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2011 FIRST QUARTER UPDATE **CURRENT HOSPITALITY LEGAL DEVELOPMENTS**

The challenging economic climate and recent changes in the law, have necessitated the formulation of innovative strategies to be in position to make a substantial difference for our clients. The purpose of this Update is to report on certain recent matters that may be relevant and useful.

The following legal areas are highlighted:

- **PERSONAL GUARANTIES CAN BE USED AS LEVERAGE IN LOAN MODIFICATION NEGOTIATIONS**
- **RECENT CHANGES TO THE AMERICANS WITH DISABILITIES ACT**
- **FRANCHISE AGREEMENTS – CURRENT DEVELOPMENTS**
- **INDEMNIFICATION OF FRANCHISORS**
- **POLICE ENTRIES AND SEARCHES OF GUESTROOMS**
- **PRIVACY ISSUES AND AUDIO RECORDINGS**
- **INSIDE SALESPERSONS**

PERSONAL GUARANTIES CAN BE USED AS LEVERAGE IN LOAN MODIFICATION NEGOTIATIONS

Many hotel loans are in default and borrowers have executed substantial personal guaranties. Guarantors naturally dread the idea of filing for a Chapter 11 reorganization under the bankruptcy code. Although advisable in certain situations, using the knowledge of the potential outcome of a reorganization and its implications for a lender (without actually filing) can frame the loan modification negotiation in such a way that can bolster the borrower/guarantor negotiating position. Loan amounts that exceed the current fair value of the loan may become unsecured obligations. A guarantee is usually an unsecured obligation. Unsecured obligations in a reorganization may have minimal value. Using these potential consequences in the negotiation to one's advantage may result in a compromise that may avoid the filing. Each situation varies and knowledgeable counsel should be consulted to help formulate these strategies and navigate these complex issues.

RECENT CHANGES TO THE AMERICANS WITH DISABILITIES ACT PRESENT OPPORTUNITIES FOR HOTEL OWNERS AND HOTEL CONTRACTORS

In July 2010, significant changes to the Americans with Disabilities Act (ADA) were announced, set to take effect on March 15, 2011. Compliance with the 2010 standards is permitted as of September 15, 2010, but not required until March 15, 2012.

The new design and construction requirements will greatly impact hotels. Because of the delay in enforcement, any new development or remodeling completed prior to March 15, 2012 using the current ADA standards, will be grandfathered as ADA compliant. Thus, for any developments or renovations that will be completed by March 15, 2012, companies can choose whether to comply with the current or new ADA requirements, allowing them to select the standards most advantageous to the companies. However, for construction that will not be completed by March 15, 2012, it is imperative that companies become aware of, and ensure compliance with, the 2010 standards.

FRANCHISE AGREEMENTS – CURRENT DEVELOPMENTS

Clauses attempting to curtail franchisee's rights continue to find their way into franchise agreements.

The Implied Covenant of Good Faith and Fair Dealing Faces Multiple Challenges

In many states, the implied covenant of good faith and fair dealing continues to be franchisees' primary means of asserting their rights. However, franchisors continue to try and minimize its effectiveness. Although many courts have held that waiving the covenant is against public policy, other courts have upheld waivers when the court finds that the parties intended to waive the covenant. Unfortunately, certain of these jurisdictions are the ones stated as the governing law in the agreement.

Alternatively, some franchisors have attempted to circumvent the implied covenant by including a provision that any discretion exercised by the franchisor pursuant to the contract will be implemented in the best interest of the "System". As such franchisees may have no expectation that the franchisor will ever act with the franchisees' interests in mind. The franchisees' reasonable expectations when signing the contract are therefore substantially, if not entirely curtailed. Although we are unaware of the courts ruling on the enforceability of this provision, we think that it presents a hurdle that franchisees will need to overcome in asserting their rights.

Arbitration Clauses Circumvent State Statutory Protections

Numerous state statutes require that any litigation regarding a franchisee must be held in that state. Consequently, some franchisors have inserted in franchise agreements, mandatory arbitration provisions wherein the venue is the franchisor's home state. Since arbitration is not technically a court action, the statutory venue schemes are not applicable. Even when courts have rejected these venue provisions, certain franchise agreements state that any arbitration will be conducted pursuant to the Federal Arbitration Act. Courts have upheld these provisions, finding that the federal law preempts state law. The result is that franchisees may have the burden of arbitrating disputes in locations far from home, often in the franchisor's backyard.

Franchisees have challenged these arbitral forum selection clauses as unconscionable when its application would prevent the application of a state law protective of franchisee's rights, but these challenges are analyzed on a case by case basis, and the success of these challenges have differed among the different jurisdictions.

Although this and many other issues may not be negotiable, franchisees need to understand the risks and know that not all franchisors are as aggressive. Such issues should be considered in selecting a franchisor with whom the franchisee will have a long term relationship.

