

# nerej

## **Shout "as One!" Line up the teams, "single column...single column," and close.**

September 18, 2014 - Front Section

We have all seen the cartoon depicting a canoe occupied by each of the parties to a real estate closing. In the first panel they are shown holding paddles poised above the water. In the next panel, the coxswain shouts "close," whereupon the occupants flail their paddles in conflicting directions. Closing on the acquisition of a hotel is a more complex process, with more occupants in the canoe. Avoiding the consequences in the cartoon depends upon close coordination among all members of the acquisition and disposition teams, best described by the character "Maximus" from the movie *Gladiator*. As Maximus and his men emerge onto the floor of the Coliseum, awaiting the opponents who will soon burst from the gates surrounding the floor, Maximus says "the only chance we have of surviving whatever comes through those gates is if we all work together."

Members of both teams will typically include the deal person, the lawyer, an operations officer, an IP/IT professional, human resources, accountants, a general manager, a lender and its counsel, a hotel brand and its counsel, and a hotel management company and its counsel. All of these professionals must work in close coordination to ensure that the hotel's operating business transitions from one owner to another with minimal disruption or error.

An orderly closing begins with the purchase and sale agreement, which should describe the process in great detail and tell the parties exactly how to allocate and deal with all hotel property, leases, employees, revenue, expense, guest property, bookings, inventory, supplies, receivables, payables, licenses and permits, any incoming or outgoing brands, software, and taxes. The lawyers drafting the document must have input from each of the team members on those sections within each member's expertise. While there are customs in the hotel industry as to how certain items are handled, every deal is different, and it is not possible to default to "customary closing adjustments" as it may be in the general real estate industry. The closing adjustments section of a hotel purchase and sale agreement usually occupies at least several pages of the document.

Hotel employees (which may be employed either by the seller or by its management company) will need to be discharged by the seller, and in most cases, offered employment by the buyer in sufficient numbers to avoid WARN Act issues for the seller. A decision must be made in the Purchase and Sale Agreement as to whether seller will pay out at closing all accrued "paid time off" (PTO) or whether the same will roll forward with buyer receiving a credit. Most often, the former option will be chosen to give the buyer a clean start. Representatives of seller and buyer will call an "all hands" meeting with the employees on the day of the closing to announce the sale and implement the transition. The nature of the message given at that meeting will need to have been worked out before-hand between those representatives. Typically, the employees will have figured out that all the people trooping through their hotel means something major is about to happen and will inevitably get nervous about their jobs. Thus, the meeting and messaging is the buyer's best

opportunity to get off to a good start with those employees.

Unless the buyer is planning to close the hotel for renovations immediately following the closing, it must obligate the seller to deliver a fully equipped and functioning hotel so that the transition into buyer's ownership can be as seamless as possible. If the buyer is planning to close the hotel, the seller and buyer teams will need to cooperate to move all post-closing bookings to other hotel facilities. The Purchase and Sale Agreement should obligate the seller to operate the hotel as it had been operated and to maintain adequate levels of inventory and supplies, all of which will be accounted for during a walk-through of the hotel which will occur the evening before the closing. If you can visualize teams of accountants counting bars of soap, bed linens, and flatware you'll have a pretty accurate picture of what happens. Often, the seller will receive a credit at actual cost for "unopened" inventory and supplies. A fellow attorney relayed to me the story of his accompanying the accountants for buyer and seller during their pre-closing inspection and witnessing a fist-fight break out between them over whether a large and expensive side of beef which had been unwrapped, but not yet carved, was "unopened." This is to be avoided.

All property management, reservation and credit card processing systems will need to be reprogrammed or replaced on the day of closing to ensure that the buyer actually receives the hotel revenue it just bought. Sales, rooms, and other state and local taxes will need to be collected as in the past, but there may be registration requirements that have to be observed by buyer to ensure ongoing compliance. Add in a hotel brand that will not be continuing with buyer, a new hotel brand that will re-flag the hotel, and a lender that requires full cash-management controls over hotel revenue, and the IT/IP and operations professionals are in for a long day indeed.

After such a long day, the first place the teams will want to go to relax is the hotel bar, which is now owned by the buyer. Unfortunately, the buyer cannot sell alcoholic beverages because it does not yet hold the hotel's liquor license. While application for transfer or issuance of a liquor license may have been made prior to closing, typically, the liquor license does not vest in buyer until some number of days or months following closing. The buyer cannot receive revenue from liquor sales until it is licensed. The work-around for this situation in common use is a so-called "Interim Beverage Management Agreement," wherein the buyer agrees to manage the licensed facilities for the outgoing seller at a fee set as close as possible to the estimated revenue from liquor operations without being an exact match. Hotels require a panoply of other licenses and permits not encountered with other types of real estate, such as common victualer's, safe serve, pool, spa, live entertainment, place of assembly, milk storage, pool table, automated amusement, and outdoor caf  . The buyer's team must make sure that each of such licenses or permits are current, in good standing, and transferable at closing. If any particular license or permit is not transferable, a new one must be issued, and the risk of problems arising from any required re-inspection by public authority must be evaluated.

When the closing bursts from the gates, don't be the straggler who is cut down in the first pass, but rather be Maximus. Shout "as One!" Line up the teams, "single column...single column," and close.

Ken MacKenzie is partner of Dalton & Finegold, LLP and a member of the International Hospitality Consultants (ISHC). Formerly MacKenzie was the co-leader of the Hospitality and Recreation Group at Goulston & Storrs. MacKenzie represents institutional investors, private equity funds, investment managers, pension funds, university endowments, REITs, major lending institutions and developers in the acquisition, financing and disposition of all classes of real estate assets both nationally and internationally. MacKenzie specializes in transactions involving hospitality assets and has significant

experience in large-scale joint-ventured deals, often involving non-profit institutions such as universities or hospitals. He frequently assists clients in structuring their responses to RFPs for complex mixed-use projects.

MacKenzie received his A.B. from Dartmouth College and his J.D. from Boston University School of Law, where he graduated magna cum laude. MacKenzie is admitted to practice law in the state of Massachusetts.

New England Real Estate Journal - 17 Accord Park Drive #207, Norwell MA 02061 - (781) 878-4540