Restricted members at end of period(11)	41,000	38,000	38,000	17,000	
Comparable club revenue (decrease) increase(12)	(1.8)%	1.6%	1.8%	(4.3)%	(5.6)%
Revenue per weighted average club (in thousands)(13)	$ 2,971	$ 3,032	$ 2,934	$ 2,881	$ 2,957
Average revenue per member(14)	$ 934	$ 922	$ 915	$ 947	$ 969
Average joining fees collected per member(15)	$ 59	$ 57	$ 55	$ 37	$ 19
Annual attrition(16)	41.9%	41.0%	39.9%	41.9%	45.2%

(1) In the year ended December 31, 2009, Payroll and related includes a correction of an accounting error of $751 related to deferred membership costs which was previously disclosed in the Company s Form 10-K for the year ended December 31, 2009.

(2) The $3,194 of insurance recovery related to damaged property in the year ended December 31, 2013 was primarily in connection with property damaged by Hurricane Sandy.

(3) The $750 loss on extinguishment of debt recorded for the year ended December 31, 2013 is comprised of the write-off of net deferred financing costs and debt discount in connection with the November 15, 2013 debt refinancing. The proceeds from the 2013 Senior Credit Facility were used to repay the remaining outstanding principal amounts of the 2011 Senior Credit Facility of $315,743 plus accrued and unpaid interest.

The $1,010 loss on extinguishment of debt recorded for the year ended December 31, 2012 is comprised of a $464 write-off of net deferred financing costs and debt discount related to the August 22, 2012 debt

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repricing and a write-off of $546 of net deferred financing costs and debt discount in connection with the August 28, 2012 voluntary prepayment of $15.0 million on our term loan facility.

The $4,865 loss on extinguishment of debt recorded for the year ended December 31, 2011 resulted from the debt refinancing on May 11, 2011. The proceeds from the 2011 Senior Credit Facility were used to repay the remaining outstanding principal amount of the 2007 Senior Credit Facility (as defined below) of $164,000 and the remaining outstanding principal amount of the Senior Discount Notes of $138,450. We incurred $2,538 of call premium on the Senior Discount Notes together with the write-off of $2,327 of net deferred financing costs related to the debt extinguishment.

(4) Corporate income taxes for the year ended December 31, 2013, 2012 and 2011 includes income tax benefits totaling $16, $483 and $343, respectively, related to the correction of accounting errors. See Note 14 Corporate Income Taxes to the Company s consolidated financial statements in this Annual Report for further details.

(5) In the fourth quarter of the year ended December 31, 2013, the board of directors of the Company declared a quarterly cash dividend of $0.16 per share, payable on December 5, 2013 to common stockholders of record at the close of business on November 26, 2013. The aggregate amount of the dividends paid totaled $3,792 with another $58 payable as restricted shares vest. In the year ended December 31, 2012, the board of directors of the Company declared a special cash dividend of $3.00 per share, payable on December 11, 2012 to common stockholders of record at the close of business on November 30, 2012. The aggregate amount of the dividends paid totaled $70,296 with another $1,104 payable as restricted shares vest.

(6) The working capital deficit reflects a revision to reclassify deferred promotion amounts of $1,569, $1,466, $1,185 and $1,581 from long-term assets to current assets as of December 31, 2012, 2011, 2010 and 2009, respectively.

The working capital deficit reflects a revision to reclassify amounts between current deferred tax assets and long-term deferred tax assets and long-term tax liability of ($5,572) and ($1,660) as of December 31, 2012 and 2011, respectively.

(7) Total assets reflects revisions of $860, $860 and $10,527 as of December 31, 2012, 2011 and 2010, respectively, related to revisions to reclassify amounts between deferred tax assets and long-term tax liability.

(8) Net debt represents the total principal balance of long-term debt outstanding, net of cash and cash equivalents.

(9) Includes wholly-owned and partly-owned clubs. Not included in the total club count are locations that are managed by us in which we do not have an equity interest. These managed sites include three managed university locations and four additional managed locations acquired on May 2013 as part of the Fitcorp acquisition as well as one new managed location added during the fourth quarter of 2013.

(10) Represents members at wholly-owned and partly-owned clubs.

(11) Restricted members primarily include students and teachers at our wholly-owned and partly-owned clubs. This membership allows for club usage at restricted times, at a discount to other memberships offered.

(12) Total revenue for a club is included in comparable club revenue increase (decrease) beginning on the first day of the thirteenth full calendar month of the club s operation.

(13) Revenue per weighted average club is calculated as total revenue divided by the product of the total number of clubs and their weighted average months in operation as a percentage of the period.

(14) Average revenue per member is total revenue from wholly-owned clubs for the period divided by the average number of memberships from wholly-owned clubs for the period, including restricted memberships, summer student and summer pool memberships, where average number of memberships for the period is

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derived by dividing the sum of the total memberships at the end of each month during the period by the total number of months in the period.

(15) Average joining fees collected per member is calculated as total initiation and processing fees divided by the number of new members, excluding pre-sold, summer student and summer pool memberships and including restricted memberships that began in April 2010, during each respective year.

(16) Annual attrition is calculated as total member losses for the year divided by the average monthly member count over the year excluding pre-sold, summer student and summer pool memberships and including our restricted memberships that began in April 2010, during each respective year.

Item 7. *Management s Discussion and Analysis of Financial Condition and Results of Operations*

You should read the following discussion and analysis of our financial condition and consolidated results of operations in conjunction with the Selected Consolidated Financial and Other Data section of this Annual Report and our consolidated financial statements and the related notes appearing at the end of this Annual Report. In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions (see FORWARD-LOOKING STATEMENTS *discussion). Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors, including, but not limited to, those set forth in Item 1A. Risk Factors of this Annual Report.*

Overview

We are the largest owner and operator of fitness clubs in the Northeast and Mid-Atlantic regions of the U.S. As of December 31, 2013, we operated 162 clubs that collectively served approximately 497,000 members. We develop clusters of clubs to serve densely populated major metropolitan regions and we service such populations by clustering clubs near the highest concentrations of our target customers areas of both employment and residence. Our clubs are located for maximum convenience to our members in urban or suburban areas, close to transportation hubs or office or retail centers. Our members include a wide age demographic covering the student market to the active mature market. Our members generally have annual income levels of between $50,000 and $150,000.

Our goal is to be the most recognized health club network in each of the four major metropolitan regions that we serve. We believe that our strategy of clustering clubs provides significant benefits to our members and allows us to achieve strategic operating advantages. In each of our markets, we have developed clusters by initially opening or acquiring clubs located in the more central urban markets of the region and then branching out from these urban centers to suburbs and neighboring communities. Capitalizing on this clustering of clubs, as of December 31, 2013, approximately 45% of our members participated in our Passport Membership which allows unlimited access to all of our clubs in our clusters within one, or all of, our regions, respectively, for a higher monthly membership dues, while approximately 31% of our members participate in our Core membership, which allows unlimited access to the member s home club. Approximately 16% of our members participate in our previously offered Gold membership which allows unlimited access to a designated club and access to all other clubs during off-peak hours. Our Restricted Membership, which is a favorably-priced, restricted-use month-to-month membership was held by approximately 8% of our members.

We have executed our clustering strategy successfully in the New York region, our most mature region, through the network of fitness clubs we operate under our New York Sports Clubs brand name. We are the largest fitness club operator in Manhattan with 37 locations and operated a total of 108 clubs under the New York Sports Clubs brand name within a 120-mile radius of New York City as of December 31, 2013. As of December 31, 2013, we owned and operated 29 clubs in the Boston region under our Boston Sports Clubs brand name, 16 clubs (two of which are partly-owned) in the Washington, D.C. region under our Washington Sports Clubs brand name, six clubs in the Philadelphia region under our Philadelphia Sports Clubs brand name and three clubs in Switzerland. We employ localized brand names for our clubs to create an image and atmosphere

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consistent with the local community and to foster recognition as a local network of quality fitness clubs rather than a national chain.

As the fitness industry continues to see a rise in popularity of private studio offerings, we have used our extensive industry experience to offer our own private studio brand called the Boutique Fitness Experience (BFX Studio) with our first unit opening in the first half of 2014. This three-dimension luxury studio brand will take advantage of the rise in consumer demand for studio experiences. Our BFX Studio will include three unique offerings: Ride Republic, which is indoor cycling, Private Sessions for personal training and Master Class for certain group exercise classes. Our BFX Studio will be staffed with high caliber instructors in each of the three core offerings and the studios will be designed to appeal to all ages and all experience levels of metropolitan, active healthy lifestylers. We estimate that this studio concept will require approximately 7,500 to 10,000 square feet of space per studio which compares to the approximately 26,000 square feet aggregate average size of our traditional clubs.

Revenue and Operating Expenses

We have two principal sources of revenue:

Membership revenue: Our largest sources of revenue are dues inclusive of maintenance fees and joining fees paid by our members. In addition, we collect usage fees on a per visit basis subject to peak and off-peak hourly restrictions depending on membership type. These dues and fees comprised 79.4% of our total revenue for the year ended December 31, 2013. We recognize revenue from membership dues in the month when the services are rendered. Approximately 97% of our members pay their monthly dues by Electronic Funds Transfer, or EFT, while the balance is paid annually in advance. We recognize revenue from joining fees over the estimated average membership life.

Ancillary club revenue: For the year ended December 31, 2013, we generated 14.1% of our revenue from personal training and 5.3% of our revenue from other ancillary programs and services consisting of programming for children, signature classes, Small Group Training and other member activities, as well as sales of miscellaneous sports products. We continue to grow ancillary club revenue by building on ancillary programs such as our personal training membership product and our fee-based Small Group Training programs.

We also receive revenue (approximately 1.3% of our total revenue for the year ended December 31, 2013) from the rental of space in our facilities to operators who offer wellness-related offerings, such as physical therapy and juice bars. In addition, we sell in-club advertising and sponsorships and generate management fees from certain club facilities that we do not wholly own. We also collect laundry related revenue for the laundering of towels for third parties. We refer to these revenues as fees and other revenue.

We currently own our 151 East 86th Street, New York location, which houses our New York Sports Clubs on East 86th Street, New York as well as a retail tenant that generates rental income for us. In December 2013, we announced the entry into an agreement to sell this property, which sale is expected to close on or about March 31, 2014. As part of the sale, we are also selling the leasehold interest in the retail tenant at this location. Upon completion of the sale, we will no longer be entitled to the rental income from this retail tenant. Rental income from this retail tenant was approximately $2.0 million in both the years ended December 31, 2013 and 2012.

Our performance is dependent on our ability to continually attract and retain members at our clubs. We experience attrition at our clubs and must attract new members in order to maintain our membership and revenue levels. In the years ended December 31, 2013 and 2012, our attrition rate, including restricted members, was 41.9% and 41.0%, respectively.

Our operating and selling expenses are comprised of both fixed and variable costs. Fixed costs include club and supervisory and other salary and related expenses, occupancy costs, including most elements of rent, utilities,

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housekeeping and contracted maintenance expenses, as well as depreciation. Variable costs are primarily related to payroll associated with ancillary club revenue, membership sales compensation, advertising, certain facility repairs and club supplies.

General and administrative expenses include costs relating to our centralized support functions, such as accounting, insurance, information and communication systems, purchasing, member relations, legal and consulting fees and real estate development expenses. Payroll and related expenses are included in a separate line item on the consolidated statement of operations and are not included in general and administrative expenses.

As clubs mature and increase their membership base, fixed costs are typically spread over an increasing revenue base and operating margins tend to improve. Conversely, when our membership base declines, our operating margins are negatively impacted.

