A KEY TO MANAGING YOUR HOTEL THROUGH TROUBLED TIMES: KEEPING YOUR LENDER HAPPY

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Maintaining Control of a Distressed Hotel Can Be a Challenge. To Meet It, Focus on Your Contingency Plan and Have the Right Team in Place

You bought your hotel with the highest expectations. And why not? All owners do.

Certainly you had good reasons for buying. The property is in a good location. It has a strong market position. It needs renovation, but the renovations can be completed on time and on budget. The local business community is strong and ready to support you. The economy is stable and beginning to expand after several challenging years.

The best-laid plans of hotel owners can go astray

What could go wrong?

As it happens, many things. A competitor opens across the street. A competitor upgrades the property beyond the level your budget can match. You contractor fails to complete the renovation project on schedule or at anything close to the estimated cost. The anchor tenant in the adjoining business park moves out. The economy drifts back into recession. And suddenly the property is in default of loan covenants or is in danger of missing payments.

What do you do? Assuming that you don't want to sell – often an option, but not necessarily the most appealing one – then you need to find a way to remain in control of the property. To do that, you need to establish or enhance a working relationship with the lender. This isn't necessarily an easy process. But there are approaches that can help turn potential confrontation into collaboration and increase the odds that the hotel remains your hotel at the end of the day.

Selling the property is an option, but it probably isn't your preferred choice

Selling a distressed property can sometimes be advantageous. In a previous article (http://www.markspaneth.com/publications/when-you-acquire-a-distressed-hotel-look-out-for-major-unseen-challenges), I explored distressed debt acquisitions from the perspective of the acquirer. Obviously the acquirer stands to benefit in such a scenario. A distressed debt acquisition can benefit the current owner as well, by providing an exit path and an opportunity for you to set your finances on an even keel.

But perhaps you're not ready to sell. And perhaps you shouldn't. Selling a distressed property may involve selling at a loss or at a level that you may not be ready, able or willing to absorb. Perhaps, also, you were right about the property in the first place. In spite of all your current hardships, the fundamentals may be sound. The hotel may yet realize the value you first envisioned. Maybe it's you – and not an acquirer – that's best qualified to turn the property around.

Under those circumstances, your challenge is this: Hold onto the property until you can realize your turnaround plan. Work with your lenders so that, at the end of the day, you remain in control.

To hold onto the property, having a contingency plan is essential

How do you do that?

The key task is to create a proactive, well thought-out action plan, one that covers the steps you'll take to respond to a sharp economic downturn, an unexpected event or a competitive blow. Ideally, worst cases should always be part of your planning process. But even if you don't have a contingency plan in place, you can develop and implement one at the first sign of trouble – provided you move quickly.

When I was CEO of The Griffin Group, Merv Griffin and I had to face the impact of the post-9/11 environment on our hotels. The combination of the terrorist threat and a plummeting economy brought leisure travel almost to a standstill. We responded by cutting back our operations and deferring some of our plans. We closed wings at the Beverly Hilton and postponed a major renovation that had been scheduled for the Hilton Scottsdale.

You will need to be ready to make similar moves to reduce the scope of your operations so that they conform to a different economic reality. Discuss contingencies, develop plans and be ready to act to close wings, reduce staff, renegotiate vendor contracts and defer capital projects.

The primary objective of the plan, of course, is to enable you to survive and minimize economic damage during a period of hardship. But there's an added advantage. Having a plan in place gives you a story to tell the lender to show that you are on top of things – ready and able to manage through difficulties.

Be ready to work with your lender

Working with the lender is your central challenge. To meet the challenge, you need first of all to determine what you want from the lender. Are you at the earliest stage of your difficulties? Is it just that you're warning them about impending problems? Or do you need something more concrete?

If the latter, what exactly do you need? A covenant waiver? Deferred payments? Perhaps a modification where you pay interest and defer principal? Do you need a total renegotiation? Or are things so bad that you are looking for a standstill agreement?

Whatever the situation, you need to make sure you're honest with the lender and that you're providing all the relevant information. There is nothing worse than preparing an update about a troubled situation and then have it appear that you are hiding information – or that you do not have a full grasp of the situation. Providing full information means explaining clearly what is happening, what you are doing to proactively minimize the damage and what you want the lender to do or provide.

In other words, go into your meeting or discussion with your complete action plan in hand. Be clear about what you need – don't make the lender guess.

Even the most hostile-seeming lender might actually be on your side

Now, it's possible that even with the most thorough preparation, your discussions with the lender won't go well. In that case, there are other, "harder" tactics you can apply. Withholding loan payments is always a reliable way to get the lender's attention but can often backfire. Hiring bankruptcy counsel is something else you may want to consider. However, these tactics are part of a different scenario, one that goes beyond the scope of this article and is better covered elsewhere.

The good news is that, in most situations, if you are well prepared and present a carefully considered, reasonable plan, the lender will be willing to work with you. This can play out in surprising ways. In one instance, when I was CEO of The Griffin Group, Merv and I found ourselves in default of the covenant. The lender was aggressive about dunning us, and on the other hand didn't seem interested in hearing about alternatives. In the midst of this, I invited the lender to a function on the property where Merv was appearing. I was worried about it because she seemed to be so threatening. But almost as soon as she showed up, she got stars in her eyes. She pulled me aside and said, "Get me my picture with Merv and I'll get you that waiver." I literally pulled him out of a limo to get her the picture. And the covenant came through.

Credibility is job one. Being credible means having the right team in place

What's the lesson here? In a phrase, be credible with your lender. Clearly, in this case, the lender didn't give us the modified covenant because she got a picture with Merv. A waiver or modification isn't something you pull out of your briefcase all of a sudden – it takes work to develop and prepare one. Our lender didn't go back to her committee and say, "I've got Merv's picture, let's give them the waiver." She'd already made her decision and the new covenant was ready to go. What really turned her around was that we were direct, honest, thorough and timely in getting her all the information she needed.

The bottom line is, be prepared. Think about the situation from the lender's perspective – what would you want to see and know about if you were financing the property? To help make sure you get on the lender's wavelength, it's best to surround yourself with a team of professionals who can give you insight into the lender's thinking and credibility at the negotiating table. Your team should consist of marketing professionals, engineers and/or architects (if the turnaround plan involves facilities work), workout attorneys and of course financial consultants with industry-specific turnaround experience.

While there is no guarantee that any of this preparation and team formation will work with the lender, more often than not, it will. At minimum, you will have gained some ground in keeping the lender happy – and you can focus on what's most important: your property.

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About Lawrence Cohen

Lawrence Cohen is the Hospitality Group Leader at Marks Paneth & Shron LLP. He rejoined the firm after having served for many years as the President and Chief Executive Officer of The Griffin Group, the investment and management company of the late Merv Griffin.

Mr. Cohen has strong roots in the hospitality industry. The Griffin Group and its affiliates owned and managed properties that ranged from high-end resorts to limited service properties. Mr. Cohen spearheaded all aspects of the business including acquisition, development and redevelopment, financing, management team hiring, supervision of operations and eventual sale.

In addition, Mr. Cohen has had business interests in the Los Angeles area for more than 25 years and shares responsibility for the firm's operations on the West Coast.

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