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Roundtable participants discuss management, real-estate

By Jeff Higley
EDITOR-IN-CHIEF

PHOENIX—The lodging industry is in for more checks and balances with management contracts as it sorts through the recent rash of lawsuits filed claiming management companies aren't doing their jobs correctly, according to several members of a roundtable involving members of the Lodging Industry Investment Council. LIIC members also discussed the place of hotels in the real-estate world.

The roundtable, held in conjunction with The Lodging Conference in Phoenix in early October, revealed that several industry executives think there is a fundamental shift in the way management contracts are handled.

"Around our office, transparency is a big buzz word," said Todd Siegel, director, Hyatt Development Corp. "I can tell in the last few agreements that I've done, the attorneys keep giving me more stuff to put in the documents, which is giving more transparency, more detail, not necessarily people asking for it, but we're making sure it's all out on the table, answering questions before they get asked."

Larry Shupnick, senior v.p. of development and acquisitions for MeriStar Hospitality, said his company also is ahead of the curve.

"A year or more ago, we put together a 10- or 11-page disclosure letter related to charges and sent it to our clients," Shupnick said. "Every new management contract proposal we send out now, we send this letter along with the management proposal; and if we have operating statements, we tell them if they want to participate in some of the areas, for like [information technology] services or some of the other items we charge extra for, based on your volume, this is what it would cost you on an annual basis. You have to disclose everything up front to the client if you want to be in the management business."

Charlie Muller, v.p. of operations for CNL Hospitality, said conditions in management contracts go beyond being affected only by lawsuits.

"You've already seen that shift," Muller said. "I don't think it was driven by the lawsuits that have taken place. I think it's driven by a more savvy set of investors in the marketplace that understand the business better and have worked with operating companies to try to draft better agreement language for the owners. A lot of the agreements that are in play in the lawsuits are older agreements. I don't think it's the effects of how the business has changed during the last several years. Clearly, we'll continue to get that, but I think the shift started before the lawsuits."

Muller

Cahill

Finding its place

The participants also agreed hotel real estate is among the most difficult real estate to gauge.

"Hotels in their purest form are real-estate — it's an operations-intensive form of real-estate," Muller said. "That's why you see a separation, generally, between companies that like to manage real-estate and companies that like to own real-estate. We love everything about real-estate ownership. We love the long-term, balanced value of real estate."

"Hotels are bought and sold as an operating business that tends to have a large real-estate component to it," said Mike Cahill, president of Hospitality Real Estate Counselors. "The question I have, and no one ever has a good answer, is when someone buys or sells turnaround properties, how much of that value is real-estate and how much is the business? My general conclusion is that most of the smart people in this industry are making money on the business side [and the real-estate side]."

That's where the argument of whether hotels are real-estate or simply business propositions stops, according to Muller.

"Even office buildings trade in value based on income generation from the property," he said. "They're not really appreciating in just real-estate value, they're appreciating in income producing value."

"That's the misnomer," said C.A. Anderson, managing director, hotel group for Cornerstone Real Estate Advisors. "They all have business-value components. It comes back to people saying office buildings have no business value, but they do. There are office buildings that have good will, they run a little more profitable. There are shopping centers that run better because there's good will. Except for just pure dirt, or a vacant building, there is a business-value component in almost all forms of real-estate."

Anderson

Shupnick said that when one gets right down to it, hotels are much like shopping centers when it comes to determining their places in the real-estate world.

"You have to go out and find a

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LIIC's mission

The Lodging Industry Investment Council is an industry think tank that meets three times annually to discuss hotel finance, development and operations issues. Its 70 members include consultants, lenders, operators, developers, educators and legal professionals.

LIIC
LODGING INDUSTRY INVESTMENT COUNCIL

Co-chairmen for LIIC are Mike Cahill of Denver-based Hospitality Real Estate Counselors and Sean Hennessey of PricewaterhouseCoopers' New York office. Vice chairman is Jim Butler of Jeffer, Mangels, Butler & Marmaro, a Los Angeles-based law firm.

Roundtable participants

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client to rent the retail space, then it's the marketing and the management company and the retailers that bring the customers in, the same way a management company brings customers into a hotel," he said. "The real-estate only has value if they're getting their return per square foot in that shopping center. They might not depend on airline lift and some of the other things we depend upon in the business, but if the economy is down and people don't have money to go shopping for extra clothes and other things, the traffic goes down the same way the occupancy goes down in our hotel."

Rob Koger, president of Molinaro Koger, said the hotel's position has much to do with its place in the real-estate scheme of things.

"One way to look at it is you look at the Marriott hotel at the Phoenix airport; that's a piece of real-estate and that's an operating business," Koger said. "If you take the Marriott name down and put up the Cahill Hotel, that real estate and our business — no offense, Mike—has a lot less value. There's a business component.

"I had this discussion with an owner who was going through a tax appeal, who argued the tax assessment for the building should be considerably less because there was so much value in the business, which technically isn't taxable from a real-estate value basis. If you look at a building with an independent name that might not have cache compared with a strong brand, there's much different value even though the building is the same."

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>
> — CHARLIE MULLER