Our primary capital expenditures relate to the construction or acquisition of new club facilities and upgrading and expanding our existing clubs. The construction and equipment costs vary based on the costs of construction labor, as well as the planned service offerings and size and configuration of the facility. We perform routine improvements at our clubs and partial replacement of the fitness equipment each year for which we are currently budgeting approximately 3% to 5% of projected annual revenue. Expansions of certain facilities are also performed from time to time, when incremental space becomes available on acceptable terms and utilization and demand for the facility dictate. In this regard, facility remodeling is also considered where appropriate.

From 2012 to 2013, operating income decreased 2.1%. 2013 operating income included benefits of $3.2 million resulting from insurance proceeds collected primarily in connection with property damaged by Hurricane Sandy and $424,000 related to the recognition of out of period non-cash rental income, partially offset by fixed asset impairment charges totaling $714,000. In 2012, we recorded fixed asset impairment charges totaling $3.4 million, of which $3.2 million related to write-offs of fixed assets for four clubs that sustained damages from Hurricane Sandy during the fourth quarter of 2012. In 2011, we did not incur any fixed asset impairment charges or one-time transactions.

	Year Ended December 31,		
	2013	2012	2011
	($ amounts in thousands)		
Operating income	$ 40,598	$ 41,433	$ 35,615
(Decrease) increase over prior period	(2.0)%	16.3%	93.1%
Net income	$ 12,324	$ 11,966	$ 6,315
(Decrease) increase over prior period	3.0%	89.5%	2,277.6%
Cash flows provided by operating activities	$ 67,388	$ 60,053	$ 74,885
Increase (decrease) over prior period	12.2%	(19.8)%	46.2%

Historically, we have focused on building or acquiring clubs in areas where we believe the market is underserved or where new clubs are intended to replace existing clubs at their lease expiration. Based on our experience, a new club tends to experience a significant increase in revenues during its first three years of operation as it reaches maturity. Because there is relatively little incremental cost associated with such increasing revenue, there is a greater proportionate increase in profitability. We believe that the revenues and operating income of our immature clubs will increase as they mature. In contrast, operating income margins may be negatively impacted in the near term by our planned new club openings. In most cases, we are able to transfer many of the members of closed clubs to other clubs thereby enhancing overall profitability. During 2013, we completed the acquisition of the Fitcorp clubs in Boston, which included five clubs and four managed sites. We also completed an acquisition of a single club in Manhattan. We will continue to pursue club acquisition opportunities as well as assess club relocations and closures of underperforming clubs. We currently are targeting to open a combined four to six NYSC and BSC clubs in 2014 and two to four BFX Studio units.

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As of December 31, 2013, 160 of our fitness clubs were wholly-owned by us and our consolidated financial statements include the operating results of all such clubs. Two locations in Washington, D.C. were partly-owned by us, with our profit sharing percentages approximating 20% (after priority distributions) and 45%, respectively, and are treated as unconsolidated affiliates for which we apply the equity method of accounting. In addition, we provide management services at locations where we do not have an equity interest which include three fitness clubs located in colleges and universities, four managed sites acquired in connection with our Fitcorp acquisition in May 2013 and one new managed site added during the fourth quarter of 2013.

Comparable Club Revenue

We define comparable club revenue as revenue at those clubs that were operated by us for over 12 months and comparable club revenue increase (decrease) as revenue for the 13th month and thereafter as applicable as compared to the same period of the prior year.

	Comparable Club Revenue Increase (Decrease)	
	Quarter	**Full-Year**
2011		
First Quarter	(0.5)%	
Second Quarter	1.5%	
Third Quarter	3.0%	
Fourth Quarter	3.4%	1.8%
2012(a)		
First Quarter	4.5%	
Second Quarter	2.1%	
Third Quarter	1.0%	
Fourth Quarter	(1.1)%	1.6%
2013		
First Quarter	(2.4)%	
Second Quarter	(1.7)%	
Third Quarter	(1.7)%	
Fourth Quarter	(1.3)%	(1.8)%

(a) Comparable club revenue for the third quarter of 2012 excludes $1.2 million of additional fees and other revenue realized in connection with the termination of a long-term marketing arrangement with a third party in-club advertiser. Comparable club revenue for the fourth quarter of 2013 excludes $424,000 of out of period rental income recognized resulting from the correction of an accounting error.

Key determinants of comparable club revenue increases (decreases) are new memberships, member retention rates, pricing and ancillary revenue increases (decreases).

The decline in the comparable club revenue in the fourth quarter of 2012 was in part due to the impact of Hurricane Sandy on our business, including decreases in personal training and ancillary revenues and a net loss of members. We experienced an overall member loss of 12,000 during the fourth quarter of 2012. The lower member base as we started 2013 combined with the additional loss of 13,000 members during 2013 largely contributed to the 1.8% decline in comparable club revenue for the year ended December 31, 2013. For the year ended December 31, 2013 compared to the year ended December 31, 2012, comparable club revenue declined by 1.8%. Memberships at our comparable clubs were down 2.8% and the combined effect of ancillary club revenue, initiation fees and other revenue decreased 0.1% which was partially offset by a 1.1% increase in the price of our dues and fees.

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Historical Club Count

	Year Ended December 31, 2013	2012	2011
Wholly-owned clubs operated at beginning of period	158	158	158
New clubs opened			2
Clubs acquired	6		
Clubs closed	(4)		(2)
Wholly-owned clubs operated at end of period	160	158	158
Partly-owned clubs operated at end of period	2	2	2
Total clubs operated at end of period(1)	162	160	160

(1) Includes wholly-owned and partly-owned clubs. Not included in the total club count are locations that are managed by us in which we do not have an equity interest. These managed sites include three managed university locations and four additional managed locations acquired in May 2013 as part of the Fitcorp acquisition as well as one new managed location added during the fourth quarter of 2013.

Results of Operations

The following table sets forth certain operating data as a percentage of revenue for the periods indicated:

	Year Ended December 31, 2013	2012	2011
Revenues	100.0%	100.0%	100.0%
Operating expenses:			
Payroll and related	37.2	37.9	38.0
Club operating	38.2	37.4	37.8
General and administrative	6.0	5.0	5.6
Depreciation and amortization	10.3	10.3	11.0
Insurance recovery related to damaged property	(0.7)		
Impairment of fixed assets	0.2	0.7	
Operating income	8.6	8.7	7.6
Loss on extinguishment of debt	0.1	0.2	1.0
Interest expense	4.8	5.2	5.2
Equity in the earnings of investees and rental income	(0.5)	(0.5)	(0.5)
Income before provision for corporate income taxes	4.2	3.8	1.9
Provision for corporate income taxes	1.6	1.3	0.6
Net income	2.6%	2.5%	1.3%

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Year ended December 31, 2013 compared to year ended December 31, 2012

Revenue

Revenue (in thousands) was comprised of the following for the periods indicated:

	Year Ended December 31,				
	2013		2012		
	Revenue	% Revenue	Revenue	% Revenue	% Variance
Membership dues	$ 358,761	76.3%	$ 366,044	76.4%	(2.0)%
Joining fees	14,392	3.0%	11,595	2.4%	24.1%
Membership revenue	373,153	79.4%	377,639	78.8%	(1.2)%
Personal training revenue	66,367	14.1%	65,641	13.7%	1.1%
Other ancillary club revenue	24,720	5.3%	29,897	6.3%	(17.3)%
Ancillary club revenue	91,087	19.4%	95,538	20.0%	(4.7)%
Fees and other revenue	5,985	1.3%	5,804	1.2%	3.1%
Total revenue	$ 470,225	100.0%	$ 478,981	100.0%	(1.8)%

Total revenue decreased $8.8 million, or 1.8%, for the year ended December 31, 2013 compared to the year ended December 31, 2012 as a result of decreases in both membership revenue and ancillary club revenue.

The prior year revenue for 2012 was impacted by the effects of Hurricane Sandy on our business during the fourth quarter of 2012 as a result of lost operating days. At the height of the storm, 131 of our 160 clubs were closed with 16 clubs that remained closed for over a week, one club that permanently closed and one club that recently reopened in December 2013. While it is very difficult to estimate the impact of the storm given the prolonged disruption in most of our markets, we estimate that revenue for 2012 was negatively impacted by approximately $1.0 million as a result of the hurricane.

For the year ended December 31, 2013, revenue decreased $8.5 million as a result of a decrease in comparable club revenue and $3.9 million related to the closure of four clubs and the temporary closure of one club due to damages from Hurricane Sandy (club reopened in late December 2013). Revenue for 2012 also included a benefit from an acceleration of in-club advertising revenue which added approximately $1.2 million to fees and other revenue, while 2013 revenue did not have such a benefit. The effect of these revenue decreases were partially offset by a $4.5 million increase in revenue resulting from the acquisition of new clubs during 2013.

Membership dues revenue decreased $7.3 million in the year ended December 31, 2013 compared to the year ended December 31, 2012 driven primarily by the decline in membership levels which accounts for approximately $12.0 million of the decrease. Increased pricing offset the decrease in membership levels for approximately $4.7 million. The impact of Hurricane Sandy contributed to an overall member loss of 12,000 during the fourth quarter of 2012. The lower member base as we started 2013 combined with the additional loss of 13,000 members during 2013 largely contributed to the decline in membership and membership dues.

Joining fees revenue increased $2.8 million in the year ended December 31, 2013 compared to the year ended December 31, 2012. The increase in joining fees was, in part, due to the effect of the lower estimated weighted average membership life of 24 months for unrestricted members during the year ended December 31, 2013, compared to 28 months during the year ended December 31, 2012. The lower amortizable life in effect during 2013 resulted in higher joining fees revenue recognition as joining fees were amortized over a shorter estimated average membership life.

Personal training revenue increased $726,000 in the year ended December 31, 2013 compared to the year ended December 31, 2012. This increase was driven, in part, by the effect of a price increase effective

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September 1, 2013 coupled with the success of our personal training membership product which was launched in June 2011 with single session membership product offerings and further expanded in 2012 and 2013 with multi-session personal training membership products. After experiencing a 3.4% year-over-year decline in personal training revenue during the first half of 2013, personal training revenue increased 6.3% in the second half of 2013 with third and fourth quarter personal training revenue year-over-year increases of 5.0% and 7.8%, respectively.

Other ancillary club revenue decreased $5.2 million in the year ended December 31, 2013 compared to the year ended December 31, 2012 driven primarily by a decline in revenue from our Sports Club for Kids programs and Small Group Training.

Fees and other revenue increased $181,000 in the year ended December 31, 2013 compared to the year ended December 31, 2013. Excluding the $424,000 out of period revision increasing 2013 rental revenue and the $1.2 million benefit from the acceleration of in in-club advertising revenue in the year ended December 31, 2012, fees and other revenue for the year ended December 31, 2013 increased approximately $957,000 driven by higher laundry service revenue and increases in club management fees.

Comparable club revenue decreased 1.8% in the year ended December 31, 2013, excluding the $1.2 million accelerated in-club advertising revenue recognized in the third quarter of 2012. Memberships at our comparable clubs were down 2.8% and the combined effect of ancillary club revenue, initiation fees and other revenue decreased 0.1% which was partially offset by a 1.1% increase in the price of our dues and fees.