INDEMNIFICATION OF FRANCHISORS

Most franchise agreements require the franchisee to indemnify, or hold harmless, the franchisor for acts, errors, omissions, or negligence by the franchisee. An indemnification agreement means the franchisee agrees to take financial responsibility if a third-party brings a legal action against the franchisee and franchisor, which can also include financial responsibility for the franchisor's attorney's fees and costs.

Franchisees should be sure to name franchisors as an additional insured in its general liability insurance policy, and include a special endorsement naming the franchisor as an additional insured. This endorsement is needed to allow both the franchisee and franchisor to tender any defense of a lawsuit to the insurer, thereby avoiding the costs and fees of a litigation, subject only to the deductible. Failing to obtain the special endorsement may require the franchisee to pay out of pocket, a franchisor's costs of defense, which can be substantial even if summarily dismissed. Franchisees should contact their insurance broker to ensure they have the special endorsement.

POLICE ENTRIES AND SEARCHES OF GUESTROOMS

Police requests to search guestrooms can place hotel owners in a difficult situation. Hotel owners must balance the interests of preventing crimes on their property, versus potential civil liability for unlawful entries or searches of guestrooms. As a general rule, hotel owners and employees should not consent to police entry or searches of guestrooms without a warrant.

A guest has a reasonable expectation of privacy in his/her room. Police must have either a warrant unless (1) the guest or someone with authority consents to the entry, (2) the guest has vacated the guestroom; or (3) exigent circumstances justify the entry. Exigent circumstances justifying entry include preventing impending physical harm to officers or others, the destruction of evidence, the escape of the suspect, or some other event improperly frustrating legitimate law enforcement efforts.

Determining the propriety of an entry or search is always a fact specific analysis of each incident. When possible, hotel owners and employees should always require a warrant before any police entry or search. It is also recommended that hotel owners and employees become apprised of situations where a warrantless entry is typically allowed. This will enable hotel owners and employees to cooperate with law enforcement officials while decreasing the hotel's potential liability for invasion of privacy claims, which can include damages for mental suffering and emotional distress, medical and psychiatric expenses, loss of earnings, and injury to reputation.

AUDIO RECORDINGS

There are numerous Federal and State laws governing audio recordings. These laws prohibit making audio recordings of confidential communications without consent. Some states require only one party's consent to the audio recording, while others require the consent of all parties to the confidential communication. A communication is confidential if any party to the conversation expects that it will be confined to the parties, but if the parties understand that it may be communicated to a third party, the communication is not confidential.

It is recommended, as a general policy, that hotel owners refrain from audio recordings unless consent is obtained from all parties before any recordings are made. Violating Federal and/or State wiretap laws can expose hotel owners to criminal prosecution and civil liability for the damages suffered by the recorded party.

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INSIDE SALESPERSONS

Mischaracterizing an inside salesperson as an outside salesperson can be costly. Inside salespersons are subject to Federal and State overtime and minimum wage laws. However, outside salespersons are exempt from the overtime and minimum wage laws. According to Federal law, an outside salesperson is one whose primary duty is making sales or obtaining orders or contracts for services or for the use of the facilities for which consideration will be paid by the client or consumer, and the employee must be customarily and regularly employed away from the employer's place of business. Some State laws have different requirements for outside salespersons to qualify for the wage exemptions, so hotel owners should confirm compliance with their State's laws.

Hotel owners employing individuals thought to be outside salespersons should examine the duties performed by the salesperson, and the amount of time spent performing the duties away from the hotel. A misclassification can subject the hotel to substantial amounts of back overtime pay.

ABOUT MILLER LAW GROUP, P.C., AND CONTACT INFORMATION

The Miller Law Group, P.C., is a full-service hospitality law firm representing hotel owners and management companies throughout the United States. Allied Memberships: AHLA, CHLA, CLIA, AAHOA, NABHOOD, ICSC and AAFD.

HOSPITALITY ASSIGNMENTS

- ◆ Purchase/Sale Transactions and Debt/ Equity Financings
- ◆ Loan Workouts and Chapter 11 Reorganizations
- ◆ Joint Ventures
- ◆ Entity Formation and Asset Protection
- ◆ Liquor Licensing
- ◆ IP, Technology And Internet Issues
- ◆ Franchise Agreements - Negotiation and Dispute Resolution
- ◆ Management Agreements
- ◆ Development And Construction Agreements
- ◆ ADA Issues
- ◆ Restaurant/Banquet Leases
- ◆ Wage And Compensation Matters

For questions, comments, or further information contact Mitch Miller, at mmiller@MillerLG.com or 650-566-2290.

The foregoing information is in no way intended as an exhaustive description of all of the pertinent laws and regulations but merely highlights some of the important rules applicable to certain highlighted issues. The recipient is advised to engage counsel when considering the impact of any of these rules to a specific situation. The State Bar Rules of Professional Conduct require that we inform you that this Update constitutes attorney advertising.