ALERTS

COVID-19's Impact On Hotel, Motel And Other Hospitality Loans

March 30, 2020

With the recent travel restrictions implemented due to COVID-19, the hospitality industry has been significantly affected. This is likely to result in numerous defaults on loans secured by hospitality properties, such as hotels and motels, in the near future.

Circumstances may vary on a case-by-case basis, but these are the key considerations for lenders and special servicers dealing with troubled hospitality industry loans that are unique to these properties:

- **Franchise Agreement** – Most all hotels or motels operating under a national brand have a corresponding franchise agreement that licenses the use of its brand to the owner of the hotel. Lenders and special servicers should consider reviewing these agreements to understand their potential rights with continued usage of such branding, especially upon the filing of a foreclosure action. Often times, the franchise agreement may automatically terminate upon the filing of a foreclosure complaint. Understanding the terms of these particular agreements may affect a lender's strategy related to remedies following a default.

- **Comfort Letter** – In connection with the franchise agreement, at loan origination the franchisor, borrower and lender often enter into a comfort letter, whereby the franchisor may agree to allow a foreclosing lender to continue using the franchisor's intellectual property. However, there are likely time limitations associated with this that do not allow a foreclosing lender to indefinitely continue using such intellectual property. Lenders should carefully

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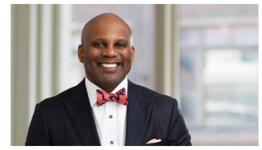

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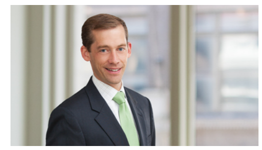

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review these letters and ensure they are compliance with the same.

- **Property Improvement Plan** – Many hospitality franchisors allow borrowers to use their branding in exchange for a commitment that the borrower must update its facilities and branding upon the reasonable request of the franchisor. These improvements often come from the franchisor through a "Property Improvement Plan" (PIP). At loan origination, lenders often include a reserve for the PIP. When a hospitality loan is in default, lenders and special servicers should assess the currently applicable PIP and determine whether the borrower has complied with the same.

- **Management Agreement** – Hospitality borrowers often execute a management agreement with a third party to actually manage the hotel or motel property. Related to this, lenders may have executed a subordination and non-disturbance agreement (SNDA) at loan origination to ensure that the rights of any such manager would be subordinate to the rights of the lender if a default occurs. Reviewing and understanding the management of a hospitality property, and any corresponding SNDA, is critical to understanding who employs the staff, who is in charge of operations, and where changes may occur to address operational deficiencies.

- **Licensing** – Although a hotel itself may have state or local licensing requirements, any additional food and bar services may have further licensing requirements. When a foreclosure is possible, consideration should be given to how such licenses may be transferred and what steps need to be taken through state or local agencies for the transfer of such licenses.

To obtain more information, please contact the Barnes & Thornburg attorney with whom you work, or Alan Mills at 317-231-7239 or alan.mills@btlaw.com or Jonathan Sundheimer at 317- 231-7319 or jonathan.sundheimer@btlaw.com.