Operating Expenses

Operating expenses (in thousands) were comprised of the following for the periods indicated:

	Year Ended December 31,			
	2013	2012	$ Variance	% Variance
Payroll and related	$ 174,894	$ 181,632	$ (6,738)	(3.7)%
Club operating	179,683	178,950	733	0.4%
General and administrative	28,431	24,139	4,292	17.8%
Depreciation and amortization	49,099	49,391	(292)	(0.6)%
Insurance recovery related to damaged property	(3,194)		(3,194)	n/a%
Impairment of fixed assets	714	3,436	(2,722)	(79.2)%
Operating expenses	$ 429,627	$ 437,548	$ (7,921)	(1.8)%

Operating expenses decreased $7.9 million, or 1.8%, in the year ended December 31, 2013 compared to the prior year. Total months of club operation increased 0.3%, remaining relatively flat compared to last year. The principal drivers of the decrease in operating expenses are described below:

Payroll and related. Payroll and related expenses for the year ended December 31, 2013 decreased $6.7 million, or 3.7%, compared to the year ended December 31, 2012. The prior year payroll and related expenses included a $2.5 million payroll bonus payment made during the fourth quarter of 2012 in connection with a special dividend payment in December 2012 compared to a payroll bonus payment of $126,000 made during the fourth quarter of 2013 in connection with a regular dividend payment in December 2013. The decrease in payroll and related expenses was also due to decreases in club commissions and bonuses related to the decline in revenue and decreases in management incentive bonuses.

As a percentage of total revenue, payroll and related expenses decreased to 37.2% in the year ended December 31, 2013 from 37.9% in the year ended December 31, 2012.

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Club operating. Club operating expenses increased $733,000 or 0.4% compared to the year ended December 31, 2012 primarily due to the $782,000 increase in rent and occupancy expenses. Rent and occupancy increased $1.8 million increase from the acquisition of new clubs and one club scheduled to open in 2014 where the lease period commenced in October 2013. Rent and occupancy expenses also increased $1.2 million at our existing clubs, net of a $254,000 decrease related to the reduction of rental space at one location. These increases were offset by a decrease of $2.3 million from the closure of four clubs and one club that was temporarily closed due to Hurricane Sandy that recently reopened in December 2013.

As a percentage of total revenue, club operating expenses increased to 38.3% in the year ended December 31, 2013 from 37.4% in the year ended December 31, 2012.

General and administrative. General and administrative expense increased $4.3 million, or 17.8%, in the year ended December 31, 2013 compared to the year ended December 31, 2012. There was a $2.0 million increase in insurance expense, due in part to favorable loss reserve adjustments in the prior year, as well as an $853,000 increase in consulting and computer maintenance expense related to the implementation of our new club operating system. Phone and data line related expenses also increased by $492,000 due primarily to transition costs related to the conversion of our communication lines to a VOIP based system. General and administrative expenses in the year ended December 31, 2013 also includes $326,000 of fees related to our club acquisitions in Manhattan and Boston and includes approximately $216,000 of consulting expenses related to our new BFX Studio concept.

Depreciation and amortization. In the year ended December 31, 2013 compared to the year ended December 31, 2012, depreciation and amortization expense was relatively flat.

Insurance recovery related to damaged property. In the year ended December 31, 2013, the Company collected $3.2 million of insurance cash proceeds related primarily due to property damaged by Hurricane Sandy. There were no such proceeds collected in the year ended December 31, 2012.

Impairment of fixed assets. In the year ended December 31, 2013, we recorded fixed asset impairment charges totaling $714,000 related to three underperforming clubs. In the year ended December 31, 2012, we recorded fixed asset impairment charges totaling $3.4 million, comprised of a $239,000 impairment charge related to one underperforming club and $3.2 million of additional impairments related to the write-down of fixed assets at four clubs that sustained severe damages from Hurricane Sandy.

Loss on Extinguishment of Debt

In the year ended December 31, 2013, loss on extinguishment of debt was $750,000 comprised of the write-off of net deferred financing costs and debt discount related to the debt refinancing in November 2013. In the year ended December 31, 2012, loss on extinguishment of debt was $1.0 million. The loss on extinguishment of debt was comprised of a $464,000 write-off of net deferred financing costs and debt discount related to the August 2012 debt repricing and a write-off of $546,000 of net deferred financing costs and debt discount in connection with the August 28, 2012 voluntary prepayment of $15.0 million on our term loan facility.

Interest Expense

Interest expense decreased by $2.0 million in the year ended December 31, 2013 compared to the year ended December 31, 2012 primarily due to the lower additional interest expense recognized in 2013 compared to 2012. In 2013, we incurred additional interest expense of $1.2 million related to the fees incurred in the debt refinancing in November 2013 as described below. In 2012, we incurred additional interest expense of $3.0 million related to the repricing amendment in August 2012 and a further amendment in November 2012.

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Provision for Corporate Income Taxes

We recorded a provision for corporate income taxes of $7.4 million and $6.3 million for the years ended December 31, 2013 and 2012, respectively. Our 2013 and 2012 effective tax rates of 37% and 35% in the years ended December 31, 2013 and 2012, respectively, were favorably impacted by the expected benefits from our captive insurance arrangement.

The State of New York has, for the past several years, been conducting an audit of our income tax returns for the tax years 2006 through 2012. The State issued a proposed assessment dated, January 13, 2014 for $3.8 million, inclusive of $1.2 million of interest. A meeting has been requested with the State of New York to discuss this assessment. We are also under audit for the same period by the City of New York and that audit continues to remain in discovery phase. The years from 2010 through 2012 remain open for the City of New York. We continue to evaluate the merits of the proposed assessment as new information becomes available when we meet the state authorities. The Company has not recorded a tax reserve related to the proposed assessment. Due to the limited availability of information at this time, an estimate of the reasonably possible change to unrecognized tax benefits within the next 12 months of the reporting date cannot be made.

The results for the year ended December 31, 2013 also include the correction of errors that resulted in an increase in tax benefits for corporate income taxes and a related increase in deferred tax assets in our consolidated statement of operations and consolidated balance sheet, respectively. In the fourth quarter of 2013, we identified corrections related to temporary differences in fixed assets for state depreciation resulting in the recognition of an income tax benefit of $225,000. Also, in the fourth quarter of 2013, we identified corrections related to temporary differences in landlord allowances resulting in the recognition of out of period expense of $209,000 for a net benefit to the Provision for corporate income taxes of $16,000 in the year ended December 31, 2013. We also made out-of period balance sheet revisions as of December 31, 2012. The balance sheet revisions relate to a reclassification of the deferred tax asset associated with deferred membership costs and the corrections related to temporary differences in landlord allowances. As of December 31, 2012, the net effect of the balance sheet adjustments was a decrease in current deferred tax assets of $5.6 million, and increases in long-term deferred tax assets of $6.4 million and long-term income tax liability (included within Other liabilities) of $860,000.

The results for the year ended December 31, 2012 include the correction of temporary differences that resulted in an increase in benefit for corporate income taxes and a related increase in deferred tax assets in the Company s consolidated statement of operations and consolidated balance sheet, respectively. In the fourth quarter of 2012, the Company identified corrections related to temporary differences in fixed assets, intangible assets and deferred revenue resulting in the recognition of an income tax benefit of $483,000.

In September 2013, the Internal Revenue Service issued new regulations relating to the treatment of repairs effective for tax years beginning after December 31, 2013 with early adoption permissible. We have opted for early adoption in the year ended December 31, 2013, which has created a timing difference for the accelerated tax deduction for repairs in excess of the book deduction.

As of December 31, 2013, we had net deferred tax assets of $28.4 million. On a quarterly basis, we assess the weight of all available positive and negative evidence to determine whether the net deferred tax asset is realizable. We have historically been a taxpayer and are in a three year cumulative income position as of December 31, 2013 for federal as well certain state jurisdictions. In addition, based on recent trends, we project future income sufficient to realize the deferred tax assets during the periods when the temporary tax deductible differences reverse. With the exception of the deductions related to our captive insurance company for state taxes, state taxable income has been and is projected to be the same as federal taxable income. Because we expect the captive insurance company to be discontinued in 2014, the assessment of the realizability of the state deferred tax assets is consistent with the federal tax analysis above. We have state net operating loss carry-forwards, which we believe will be realized within the available carry-forward period, except for a small net operating loss carry-forward in Rhode Island due to the short carry-forward period in that state. Accordingly, we concluded that it is more likely than not that the deferred tax assets will be realized. If actual results do not meet our forecasts and we incur lower than expected income or losses in 2014 and beyond, then a valuation allowance against the deferred tax assets may be required in the future. In 2014, we expect our effective tax rate to approximate 36% to 39% and will be favorably impacted from tax benefits derived from the captive insurance arrangement. Upon the completion of the pending sale of our East 86th Street building, the effective tax rate will range from 42% to 44%.

Year ended December 31, 2012 compared to year ended December 31, 2011

Revenue

Revenue (in thousands) was comprised of the following for the periods indicated:

	Year Ended December 31,				
	2012		2011		
	Revenue	% Revenue	Revenue	% Revenue	% Variance
Membership dues	$ 366,044	76.4%	$ 364,536	78.1%	0.4%
Joining fees	11,595	2.4%	6,824	1.4%	69.9%
Membership revenue	377,639	78.8%	371,360	79.5%	1.7%
Personal training revenue	65,641	13.7%	62,394	13.4%	5.2%
Other ancillary club revenue	29,897	6.3%	28,297	6.1%	5.7%
Ancillary club revenue	95,538	20.0%	90,691	19.5%	5.3%
Fees and other revenue	5,804	1.2%	4,890	1.0%	18.7%
Total revenue	$ 478,981	100.0%	$ 466,941	100.0%	2.6%

Total revenue increased $12.0 million, or 2.6%, for the year ended December 31, 2012 compared to the year ended December 31, 2011. Revenue for 2012 included a benefit from an acceleration of in-club advertising revenue which added approximately $1.2 million to fees and other revenue. For the year ended December 31, 2012, revenue increased $4.4 million at the two clubs opened or acquired subsequent to December 31, 2010 (both opened in the fourth quarter of 2011) and $7.1 million at our clubs opened or acquired prior to December 31, 2010. Revenue decreased $640,000 at the two clubs that were closed subsequent to December 31, 2010.

Revenue for 2012 was impacted by the effects of Hurricane Sandy on our business during the fourth quarter of 2012 as a result of lost operating days. At the height of the storm, 131 of our 160 clubs were closed with 16 clubs that remained closed for over a week, one club that permanently closed and one club that recently reopened in December 2013. While it is very difficult to estimate the impact of the storm given the prolonged disruption in most of our markets, we estimate that revenue for 2012 was negatively impacted by approximately $1.0 million as a result of the hurricane.

Personal training revenue increased $3.2 million in the year ended December 31, 2012 compared to the year ended December 31, 2011. This increase was primarily due to increased member interest in personal training sessions, increases in products offered and improvements in the selling process.

Joining fees revenue in 2012 increased $4.8 million compared to 2011 due to the increasing rate of joining fees collected over the past four years. Joining fees collected in the year ended December 31, 2012, 2011, 2010 and 2009 were $11.4 million, $12.9 million, $7.9 million, and $4.0 million, respectively. Joining fees are recognized into revenue over the estimated average membership life

Fees and other revenue increased $914,000 in the year ended December 31, 2012 compared to the year ended December 31, 2011, primarily due to an increase in in-club advertising revenue related to the acceleration of deferred revenue recognized on a terminated arrangement.

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Comparable club revenue increased 1.6% for the year ended December 31, 2012, excluding the $1.2 million accelerated in-club advertising revenue recognized in the third quarter of 2012. There was a 0.8% increase due to an increase in average membership and a 1.8% increase due to a collective increase in ancillary club revenue, initiation fees and other revenue. These increases were partially offset by a 1.0% decrease in the average price of our dues and fees.

