HOTEL FINANCIAL
STRATEGIES

FINANCIAL ARCHITECTS TO THE HOTEL INDUSTRY

Critical Issues to Ask Before Entering a Joint Venture or Partnership

Joint Ventures and Partnerships can be complex, lucrative, and/or difficult and expensive. As is so often the case, thorough planning and attention to detail before entering into an agreement JV will result in a more streamlined and likely positive transaction. Begin with an experienced attorney to guide you through the process. There are a lot more issues than this list contains, however, it may be helpful.

1. Will the investor cover all costs, or is their investment preferred equity to your contribution?
   a. Who is responsible for construction and occupancy cost overruns?

2. Is there a preferred or guaranteed return to the investor?

3. What are the sharing arrangements for
   a. cash flow
   b. construction savings
   c. tax losses
   d. sale proceeds

4. When are funds to be contributed?
   a. land acquisition
   b. start of construction
   c. funding of the permanent loan

5. Who is in control of the investment?
   a. construction decisions
   b. marketing decisions
   c. capital expenditures
   d. management
   e. sale and refinance

6. Do you have a capital account?

7. Is there an earn- out formula?
   a. time allocation
   b. based on an IRR
   c. what if project has not stabilized at time of earn-out?

8. Does the investor guarantee the construction loan?

9. Will the investor cover the equity gap?

10. Are there guarantees with regard to future funding obligations?

11. Can the transaction be unwound?
    a. failure to get financing

12. What are the forms of additional obligations?
    a. loan from investor
    b. if there is an additional contribution how does it change percentage allocation?

13. Does the investor get a capital account for hard equity investment?
    a. what if developer covers overruns ?

14. Is there a buy-sell provision?
    a. adequate notice to developer to get new financing

15. What experience in joint ventures does the investor have?

16. What is the developer's IRR

17. Is there a 100% squeeze- out formula?
    a. can developer preserve minimum interest?
    b. is there a fair dilution formula?

18. Is the investor prepared to take on construction phases with a predetermine formula?

19. What is the blended interest rate on joint venture capital?
    a. what is the true cost of money?

20. Will the early joint venture conflict with the developer's future ability to optimize their position?

21. Does the accrued return increase the investor's position?
    a. does accrued return bear interest?
    b. is the accrued return paid when cash is available, or out of sale proceeds?

22. Is the asset-holding period compatible with the developer's?
    a can the developer sell his interest before sale of the property?

23. What is the formula governing release of cash set aside to cover FF&E, improvements, marketing, construction completion, or negative cash flow?
    a. use of L.C. or cash?

24. Is there a mechanism governing the modification of the sharing of cash flow or sale proceeds after investor receives prescribed return?
    a. 75/25 modified to 50/50, etc.

25. Will the joint venture trigger?
    a. taxable event
    b. capital gain
    c. payment of soft dollars by investor
    d. short term gain

26. Will investor assume existing partnership?

27. Will investor assume existing project liabilities?

28. Will investor recognize a land profit or developer fee?
    a. cash payment or capital account

29. Will investor pay for 100% of tax losses?
    a. will investor allocate tax losses for lower price, or higher yield?

30. Will investor give 100% of cash flow for two years in exchange for 100% of the tax losses?

31. Who controls partnership funds?
    a. construction loan
    b. permanent loan

32. Does investor have continuing ability to cover deficits after breakeven?
    a. what if major decline occurs in future years?
    b. is there a contingency reserve set aside by investor?

33. If the investor controls the transaction, is the developer a general, or limited partner relative to future partnership liabilities?

34. Does the developer guarantee breakeven?
    a. what if projections are not met?

35. What is the scope of reporting to the investor?

36. What is the right of the developer to build and manage a competitive project?

37. Is a monthly reserve account required?

38. What are the investor's IRR, immediate cash return, and tax loss objectives?

39. When do investor's funds go at risk?

40. Will investor funds help lower construction interest?

41. Does the investor require an appraisal before funding?

42. Will the developer subordinate the management fee in order to qualify for a permanent loan?

43. If a permanent loan is obtained what if the ceiling is not obtained?

44. Is the investor contact person experienced?
    a. years with investor
    b. articulate spokesman
    c. independent authority

45. What representations and warranties are required?

46. Will the investor perform like a partner, or lender?

47. Does a committee govern the investor?
    a. decision-making process
    b. local authority

48. Will the investor want to control property management?
    a. risk of capital calls

49. Does the developer earn a cumulative, or non-cumulative return?

50. Is another financing vehicle available?
    a. participating mortgage
    b. mezzanine loan

51. Do the parties understand the difference between simple interest and an IRR?

Hotel Financial Strategies specializes in these types of transactions. They have been successful in seeking equity from as low as $2 million to as high as $50 million per individual transaction. They understand investor needs and have a great deal of experience in this segment of the marketplace. Please give us a call to answer any questions you may have.

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