Condo hotels: Don’t forget the secret sauce!

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Condo hotels are back in vogue as “securities”

Developers particularly like the “new model” where condo hotel investments are offered as a “securities” using the new SEC Rule 506(c) for private placements with public solicitation.

Unfortunately, in their enthusiasm for this new model— which is well deserved — many developers will create dysfunctional structures that will be difficult or impossible to correct once they are put in place. These issues can all be avoided with an experienced team of experts who know and understand condo hotels.

What is right about this “new model”?

Condo hotels make sense in many situations. (See Condominium Hotels are hot! What is a Condo Hotel?) They can be a great financing device for developers, particularly at the luxury and high-end spectrum of hotel development. The “new model” of selling condo hotels as securities will clearly be the way to go in most situations. SEC Rule 506(c) is the key to this approach. (See: The “new breed” of condominium hotels — Key to financing new hotel development? Selling condo hotels as “securities” under new SEC Rule 506(c) . . .)

So what’s the problem?

With the right team of experienced experts, there is no problem. But some people don’t recognize the legal and business complexity of a condo hotel. Every mixed-use project introduces new dimensions of issues for development, design and operation. And a condo hotel adds an entirely new dimension of issues related to hotel operations, condo hotel operations, integration of the project components, design of the rental program and terms of participation by condo owners in that program. Who owns what? Who pays for what? Who gets to use what? How are these terms implemented in CC&Rs, HOA articles and bylaws, rental agreements, maintenance agreements, and the like?

Examples of some unique condo hotel issues

There is a dizzying array of options to choose from in developing your condo hotel format. Assuming you have selected the Rule 506(c) approach of offering the condo hotel units as securities, how many regime structures will you have in the project? Just regular hotel rooms and condo hotel units? Or will you have some branded condo hotel units, some
unbranded, some units serviced by the hotel and others not serviced. Will you add any for-sale whole ownership condos (not part of the condo hotel structure) or fractionals, or club units?

For your condo hotel units, will you make participation in the hotel rental program mandatory? Will you give owners the income from their individual units or a predefined share of the income pool from all condo hotel units? Will you use “splits” or some other allocation method for expenses to be paid by unit owners? What restrictions, if any, will you impose on owner use (e.g. not more than 30 days occupancy at a time nor more than 90 days per year)? Will there be blackout periods when an owner cannot use a unit? Will the owner get to use his unit, or just a comparable unit? What preferential booking rights will an owner have (when can the owner book a room)? What rights do condo unit owners have with respect to the hotel operator?

The issues go on.

**You only get one chance to get it right!**

In many business arrangements, if you make a mistake, you can just change things and make them right. That is very difficult in a condo hotel regime structure, because each part of the regime has a ripple impact on all the other parts of the structure. And many elements of the structure tend to get “locked down” like the provisions that go in the CC&Rs. Once a single condo hotel unit has been sold, it is extremely difficult or impossible to “fix” any problems or oversights. This really puts a premium on getting it right the first time.

**Other condo hotel resources**

You can access the full library of Condo Hotel materials on Hotel Law Blog by going to the home page, selecting the tab at the top that says “HOTEL LAW TOPICS”, and then clicking on “Condo Hotels” in the drop down menu . . . or by clicking here.

Below is a partial listing of articles by JMBM’s Condo Hotel Lawyers:

- Condo hotels: Don’t forget the secret sauce!
- Condo Hotel Lawyer: What is a Condo Hotel?
- The “new breed” of condo hotels — Key to financing new hotel development? Selling condo hotels as “securities” under new SEC Rule 506(c) . . .
- Using condo hotels for financing new hotel development: Traditional condo hotel structures as “non-securities”
- Condo Hotel fundamentals — 5 Keys to Success!
- Condo Hotels’ enduring legacy: hotel-enhanced mixed-use
- Hospitality Lawyer: The 5 biggest misconceptions about Condo Hotels
- Condo Hotel Lawyer: Why does the SEC care about condo hotels?
- Condo Hotel Lawyer: Standards must be “built in”
- Condo Hotel Lawyer: Not so fast! Locking down the condo hotel structure
- Condo Hotel Lawyer — What is fanning the condo hotel wild fire in Latin America, the Caribbean, Europe, China, India and the Middle East?
- Condo Hotel Lawyer — Las Vegas Report: What drives successful sellouts today?
- Condo Hotel Lawyer — What in the world is going on with condo hotels now?
- Hospitality Lawyer — Trump’s luxury residential mixed-use project in Hawaii sells out in 8 hours. New sales record claimed.

This is Jim Butler, author of www.HotelLawBlog.com and hotel lawyer, signing off. We’ve done more than $87 billion of hotel transactions and have developed innovative solutions to unlock value from hotels. Who’s your hotel lawyer?

Our Perspective. We represent hotel owners, developers and investors. We have helped our clients find business and legal solutions for more than $87 billion of hotel transactions, involving more than 3,900 properties all over the world, including more than 100 condo hotels and hotel condos. For more information, please contact Jim Butler at jbutler@jmbm.com or +1 (310) 201-3526.

Jim Butler is a founding partner of JMBM, and Chairman of its Global Hospitality Group® and Chinese Investment Group™. Jim is one of the top hospitality attorneys in the world. GOOGLE “hotel lawyer” and you will see why. Jim and his team are more than “just” great hotel lawyers. They are also hospitality consultants and business advisors. They are deal makers. They can help find the right operator or capital provider. They know who to call and how to reach them.