Operating Expenses

Operating expenses (in thousands) were comprised of the following for the periods indicated:

	Year Ended December 31, 2012	Year Ended December 31, 2011	$ Variance	% Variance
Payroll and related	$ 181,632	$ 177,528	$ 4,104	2.3%
Club operating	178,950	176,463	2,487	1.4%
General and administrative	24,139	25,799	(1,660)	(6.4)%
Depreciation and amortization	49,391	51,536	(2,145)	(4.2)%
Impairment of fixed assets	3,436		3,436	n/a%
Operating expenses	$ 437,548	$ 431,326	$ 6,222	1.4%

Operating expenses for the year ended December 31, 2012 were impacted by a 0.5% increase in the total months of club operation from 1,886 to 1,896, the effects of which are included in the additional descriptions of changes in operating expenses below.

Payroll and related. This change was primarily impacted by the following factors:

A $2.5 million payroll bonus payment was made during the fourth quarter of 2012 in connection with the special dividend payment in December 2012. Certain option holders with vested in-the-money options as of December 11, 2012 were paid a dividend equivalent cash bonus of $3.00 per option. No such charges were recorded in the year ended December 31, 2011.

Payroll overhead costs increased by $1.1 million for the year ended December 31, 2012 compared to the year ended December 31, 2011. There was a $1.3 million increase in overhead costs primarily attributable to increases in full-time employment levels and higher overhead salaries resulting from the hiring of several new senior management and corporate sales personnel.

As a percentage of total revenue, payroll and related expenses decreased to 37.9% in the year ended December 31, 2012 from 38.0% in the year ended December 31, 2011.

Club operating. This change was primarily impacted by the following factors:

Rent and occupancy expenses increased $3.5 million in the year ended December 31, 2012 compared to the year ended December 31, 2011. Rent and occupancy expenses increased $565,000 at our two clubs that opened after December 31, 2010 and increased $2.7 million at our clubs that opened prior to December 31, 2010. Rent and occupancy expenses decreased $212,000 related to two clubs that were closed after December 31, 2010, excluding $275,000 received in 2011 as an incentive payment from a landlord in connection with a lease termination.

The increase in rent and occupancy expenses were partially offset by lower credit and debit card transaction fees of $1.0 million compared to the prior year due to changes to laws affecting the debit card processing fees that banks can charge.

As a percentage of total revenue, club operating expenses decreased slightly to 37.4% in the year ended December 31, 2012 from 37.8% in the year ended December 31, 2011.

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General and administrative. The decrease in general and administrative expenses for the year ended December 31, 2012 when compared to the year ended December 31, 2011 was principally attributable to the cost reductions within various general and administrative expense accounts including a reduction in general liability insurance, consulting and legal expenses, and office related procurement costs. As a percentage of total revenue, general and administrative expenses decreased to 5.0% in the year ended December 31, 2012 from 5.6% in the year ended December 31, 2011.

Depreciation and amortization. In the year ended December 31, 2012 compared to the year ended December 31, 2011, depreciation and amortization decreased due to a decline in our depreciable fixed asset base. Contributing to this is our limited number of club openings over the past five years. The Company has opened only two clubs over the past three years and the asset base at the remaining 158 clubs is declining as certain clubs move beyond their original lease terms, and other fixed assets become fully amortized. As a percentage of total revenue, depreciation and amortization expenses decreased to 10.3% in the year ended December 31, 2012 from 11.0% in year ended December 31, 2011.

Impairment of fixed assets. In the year ended December 31, 2012, we recorded fixed asset impairment charges totaling $3.4 million, comprised of a $239,000 impairment charge related to one underperforming club and $3.2 million of additional impairments related to the write-down of fixed assets at four clubs that sustained severe damages from Hurricane Sandy. There were no fixed asset impairment charges in the year ended December 31, 2011.

Loss on Extinguishment of Debt

In the year ended December 31, 2012, loss on extinguishment of debt was $1.0 million. The loss on extinguishment of debt was comprised of a $464,000 write-off of net deferred financing costs and debt discount related to the August 22, 2012 debt repricing and a write-off of $546,000 of net deferred financing costs and debt discount in connection with the August 28, 2012 voluntary prepayment of $15.0 million on our term loan facility.

In the year ended December 31, 2011, loss on extinguishment of debt was $4.9 million. The proceeds from the 2011 Senior Credit Facility obtained on May 11, 2011 were used to repay the remaining outstanding principal amount of the 2007 Senior Credit Facility of $164.0 million and the remaining outstanding principal amount of the Senior Discount Notes of $138.45 million. We incurred $2.5 million of call premium on the Senior Discount Notes together with the write-off of $2.4 million of net deferred financing costs related to the debt extinguishment.

Interest Expense

In the year ended December 31, 2012, interest expense was $24.6 million compared to $24.3 million in the year ended December 31, 2011. In 2012, we incurred additional interest expense of $3.0 million related to the repricing amendment in August 2012 and a further amendment in November 2012 to allow for an additional borrowing under our 2011 Senior Credit Facility. This increase in interest expense was partially offset by interest savings recognized from the lower interest rates resulting from the May 11, 2011 refinancing as well as a further interest rate reduction in August 2012 combined with a lower average principal balance of debt outstanding for the majority of 2012.

Provision for Corporate Income Taxes

We recorded a provision for corporate income taxes of $6.3 million for the year ended December 31, 2012 compared to a provision of $2.7 million for the year ended December 31, 2011. Our effective tax rate was 35% in the year ended December 31, 2012 compared to 30% in the year ended December 31, 2011. The expected benefits from our captive insurance arrangement decreased our effective tax rate on our pre-tax income in the year ended December 31, 2012 and 2011.

The results for the year ended December 31, 2012 and December 31, 2011 include error corrections that resulted in an increase in benefit for corporate income taxes and a related increase in deferred tax assets in our consolidated statement of operations and consolidated balance sheet, respectively. In the fourth quarter of 2012, we identified corrections related to temporary differences in fixed assets, intangible assets and deferred revenue resulting in the recognition of an income tax benefit of $483,000. In the fourth quarter of 2011, we identified adjustments related to the tax effect of net operating loss carry-forwards resulting in the recognition of an income tax benefit of $343,000. We do not believe that these error corrections are material to the current or prior reporting periods.

As of December 31, 2012, we had net deferred tax assets of $35.1 million. Quarterly, we assess the weight of all available positive and negative evidence to determine whether the net deferred tax asset is realizable. In 2011, the Company returned to profitability after sustaining losses in 2009 and 2010. We have historically been a taxpayer and are in a three year cumulative income position for federal purposes as of December 31, 2012. In addition, based on recent trends, we project future income sufficient to realize the deferred tax assets during the periods when the temporary tax deductible differences reverse. With the exception of the deductions related to our captive insurance company for state taxes, state taxable income has been and is projected to be the same as federal taxable income. Because we expect the captive insurance company to be discontinued in 2014, the assessment of the realizability of the state deferred tax assets is consistent with the federal tax analysis above. We have federal and state net operating loss and tax credit carry-forwards, which we believe will be realized within the available carry-forward period, except for a small net operating loss carry-forward in Rhode Island due to the short carry-forward period in that state. Accordingly, we concluded that it is more likely than not that the deferred tax assets will be realized. If actual results do not meet our forecasts and we incur lower than expected income or losses in 2013 and beyond, then a valuation allowance against the deferred tax assets may be required in the future.

Liquidity and Capital Resources

Historically, we have satisfied our liquidity needs through cash generated from operations and various borrowing arrangements. Principal liquidity needs have included the acquisition and development of new clubs, debt service requirements, and other capital expenditures necessary to upgrade, expand and renovate existing clubs. In December 2012, we also paid a special cash dividend of $3.00 per share and in December 2013 we instituted what we intend to be a regular quarterly cash dividend of $0.16 per share, with the initial quarterly dividend paid in December 2013 and the second announced in February 2014, which will be paid in March 2014, of $0.16 per share. While it is our intention to pay a quarterly cash dividend in the future, any determination to pay such future dividends will be made by the board of directors and will take into account such matters as cash on hand, general economic and business conditions, our strategic plans, our financial results and condition, contractual, legal and regulatory restrictions on the payment of dividends by us and our subsidiaries and such other factors as our board of directors may consider to be relevant. We believe that our existing cash and cash equivalents, cash generated from operations and our existing credit facility will be sufficient to fund capital expenditures, working capital needs, dividend payments, and other liquidity requirements associated with our operations through at least the next 12 months.

Operating Activities. Net cash provided by operating activities for the year ended December 31, 2013 was $67.4 million compared to $60.1 million for the year ended December 31, 2012, an increase of 12.2%. This increase was driven by a decrease in cash paid for interest of $4.0 million and cash flows from the timing of certain payments and collections made associated with our accounts payable, accrued expenses, accounts receivable and deferred membership costs. The decrease in accounts receivable was primarily due to a change in our billing policy effective January 1, 2013 related mainly to personal training session sales that were previously sold on account. These cash increases were offset by an overall decrease in overall operating results.

Net cash provided by operating activities for the year ended December 31, 2012 was $60.1 million compared to $74.9 million for the year ended December 31, 2011, a decrease of 19.8%. Cash flow related to income taxes decreased operating cash flows as 2011 cash flows benefitted from a net tax refund of $6.6 million while in 2012 net taxes of $836,000 were paid. This decrease was also driven by reductions in cash flows resulting from the timing of payments and collections made associated with prepaid expenses, accounts payable and accrued expenses and deferred revenues.

Investing Activities. Net cash used in investing activities increased 36.1% to $30.6 million in the year ended December 31, 2013 compared to the year ended December 31, 2012. Investing activities in the year ended December 31, 2013 consisted of capital expenditures for the remodeling of existing clubs, the purchase of new fitness equipment and capital investment in information technology. The 2013 amount includes approximately $16.2 million to continue to upgrade existing clubs, $8.0 million principally related to major renovations at clubs with recent lease renewals and upgrading certain clubs for our UXF zones and our in-club entertainment system network, and $1.1 million related to our planned 2014 club openings. In addition, we invested $3.8 million to enhance our management information and communication systems and approximately $195,000 related to our warehouse and laundry facility. Investing activities in the year ended December 31, 2013 also consisted of $2.9 million of net cash paid for the acquisition of clubs and approximately $1.4 million related to renovations at these clubs. These capital investments were partially offset by $3.2 million of insurance proceeds primarily in connection with insurance recoveries related to property damages from Hurricane Sandy.

Net cash used in investing activities decreased 27.2% to $22.5 million in the year ended December 31, 2012 compared to the year ended December 31, 2011. Investing activities in the year ended December 31, 2012 consisted primarily of remodeling existing clubs, the purchase of new fitness equipment and capital investment in information technology. The 2012 amount includes approximately $17.2 million to continue to upgrade existing clubs and $1.6 million principally related to major renovations at clubs with recent lease renewals and upgrading certain clubs for our UXF zones and our in-club entertainment system network. In addition, we invested $2.9 million to enhance our management information and communication systems and approximately $800,000 related to our warehouse and laundry facility.

For the year ending December 31, 2014, we currently plan to invest between $45.0 million and $50.0 million in capital expenditures. This amount includes approximately $20.0 million to $22.0 million related to potential 2014 and 2015 club openings inclusive of amounts for our planned openings of our new BFX Studios. Total capital expenditures also includes approximately $18.0 million to $20.0 million to continue to upgrade existing clubs and $4.0 million to $4.5 million principally related to major renovations at clubs with recent lease renewals and upgrading our in-club entertainment system network. We also expect to invest $3.0 million to $3.2 million to enhance our management information and communication systems. We expect these capital expenditures to be funded by cash flow provided by operations and available cash on hand and the after-tax proceeds from the sale of the East 86th Street property. If such proceeds are not reinvested in our business, we may be required to pay such amounts to pay down our outstanding debt, as provided under the terms of our 2013 Senior Credit Facility.

Financing Activities. Net cash used in financing activities decreased $46.7 million for the year ended December 31, 2013 compared to the year ended December 31, 2012. In the year ended December 31, 2013, we were not required to make the regularly scheduled quarterly principal payments pursuant to our previous 2011 Term Loan Facility (defined below) as a result of a voluntary prepayment made in August 2012 of $15.0 million. In addition, the second amendment to our previous 2011 Senior Credit Facility (defined below) in November 2012 waived the requirement to pay the excess cash flow payment that was due on March 31, 2013. On November 15, 2013, we refinanced our long-term debt. In connection with the refinancing, we repaid the remaining principal amounts of the 2011 Term Loan Facility of $315.7 million received $323.4 million under the 2013 Term Loan Facility (defined below), net of original issue discount (OID) of $1.6 million. In connection with the debt refinancing, we paid $5.1 million in debt issuance costs. We also received $600,000 related to proceeds from stock option exercises in the year ended December 31, 2013, while in the year ended December 31, 2012 we received $2.4 million. In the year ended December 31, 2013, we also paid $4.0 million of dividends comprised of a quarterly dividend of $3.8 million and $296,000 of dividends paid on the vesting of restricted stock. This compares the special dividends paid totaling $70.3 million in the year ended December 31, 2012.

Net cash used in financing activities increased $12.4 million for the year ended December 31, 2012 compared to the year ended December 31, 2011. In the year ended December 31, 2012, we made principal payments of $36.0 million on the 2011 Term Loan Facility, of which $15.0 million was related to a voluntary prepayment made in August 2012. In connection with the repricing amendment in August 2012, we paid related financing costs of $2.7 million. On November 14, 2012, we made further amendments to the 2011 Senior Credit Facility to, among other things, allow for the borrowing of an incremental term loan of $60.0 million which was used together with cash-on-hand to pay a special dividend in December 2012 of $70.3 million. The net proceeds from the incremental term loan were $59.7 million, net of OID of 0.50% or $300,000. In connection with the execution of this additional amendment, we paid additional financing costs of $640,000 related to a 0.25% amendment fee and incurred debt issuance costs of $125,000. We also received $2.4 million related to proceeds from stock option exercises in the year ended December 31, 2012. In the year ended December 31, 2011, we made principal payments of $14.1 million on the 2007 Term Loan Facility (defined below). On May 11, 2011, we refinanced our long-term debt. In connection with the May 11, 2011 refinancing, we repaid the remaining principal amounts of the 2007 Term Loan Facility of $164.0 million and the Senior Discount Notes (defined below) of $138.5 million and received $297.0 million under the 2011 Term Loan Facility, net of the OID of $3.0 million. We also paid $8.1 million in debt issuance costs in connection with this refinancing. In addition, we repaid $8.3 million in principal on the 2011 Term Loan Facility. We also received $479,000 related to proceeds from stock options exercises in the year ended December 31, 2011.

2013 Senior Credit Facility

On November 15, 2013, TSI, LLC, an indirect, wholly-owned subsidiary, entered into a $370.0 million senior secured credit facility (2013 Senior Credit Facility), among TSI, LLC, TSI Holdings II, LLC, a newly-formed, wholly-owned subsidiary of the Company (Holdings II), as a Guarantor, the lenders party thereto, Deutsche Bank AG, as administrative agent, and Keybank National Association, as syndication agent. The 2013 Senior Credit Facility consists of a $325.0 million term loan facility maturing on November 15, 2020 (2013 Term Loan Facility) and a $45.0 million revolving loan facility maturing on November 15, 2018 (2013 Revolving Loan Facility). Proceeds from the 2013 Term Loan Facility of $323.4 million was issued, net of an OID of 0.5%, or $1.6 million. Debt issuance costs recorded in connection with the 2013 Senior Credit Facility was $5.1 million and will be amortized as interest expense and are included in other assets in the accompanying consolidated balance sheets. The proceeds from the 2013 Term Loan Facility were used to pay off amounts outstanding under our previously outstanding long-term debt facility originally entered into on May 11, 2011 (as amended from time to time), and to pay related fees and expenses. None of the revolving loan facility was drawn upon as of the closing date on November 15, 2013, but loans under the 2013 Revolving Loan Facility may be drawn from time to time pursuant to the terms of the 2013 Senior Credit Facility. The borrowings under the 2013 Senior Credit Facility are guaranteed and collateralized by assets and pledges of capital stock by Holdings II, TSI, LLC, and, subject to certain customary exceptions, the wholly-owned domestic subsidiaries of TSI, LLC.

Borrowings under the 2013 Term Loan Facility and the 2013 Revolving Loan Facility, at TSI, LLC s option, bear interest at either the administrative agent s base rate plus 2.5% or a LIBOR rate adjusted for certain additional costs (the Eurodollar Rate) plus 3.5%, each as defined in the 2013 Senior Credit Facility. With respect to outstanding term loans, the Eurodollar Rate has a floor of 1.00% and the base rate has a floor of 2.00%. Commencing with the last business day of the fiscal quarter ending March 31, 2014, TSI, LLC is required to pay 0.25% of the principal amount of the term loans each quarter, which may be reduced by voluntary prepayments.

The terms of the 2013 Senior Credit Facility provide for a financial covenant in the situation where the utilization of the revolving loan commitments (other than letters of credit up to $5.5 million at any time outstanding) exceeds 25% of the commitment. In such event, TSI, LLC is required to maintain a total leverage ratio, as defined in the 2013 Senior Credit Facility, of no greater than 4.50:1.00. The 2013 Senior Credit Facility also contains certain affirmative and negative covenants, including covenants that may limit or restrict TSI, LLC and Holdings II s ability to, among other things, incur indebtedness and other liabilities; create liens; merge or consolidate; dispose of assets; make investments; pay dividends and make payments to shareholders; make payments on certain indebtedness; and enter into sale leaseback transactions, in each case, subject to certain qualifications and exceptions. The 2013 Senior Credit Facility also includes customary events of default (including non-compliance with the covenants or other terms of the 2013 Senior Credit Facility) which may allow the lenders to terminate the commitments under the 2013 Revolving Loan Facility and declare all outstanding term loans and revolving loans immediately due and payable and enforce its rights as a secured creditor.

TSI, LLC may prepay the 2013 Term Loan Facility and 2013 Revolving Loan Facility without premium or penalty in accordance with the 2013 Senior Credit Facility except that a premium of 1.0% is payable for any prepayments made prior to May 15, 2014 in connection with a repricing transaction that reduces the effective yield of the initial term loans. Mandatory prepayments are required relating to certain asset sales, insurance recovery and incurrence of certain other debt and commencing in 2015 in certain circumstances relating to excess cash flow (as defined) for the prior fiscal year, as described below, in excess of certain expenditures. The 2013 Senior Credit Facility contains provisions that require excess cash flow payments, as defined, to be applied against outstanding 2013 Term Loan Facility balances. The excess cash flow is calculated annually commencing with the fiscal year ending December 31, 2014 and paid 95 days after the fiscal year end. The applicable excess cash flow repayment percentage is applied to the excess cash flow when determining the excess cash flow payment. Earnings, changes in working capital and capital expenditure levels all impact the determination of any excess cash flow. The applicable excess cash flow repayment percentage is 50% when the total leverage ratio, as defined in the 2013 Senior Credit Facility, exceeds 2.50:1.00; 25% when the total leverage ratio is greater than 2.00:1.00 but less than or equal to 2.50:1.00 and 0% when the total leverage ratio is less than or equal to 2.00:1.00. The total leverage ratio as of December 31, 2013 was 3.07:1.00. There will be no excess cash flow payment required until April 2015.

As of December 31, 2013, the 2013 Term Loan Facility has a gross principal balance of $325.0 million and a balance of $314.9 million, net of unamortized debt discount of $10.1 million which is comprised of the unamortized portions of the OID recorded in connection with the May 11, 2011 debt issuance and the unamortized balance of the additional debt discounts recorded in connection with the First Amendment and Second Amendment to the 2011 Senior Credit Facility, described below. The unamortized debt discount balance is recorded as a contra-liability to long-term debt on the accompanying consolidated balance sheet and is being amortized as interest expense using the effective interest method. As of December 31, 2013, the unamortized balance of debt issuance costs of $4.4 million is being amortized as interest expense, and is included in other assets in the accompanying consolidated balance sheets.

As of December 31, 2013, there were no outstanding 2013 Revolving Loan Facility borrowings and outstanding letters of credit issued totaled $3.0 million. The unutilized portion of the 2013 Revolving Loan Facility as of December 31, 2013 was $42.0 million.

2011 Senior Credit Facility

TSI, LLC s previously outstanding senior secured credit facility was originally entered into on May 11, 2011 (as amended from time to time) and consisted of a $350.0 million senior secured credit facility (2011 Senior Credit Facility) comprised of a $300.0 million term loan facility (2011 Term Loan Facility) scheduled to mature on May 11, 2018 and a $50.0 million revolving loan facility scheduled to mature on May 11, 2016 (2011 Revolving Loan Facility). The 2011 Term Loan Facility was issued at an OID of 1.0% or $3.0 million and debt issuance costs recorded in connection with the 2011 Senior Credit Facility were $8.1 million. The proceeds from the 2011 Term Loan Facility were used to pay off amounts outstanding under a previously outstanding long-term debt facility entered into in 2007 (2007 Senior Credit Facility), to pay the redemption price on outstanding 11% senior discount notes due in 2014 (Senior Discount Notes), and to pay related fees and expenses. In the year ended December 31, 2011, loss on extinguishment of debt totaling $4.9 million was recorded in connection with the debt refinancing on May 11, 2011 and consisted of the write-off of unamortized debt costs of $1.6 million related to the 2007 Senior Credit Facility and the Senior Discount Notes, $777,000 of costs related to the 2011 Senior Credit Facility and a call premium of $2.5 million related to the early redemption of the Senior Discount Notes.

The 2011 Senior Credit Facility was first amended on August 22, 2012 (First Amendment) to reduce the then-current interest rates on the 2011 Term Loan Facility by 125 basis points and also convert the existing voluntary prepayment penalty provision from a 101 hard call provision (which required the payment of a 1% fee on the amount of any term loans that are voluntarily prepaid), originally scheduled to end in May 2013, to a 101 soft call provision (which required the payment of a 1% fee on the amount of any term loans repaid in connection with a refinancing or repricing transaction) ending in August 2013, and subsequently extended by the November 14, 2012 amendment to November 2013. All other principal provisions, including maturity and covenants under the then-existing 2011 Senior Credit Facility remained unchanged in all material respects. The First Amendment was subject to the consent of term loan lenders. Non-consenting term loan lenders with term loan principal outstanding totaling $13.8 million were replaced with replacement term loan lenders in order to execute the First Amendment. In connection with the pay off of non-consenting term loan lenders, during the year ended December 31, 2012, we recorded a loss on extinguishment of debt of $464,000 consisting of the write-offs of the related portions of unamortized debt issuance costs and OID of $260,000 and $204,000, respectively. In addition, we recorded additional debt discount of $2.7 million related to a 1.00% amendment fee paid to consenting lenders and recognized additional interest expense totaling $1.4 million related primarily to bank and legal related fees paid to third parties to execute the First Amendment.

Subsequent to the effective date of the First Amendment, we made a voluntary prepayment of $15.0 million on the 2011 Term Loan Facility. In connection with this voluntary prepayment, during the year ended December 31, 2012, we recorded loss on extinguishment of debt of $546,000, consisting of the write-offs of the related portions of unamortized debt issuance costs and debt discount of $269,000 and $277,000, respectively.

On November 16, 2012, TSI, LLC entered into a Second Amendment (Second Amendment) to the 2011 Senior Credit Facility. Under the Second Amendment, TSI, LLC borrowed an additional $60.0 million incremental term loan issued at an OID of 0.50% or $300,000. The new borrowings were used, together with cash on hand, to pay a special cash dividend to our stockholders, including an equivalent cash bonus payment to certain option holders, on December 11, 2012. In addition, the Second Amendment provided for a waiver of any prepayment required to be paid using our excess cash flow for the period ended December 31, 2012, amended the restricted payments covenant to permit the payment of the dividend and cash bonus payments and permitted adjustments to our calculation of consolidated EBITDA with respect to the cash bonus payment and with respect to fees and expenses associated with certain permitted transactions. In connection with the execution of the Second Amendment, we recorded additional debt discount of $639,000 related to a 0.25% amendment fee, debt issuance costs of $125,000 and additional interest expense totaling $1.6 million related primarily to bank, arrangement and legal fees paid to third parties.

Repayment of 2011 Senior Credit Facility

Contemporaneously with entry into the 2013 Senior Credit Facility, TSI, LLC repaid the outstanding principal amount of the 2011 Term Loan Facility of $315.7 million. The 2011 Term Loan Facility was set to expire on May 11, 2018. There were no outstanding amounts under the 2011 Revolving Loan Facility as of November 15, 2013, the date of the initial borrowing under the 2013 Senior Credit Facility. The 2011 Term Loan Facility was repaid at face value of $315.7 million plus accrued and unpaid interest of $807,000 and letter of credit fees and commitment fees of $67,000. The total cash paid in connection with this repayment was $316.6 million as of November 15, 2013 with no early repayment penalty. We determined that the 2013 Senior Credit Facility was not substantially different than the 2011 Senior Credit Facility for certain lenders based on the less than 10% difference in cash flows of the respective debt instruments. A portion of the transaction was therefore accounted for as a modification of the 2011 Senior Credit Facility and a portion was accounted for as an extinguishment. As of November 15, 2013, we recorded loss on extinguishment of debt of approximately $750,000, representing the write-off of the remaining unamortized debt costs and debt discount related to the portion of the 2011 Senior Credit Facility that was accounted for as an extinguishment, and is included in loss on extinguishment of debt in the accompanying consolidated statements of operations for the year ended December 31, 2013.

Repayment of 2007 Senior Credit Facility

Contemporaneously with entry into the 2011 Senior Credit Facility, TSI, LLC repaid the outstanding principal amount of the 2007 Term Loan Facility of $164.0 million. The 2007 Term Loan Facility was set to expire on the earlier of February 27, 2014, or August 1, 2013, if the Senior Discount Notes were still outstanding. There were no outstanding amounts under the 2007 Revolving Loan Facility as of such date. The 2007 Term Loan Facility was repaid at face value plus accrued and unpaid interest of $447,000 and fees related to the letters of credit of $27,000. The total cash paid in connection with this repayment was $164.5 million as of May 11, 2011 with no early repayment penalty. We determined that the 2011 Senior Credit Facility was not substantially different than the 2007 Senior Credit Facility for certain lenders based on the less than 10% difference in cash flows of the respective debt instruments. A portion of the transaction was therefore accounted for as a modification of the 2007 Senior Credit Facility and a portion was accounted for as an extinguishment. As of May 11, 2011, we recorded refinancing charges of approximately $634,000, representing the write-off of the remaining unamortized debt costs related to the 2007 Senior Credit Facility, which is included in loss on extinguishment of debt in the accompanying consolidated statements of operations for the year ended December 31, 2011.

Redemption of Senior Discount Notes

A portion of the proceeds from the 2011 Senior Credit Facility were also used to pay the remaining principal amount on the Senior Discount Notes of $138.5 million plus a call premium of 1.833% of the principal amount thereof totaling approximately $2.5 million and accrued interest of $5.5 million. The accrued interest included interest through May 11, 2011 of $4.2 million, plus 30 days of additional interest of $1.3 million, representing the interest charge during the 30 day notification period. We determined that the 2011 Senior Credit Facility was substantially different than the Senior Discount Notes. As of May 11, 2011, we wrote-off unamortized deferred financing costs of approximately $916,000 related to the redemption of the Senior Discount Notes, which is included in loss on extinguishment of debt in the accompanying consolidated statements of operations for the year ended December 31, 2011.

Financial Instruments

In our normal operations, we are exposed to market risks relating to fluctuations in interest rates. In order to minimize the possible negative impact of such fluctuations on our cash flows we may enter into derivative financial instruments (derivatives), such as interest-rate swaps. Any instruments are not entered into for trading purposes and we only use commonly traded instruments. Currently, we have used derivatives solely relating to the variability of cash flows from interest rate fluctuations.

We originally entered into our interest rate swap arrangement on July 13, 2011 in connection with the 2011 Senior Credit Facility. We entered into an interest rate swap arrangement which effectively converted $150.0 million of our variable-rate debt based on a one-month Eurodollar rate to a fixed rate of 1.983%, or a total fixed rate of 7.483%, on this $150.0 million when including the applicable 5.50% margin that was in effect under the 2011 Senior Credit Facility at that time. In August 2012, we amended the terms of the 2011 Senior Credit Facility to, among other things, reduce the applicable margin on Eurodollar rate loans from 5.50% to 4.50% and reduce the interest rate floor on Eurodollar rate loans from 1.50% to 1.25%. In conjunction with the First Amendment to the 2011 Senior Credit Facility in August 2012, the interest rate swap arrangement was amended to reduce the one-month Eurodollar fixed rate from 1.983% to 1.783%, or a total fixed rate of 6.283% when including the applicable 4.50% margin on Eurodollar rate loans in effect under the 2011 Senior Credit Facility at that time. On November 14, 2012, we further amended the terms of the 2011 Senior Credit Facility to, among other things, allow for the borrowing of a $60.0 million incremental term loan. In connection with the Second Amendment to the 2011 Credit Facility, we further amended the interest rate swap to increase the notional amount to $160.0 million and extended the maturity of the swap to from July 13, 2014 to May 13, 2015. In addition, the one-month Eurodollar fixed rate was lowered from 1.783% to 1.693%, or a total of 6.193% when including the applicable 4.50% margin on Eurodollar rate loans in effect under the 2011 Senior Credit Facility at that time. In connection with entering into the 2013 Senior Credit Facility, we amended and restated the interest rate swap arrangement it initially entered into on July 13, 2011 (and amended in August 2012 and November 2012). Effective as of November 15, 2013, the closing date of the 2013 Senior Credit Facility, the interest rate swap will continue to have a notional amount of $160.0 million and will mature on May 15, 2018. The swap effectively converts $160.0 million of the $325.0 million total variable-rate debt under the 2013 Senior Credit Facility to a fixed rate of 5.384%, when including the applicable 3.50% margin. As permitted by FASB Accounting Standards Codification (ASC) 815, Derivatives and Hedging, we have designated this swap as a cash flow hedge, the effects of which have been reflected in our consolidated financial statements as of and for the years ended December 31, 2013, 2012 and 2011. The objective of this hedge is to manage the variability of cash flows in the interest payments related to the portion of the variable-rate debt designated as being hedged.

When our derivative was executed hedge accounting was deemed appropriate and it was designated as a cash flow hedge at inception with re-designation being permitted under ASC 815, Derivatives and Hedging. Interest rate swaps are designated as cash flow hedges for accounting purposes since they are being used to transform variable interest rate exposure to fixed interest rate exposure on a recognized liability (debt). On an ongoing basis, we perform a quarterly assessment of the hedge effectiveness of the hedge relationship and measure and recognize any hedge ineffectiveness in the consolidated statements of operations. For the years ended December 31, 2013, 2012 and 2011, hedge ineffectiveness was evaluated using the hypothetical derivative method. There was no hedge ineffectiveness in the years ended December 31, 2013 and 2011, and the amount related to hedge ineffectiveness for the year ended December 31, 2012 was de minimis.

Counterparties to our derivatives are major banking institutions with credit ratings of investment grade or better and no collateral is required, and there are no significant risk concentrations. We believe the risk of incurring losses on derivative contracts related to credit risk is unlikely.

As of December 31, 2013, we were in compliance with our debt covenants in the 2013 Senior Credit Facility. These covenants may limit TSI, LLC s ability to incur additional debt. As of December 31, 2013, permitted borrowing capacity of $45.0 million was not restricted by the covenants.

As of December 31, 2013, we had $73.6 million of cash and cash equivalents. Financial instruments that potentially subject us to concentrations of credit risk consist of cash and cash equivalents. Although we deposit our cash with more than one financial institution, as of December 31, 2013, $54.2 million was held at one financial institution. We have not experienced any losses on cash and cash equivalent accounts to date and we do not believe that, based on the credit ratings of the aforementioned institutions, we are exposed to any significant credit risk related to cash at this time.

Consolidated Debt

As of December 31, 2013, our total principal amount of debt outstanding was $325.0 million. This substantial amount of debt could have significant consequences, including:

- making it more difficult to satisfy our obligations with respect to our outstanding indebtedness;
- increasing our vulnerability to general adverse economic and industry conditions;
- limiting our ability to obtain additional financing to fund future working capital, capital expenditures, acquisitions of new clubs and other general corporate requirements;
- requiring a substantial portion of our cash flow from operations for the payment of interest on our debt, which is variable on our 2013 Revolving Loan Facility and partially variable on our 2013 Term Loan

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Facility, and/or principal pursuant to excess cash flow requirements and reducing our ability to use our cash flow to fund working capital, capital expenditures and acquisitions of new clubs and general corporate requirements;

increasing our vulnerability to interest rate fluctuations in connection with borrowings under our 2013 Senior Credit Facility, some of which are at variable interest rates;

limiting our ability to refinance our existing indebtedness on favorable terms, or at all; and

limiting our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate.

These limitations and consequences may place us at a competitive disadvantage to other less-leveraged competitors.

We believe that we have, or will be able to, obtain or generate sufficient funds to finance our current operating and growth plans through the next 12 months. Any material acceleration or expansion of our plans through newly constructed clubs or acquisitions (to the extent such acquisitions include cash payments) may require us to pursue additional sources of financing prior to the end of 2014. There can be no assurance that such financing will be available, or that it will be available on acceptable terms.

Contractual Obligations and Commitments

The aggregate long-term debt and operating lease obligations as of December 31, 2013 were as follows:

	Payments Due by Period (in thousands)				
Contractual Obligations(4)	**Total**	**Less than 1 Year**	**1-3 Years**	**3-5 Years**	**More than 5 Years**
Long-term debt(1)	$ 325,000	$ 3,250	$ 6,500	$ 6,500	$ 308,750
Interest payments on long-term debt(2)	104,548	16,200	31,954	30,223	26,171
Operating lease obligations(3)	654,839	88,983	169,500	138,007	258,349
Total contractual cash obligations	$ 1,084,387	$ 108,433	$ 207,954	$ 174,730	$ 593,270

Notes:

(1) Principal amounts paid each year will increase as annual excess cash flow amounts are required (as described above). There are no excess cash flow payments required until April 2015.

(2) Based on interest rates pursuant to the 2013 Term Loan Facility and the interest swap agreement as of December 31, 2013.

(3) Operating lease obligations include base rent only. Certain leases provide for additional rent based on real estate taxes, common area maintenance and defined amounts based on the operating results of the lessee.

(4) The table above does not include any future obligations that would result in connection with the sale agreement that was entered in December 2013 related to the sale of our property located on East 86th Street in New York as this sale is subject to adjustment, and is expected to close on or about March 31, 2014.

The following long-term liabilities included on the consolidated balance sheet are excluded from the table above: income taxes (including uncertain tax positions), insurance accruals and other accruals. We are unable to estimate the timing of payments for these items.

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In recent years, we have typically operated with a working capital deficit. We had working capital of $27.8 million at December 31, 2013, as compared with a working capital deficit of $11.8 million at December 31, 2012. Major components of our working capital on the current liability side are deferred revenues, accounts payable, accrued expenses (including, among others, accrued construction in progress and equipment, payroll and occupancy costs) and the current portion of long-term debt. As of December 31, 2012, these current liabilities more than offset the main current assets, which consist of cash and cash equivalents, accounts receivable, prepaid expenses and other current assets, and the current portion of deferred tax assets. Payments underlying the current liability for deferred revenue are generally not held as cash and cash equivalents, but rather are used for our business needs, including financing and investing commitments, which use contributes to the working capital deficit. The deferred revenue liability relates to dues and services paid-in-full in advance and joining fees paid at the time of enrollment and totaled $33.9 million and $37.1 million at December 31, 2013 and 2012, respectively. Joining fees received are deferred and amortized over the estimated average membership life of a club member. Prepaid dues are generally realized over a period of up to twelve months, while fees for prepaid services normally are realized over a period of one to nine months. In periods when we increase the number of clubs open and consequently increase the level of payments received in advance, we would expect to see increased deferred revenue balances. By contrast, any decrease in demand for our services or reductions in joining fees collected would have the effect of reducing deferred revenue balances, which would likely require us to rely more heavily on other sources of funding. In either case, a significant portion of the deferred revenue is not expected to constitute a liability that must be funded with cash. At the time a member joins our club, we incur enrollment costs, a portion of which are deferred over the estimated average membership life. These costs are recorded as a long-term asset and as such do not offset working capital. Should we record a working capital deficit in future periods, as in the past, we will fund such deficit using cash flows from operations and borrowings under our 2013 Senior Credit Facility. We believe that these sources will be sufficient to cover such deficit.

Recent Changes in or Recently Issued Accounting Standards

For details of applicable new accounting standards, please, see Note 4 Recent Accounting Pronouncements to our consolidated financial statements in this Annual Report.

Use of Estimates and Critical Accounting Policies

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

Our most significant assumptions and estimates relate to estimated average membership life, the allocation and fair value ascribed to fixed and intangible assets, the useful lives of long-term assets, recoverability and impairment of fixed and intangible assets, valuation of and expense incurred in connection with stock options, valuation of interest-rate swap arrangements, legal contingencies, estimated self-insurance reserves, and valuation of deferred income taxes.

Estimated average membership life. Our one-time member joining fees and a portion of related direct expenses, up to the amount of total deferred joining fees, are deferred and recognized on a straight-line basis in operations over our current estimated average membership life of 23 months for our unrestricted members and 28 months for our restricted members. We monitor factors that might affect the estimated average membership life including retention trends, attrition trends, membership sales volumes, membership composition, competition, and general economic conditions, and adjust the estimate on a quarterly basis. The estimated average membership life could increase or decrease in future periods. Consequently, deferred initiation fees and direct expenses would increase or decrease accordingly.

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Fixed and intangible assets. Fixed assets are recorded at cost and depreciated on a straight-line basis over the estimated useful lives of the assets, which are 30 years for building and improvements, five years for club equipment, furniture, fixtures, flooring and computer equipment and three to five years for computer software. Leasehold improvements are amortized over the shorter of their estimated useful lives or the remaining period of the lease. Expenditures for maintenance and repairs are charged to operations as incurred. The cost and related accumulated depreciation, or amortization of assets retired or sold, are removed from the respective accounts and any gain or loss is recognized in operations. The costs related to developing web applications, developing web pages and installing developed applications on the web servers are capitalized and classified as computer software. Web site hosting fees and maintenance costs are expensed as incurred.

Long-lived assets, such as fixed assets and intangible assets are reviewed for impairment when events or circumstances indicate that the carrying value may not be recoverable. Our long-lived assets are grouped at the individual club level which is the lowest level for which there are identifiable cash flows. Estimated undiscounted expected future cash flows are used to determine if an asset group is impaired, in which case the asset s carrying value would be reduced to its fair value, calculated using discounted cash flows. Projected cash flows are based on internal budgets and forecasts through the end of each respective lease. The most significant assumptions in those budgets and forecasts relate to estimated membership and ancillary revenue, attrition rates, and maintenance capital expenditures, which are generally estimated at approximately 3% to 5% of total revenue. Actual cash flows realized could differ from those estimated and could result in asset impairments in the future. See Note 5 Fixed Assets to our consolidated financial statements in this Annual Report. Due unforeseen to poor performance and lower than expected membership results experienced in January 2014, the Company anticipates having fixed asset impairment in the first quarter of 2014.

Goodwill has been allocated to reporting units that closely reflect the regions served by our four trade names: New York Sports Clubs (NYSC), Boston Sports Clubs (BSC), Washington Sports Clubs (WSC) and Philadelphia Sports Clubs (PSC), with certain more remote clubs that do not benefit from a regional cluster being considered single reporting units (Outlier Clubs) and our three clubs located in Switzerland (SSC). We have one Outlier Club with goodwill. The BSC, WSC and PSC regions do not have any goodwill as of December 31, 2013. The carrying value of goodwill was allocated to our reporting units pursuant to FASB guidance.

As of February 28, 2013 and February 29, 2012, we performed our annual impairment test of goodwill. These impairment tests supported the recorded goodwill balances and as such no impairment of goodwill was required. The valuation of intangible assets requires assumptions and estimates of many critical factors, including revenue and market growth, operating cash flows and discount rates. We will complete an interim evaluation of the goodwill by reporting unit if a triggering event exists. The determination as to whether a triggering event exists that would warrant an interim review of goodwill and whether a write-down of goodwill is necessary involves significant judgment based on short-term and long-term projections of the Company.

Legal contingencies. In accordance with FASB guidance, we determine whether to disclose and accrue for loss contingencies based on an assessment of whether the risk of loss is remote, reasonably possible or probable. Our assessment is developed in consultation with our outside counsel and other advisors and is based on an analysis of possible outcomes under various strategies. Loss contingency assumptions involve judgments that are inherently subjective and can involve matters that are in litigation, which, by its nature are unpredictable. We believe that our assessment of the probability of loss contingencies is reasonable, but because of the subjectivity involved and the unpredictable nature of the subject matter at issue, our assessment may prove ultimately to be incorrect, which could materially impact the consolidated financial statements.

Self-insurance reserves. We limit our exposure to casualty losses on insurance claims by maintaining liability coverage subject to specific and aggregate liability deductibles. Self-insurance losses for claims filed and claims incurred but not reported are accrued based upon a number of factors including sales estimates for each insurance year, claim amounts, claim settlements and number of claims, our historical loss experience and valuations provided by independent third-party consultants. To the extent that estimated self-insurance losses

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differ from actual losses realized, our insurance reserves could differ significantly and may result in either higher or lower insurance expense in future periods.

Deferred income taxes. As of December 31, 2013, our net deferred tax assets totaled $28.4 million. These net assets represent cumulative net temporary differences that will result in tax deductions in future years. Quarterly, we assess whether a valuation allowance is required based on the weight of all positive and negative evidence to determine whether it is more likely than not that the net deferred tax asset will be realized. We have historically been a taxpayer and are in a three year cumulative income position as of December 31, 2013 for both federal and certain state jurisdictions. In addition, based on recent trends, we project future income sufficient to realize the deferred tax assets during the periods when the temporary tax deductible differences reverse. With the exception of the deductions related to our captive insurance company for state taxes, taxable income has been and is projected to be the same as federal taxable income. Because we expect to discontinue the captive insurance company as of December 31, 2014, the assessment of realizability of the state deferred tax assets is consistent with the federal tax analysis above. We have state net operating loss carry-forwards which we believe will be realized within the available carry-forward period, except for a small net operating loss forward in Rhode Island due to the short carry forward period in that state. Accordingly, we concluded that it is more likely than not that the deferred tax assets will be realized. If actual results do not meet our forecasts and we incur losses in 2014 and beyond, a valuation allowance against the deferred tax assets may be required in the future.

FASB guidance related to accounting for uncertain tax positions prescribes a recognition threshold and measurement attribute for a tax position taken or expected to be taken in a tax return and also provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. We recognize interest and penalties accrued related to unrecognized tax benefits in income tax expense.

Inflation

Although we cannot accurately anticipate the effect of inflation on our operations, we believe that inflation has not had a material impact on our results of operations or financial condition. Should there be periods of high inflation in the future, our results of operations or financial condition would be exposed to the effects of inflation, such as higher rents for our leases under escalation terms based on the consumer price index and higher interest expense on the variable rate portion of our debt.

Item 7A. ***Quantitative and Qualitative Disclosures About Market Risk***

Our debt is effectively at both fixed and variable rates so that we are exposed to market risks resulting from interest rate fluctuations. We regularly evaluate our exposure to these risks and take measures to mitigate these risks on our consolidated financial results. We do not participate in speculative derivative trading.

Borrowings for the 2013 Term Loan Facility are for one-month periods in the case of Eurodollar borrowings. Our exposure to market risk for changes in interest rates relates to interest expense on variable rate debt. As of December 31, 2013, we had $325.0 million of outstanding borrowings under our 2013 Term Loan Facility of which $160.0 million of this variable rate debt is hedged to a fixed rate under an interest rate swap agreement. Changes in the fair value of the interest rate swap derivative instrument is recorded each period in accumulated other comprehensive income (loss). Based on the amount of our variable rate debt and our interest rate swap agreement as of December 31, 2013, a hypothetical 100 basis point interest increase would have increased our interest cost by approximately $285,000.

For additional information concerning the terms of our 2013 Term Loan Facility, see Note 9 Long-Term Debt to our consolidated financial statements in this Annual Report.

Item 8. ***Financial Statements and Supplementary Data***

Our Financial Statements appear following the signature page hereto, are incorporated herein by reference and are listed in the index appearing under Item 15.

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Item 9. ***Changes in and Disagreements with Accountants on Accounting and Financial Disclosure***
None

Item 9A. ***Controls and Procedures***
Evaluation of Disclosure Controls and Procedures: Disclosure controls and procedures are designed to ensure that the information required to be disclosed in reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and the Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. Any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired controls.

As of December 31, 2013, we carried out an evaluation, under the supervision and with the participation of our management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act). Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of December 31, 2013, our disclosure controls and procedures were not effective at the reasonable assurance level, because of the material weakness in the Company s internal control over financial reporting described below. This material weakness did not result in any audit adjustments or misstatements.

Management s Annual Report on Internal Control Over Financial Reporting: Our management is responsible for establishing and maintaining adequate internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act).

Internal control over financial reporting is defined as a process to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with generally accepted accounting principles. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we assessed the effectiveness of our internal control over financial reporting as of December 31, 2013. In making this assessment, our management used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control Integrated Framework* (1992 Framework). Based on our management s assessment using those criteria, our management concluded that a material weakness in internal control over financial reporting existed as of December 31, 2013 as described below, and that as a result, our internal control over financial reporting was not effective as of December 31, 2013. A material weakness is defined as a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the registrant s annual or interim financial statements will not be prevented or detected on a timely basis.

The material weakness is that certain accounting personnel have system access to both create and post journal entries to substantially all of the key accounts as of December 31, 2013 which are not subject to an independent review process.

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The material weakness did not result in any adjustments or misstatements. However, this material weakness could result in a material misstatement of the annual or interim consolidated financial statements that would not have been prevented or detected.

PricewaterhouseCoopers LLP, our independent registered public accounting firm, has audited the effectiveness of our internal control over financial reporting as of December 31, 2013, as stated in their report included following the signature page hereto, included in Item 15.

Remediation: We are in the process of addressing the access of these accounting personnel and will establish access limitations specific to job functions and roles that we believe will address the risks described above. This will include removing the ability for any member of the accounting department to both create and post journal entries without independent review. We believe that the design, implementation and testing of this control, which we expect to be implemented during the first and second quarters of 2014, should remediate the material weakness. Until such time as such procedures have been completed and verified, we will continue to perform manual reviews of all journal entries posted by accounting personnel with this access.

Changes in Internal Control Over Financial Reporting: As described below, there have been changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended December 31, 2013 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Prior to December 31, 2013, we had maintained an independent review process for any manual journal entries initiated by accounting personnel with the ability to both create and post such entries. Following December 31, 2013, we removed the independent review process and sought to limit the access of such individuals such that they no longer could both create and post manual journal entries. However, certain accounting personnel continued to have system access to both create and post such entries to substantially all of the key accounts as of December 31, 2013, which were then no longer subject to the independent review process. We have been able to determine that there were no journal entries actually created and posted by these accounting personnel during the time when there was no independent review process.

Item 9B. Other Information

None.

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PART III

Item 10. ***Directors, Executive Officers and Corporate Governance***

The information with respect to directors, executive officers and corporate governance of the Company is incorporated herein by reference to the following sections of the Company s definitive Proxy Statement relating to the Company s 2014 Annual Meeting of Stockholders to be filed with the SEC within 120 days of the Company s fiscal year ended December 31, 2013 (the Proxy Statement): Matters to be Considered at Annual Meeting Proposal One Election of Directors, Corporate Governance and Board Matters Corporate Governance Documents, Corporate Governance and Board Matters Committee Membership Audit Committee, Section 16(A) Beneficial Ownership Reporting Compliance, Executive Officers, and Deadline for Receipt of Stockholder Proposals.

The following are the members of our Board of Directors and our Executive Officers:

Board of Directors:	
Robert Giardina	Chief Executive Officer, Town Sports International Holdings, Inc.
Paul N. Arnold	Former Chairman of the Board and Chief Executive Officer, Cort Business Services, Inc.
Bruce C. Bruckmann	Managing Director, Bruckmann, Rosser, Sherrill & Co., LP
J. Rice Edmonds	Managing Director, Edmonds Capital, LLC
John H. Flood III	Chief Executive Officer, Synergy Global Outsourcing, LLC
Thomas J. Galligan III	Former Executive Chairman, Papa Gino s Holdings Corp.
Kevin McCall	Chief Executive Officer and President, Paradigm Properties, LLC
Executive Officers:	
Robert Giardina	Chief Executive Officer
Daniel Gallagher	President, Chief Operating Officer and Chief Financial Officer
Paul Barron	Senior Vice President Chief Information Officer
David M. Kastin	Senior Vice President General Counsel and Corporate Secretary
Scott Milford	Senior Vice President Human Resources

Item 11. ***Executive Compensation***

The information with respect to executive compensation is incorporated herein by reference to the following sections of the Proxy Statement: Executive Compensation and Corporate Governance and Board Matters Compensation Committee Interlocks and Insider Participation.

The information with respect to compensation of directors is incorporated herein by reference to the following section of the Proxy Statement: Corporate Governance and Board Matters Directors Compensation for the 2013 Fiscal Year.

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Item 12. ***Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters***
Securities Authorized for Issuance Under Equity Compensation Plans

The following table provides information with respect to compensation plans (including individual compensation arrangements) under which our equity securities are authorized for issuance to employees as of December 31, 2013:

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights (a)	Weighted-Average Exercise Price of Outstanding Options, Warrants and Rights (b)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column(a)) (c)
Equity compensation plans approved by security holders	1,140,231	$ 5.29	423,239
Equity compensation plans not approved by security holders			
Total	1,140,231	$ 5.29	423,239

The information with respect to security ownership of certain beneficial owners and management is incorporated herein by reference to the following section of the Proxy Statement: Ownership of Securities.

Item 13. ***Certain Relationships and Related Transactions, and Director Independence***
The information with respect to certain relationships and related transactions and director independence is incorporated herein by reference to the following sections of the Proxy Statement: Certain Relationships and Related Transactions and Corporate Governance and Board Matters Director Independence.

Item 14. ***Principal Accountant Fees and Services***
The information with respect to principal accountant fees and services is incorporated herein by reference to the following section of the Proxy Statement: Matters to be Considered at Annual Meeting Proposal Two Ratification of Independent Registered Public Accounting Firm.

PART IV

Item 15. ***Exhibits And Financial Statements***

(a) *Financial Statements*

(1) Financial statements filed as part of this report:

(2) Financial Statements Schedules:

The schedules have been omitted because they are not applicable or the required information has been included in the financial statements or notes thereto.

(3) Exhibits. See Item 15(b) below.

(b) *Exhibits required by Item 601 of Regulation S-K*

The information required by this item is incorporated herein by reference from the Index to Exhibits immediately following page F-41 of this Annual Report.

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized, on March 14, 2014.

TOWN SPORTS INTERNATIONAL HOLDINGS, INC.

By: /s/ ROBERT GIARDINA

Chief Executive Officer
(principal executive officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

Signature	Title	Date
By: /s/ ROBERT GIARDINA Robert Giardina	Chief Executive Officer (principal executive officer) and Director	March 14, 2014
By: /s/ DANIEL GALLAGHER Daniel Gallagher	President, Chief Operating Officer and Chief Financial Officer (principal financial and accounting officer)	March 14, 2014
By: /s/ PAUL ARNOLD Paul Arnold	Director	March 14, 2014
By: /s/ BRUCE BRUCKMANN Bruce Bruckmann	Director	March 14, 2014
By: /s/ J. RICE EDMONDS J. Rice Edmonds	Director	March 14, 2014
By: /s/ JOHN H. FLOOD III John H. Flood III	Director	March 14, 2014
By: /s/ THOMAS J. GALLIGAN III Thomas J. Galligan III	Director	March 14, 2014
By: /s/ KEVIN MCCALL Kevin McCall	Director	March 14, 2014

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Report of Independent Registered Public Accounting Firm

To the Board of Directors and Stockholders of

Town Sports International Holdings, Inc.:

In our opinion, the accompanying consolidated balance sheets and the related consolidated statements of operations, comprehensive income, stockholders (deficit) equity and cash flows present fairly, in all material respects, the financial position of Town Sports International Holdings, Inc. and its subsidiaries at December 31, 2013 and 2012, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2013 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, the Company did not maintain, in all material respects, effective internal control over financial reporting as of December 31, 2013, based on criteria established in *Internal Control Integrated Framework* (1992 Framework) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) because a material weakness in internal control over financial reporting related to the ability of certain accounting personnel to create and post journal entries without an independent review existed as of that date. A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weakness referred to above is described in Management s Annual Report on Internal Control Over Financial Reporting appearing under Item 9A. We considered this material weakness in determining the nature, timing and extent of audit tests applied in our audit of the 2013 consolidated financial statements, and our opinion regarding the effectiveness of the Company s internal control over financial reporting does not affect our opinion on those financial statements. The Company s management is responsible for these financial statements, for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in management s report referred to above. Our responsibility is to express opinions on these financial statements and on the Company s internal control over financial reporting based on our integrated audits. We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company s internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company s internal control over financial reporting includes those policies and procedures that (i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company s assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

/s/ PricewaterhouseCoopers LLP

New York, New York

March 14, 2014

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TOWN SPORTS INTERNATIONAL HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

As of December 31, 2013 and 2012

(All figures in thousands except share data)

	2013	2012
ASSETS		
Current assets:		
Cash and cash equivalents	$ 73,598	$ 37,758
Accounts receivable, net	3,704	6,508
Inventory	473	438
Deferred tax assets, net	17,010	19,325
Prepaid corporate income taxes	6	550
Prepaid expenses and other current assets	10,850	11,435
Total current assets	105,641	76,014
Fixed assets, net	243,992	256,871
Goodwill	32,870	32,824
Intangible assets, net	908	
Deferred tax assets, net	11,340	15,728
Deferred membership costs	8,725	10,811
Other assets	10,316	12,522
Total assets	$ 413,792	$ 404,770
LIABILITIES AND STOCKHOLDERS DEFICIT		
Current liabilities:		
Current portion of long-term debt	$ 3,250	$ 15,787
Accounts payable	8,116	7,467
Accrued expenses	31,536	27,053
Accrued interest	737	89
Dividends payable	259	305
Deferred revenue	33,913	37,138
Total current liabilities	77,811	87,839
Long-term debt	311,659	294,552
Dividends payable	407	799
Deferred lease liabilities	56,882	61,732
Deferred revenue	2,460	3,889
Other liabilities	8,089	11,455
Total liabilities	457,308	460,266
Contingencies (Note 15)		
Stockholders (deficit) equity:		
Common stock, $.001 par value; issued and outstanding 24,072,705 and 23,813,106 shares at December 31, 2013 and December 31, 2012, respectively	24	24
Additional paid-in capital	(13,846)	(16,326)
Accumulated other comprehensive income	2,052	1,226
Accumulated deficit	(31,746)	(40,420)
Total stockholders deficit	(43,516)	(55,496)

Total liabilities and stockholders deficit	$ 413,792	$ 404,770

See notes to consolidated financial statements.

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TOWN SPORTS INTERNATIONAL HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

Years Ended December 31, 2013, 2012 and 2011

(All figures in thousands except share and per share data)

	2013	2012	2011
Revenues:			
Club operations	$ 464,240	$ 473,177	$ 462,051
Fees and other	5,985	5,804	4,890
	470,225	478,981	466,941
Operating Expenses:			
Payroll and related	174,894	181,632	177,528
Club operating	179,683	178,950	176,463
General and administrative	28,431	24,139	25,799
Depreciation and amortization	49,099	49,391	51,536
Insurance recovery related to damaged property	(3,194)		
Impairment of fixed assets	714	3,436	
	429,627	437,548	431,326
Operating income	40,598	41,433	35,615
Loss on extinguishment of debt	750	1,010	4,865
Interest expense	22,617	24,640	24,274
Interest income	(1)	(43)	(147)
Equity in the earnings of investees and rental income	(2,459)	(2,461)	(2,391)
Income before provision for corporate income taxes	19,691	18,287	9,014
Provision for corporate income taxes	7,367	6,321	2,699
Net income	$ 12,324	$ 11,966	$ 6,315
Earnings per share:			
Basic	$ 0.51	$ 0.51	$ 0.28
Diluted	$ 0.50	$ 0.50	$ 0.27
Weighted average number of shares used in calculating earnings per share:			
Basic	24,031,533	23,436,393	22,828,031
Diluted	24,736,961	24,114,540	23,423,797
Dividends declared per common share	$ 0.16	$ 3.00	$

See notes to consolidated financial statements.

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TOWN SPORTS INTERNATIONAL HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Years Ended December 31, 2013, 2012 and 2011

(All figures in thousands)

	2013	2012	2011
Net income	$ 12,324	$ 11,966	$ 6,315
Other comprehensive (loss) income, net of tax:			
Foreign currency translation adjustments, net of tax of ($49), $0 and $777 for the years ended December 31, 2013, 2012 and 2011, respectively	68	95	(129)
Interest rate swap, net of tax of ($583), $61 and $601 for the years ended December 31, 2013, 2012 and 2011, respectively	758	(120)	(741)
Total other comprehensive income (loss), net of tax	826	(25)	(870)
Total comprehensive income	$ 13,150	$ 11,941	$ 5,445

See notes to consolidated financial statements.

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TOWN SPORTS INTERNATIONAL HOLDINGS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS (DEFICIT) EQUITY

Years Ended December 31, 2013, 2012 and 2011

(All figures in thousands except share and per share data)

	Common Stock ($.001 par)	Additional Paid-in Capital