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Hospitalitas

The Hospitality Industry Newsletter from Baker Donelson

FTC Announces New Thresholds for Pre-Merger Filing

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Under the Hart-Scott-Rodino Act, mergers and acquisitions above a certain size must be reported to the Federal Trade Commission and the Antitrust Division of the Department of Justice before the merger or acquisition is consummated. Those agencies then have thirty days to decide whether to seek additional information about the competitive effects of the deal, which could lead to a subsequent action to block it.

Each year the FTC calculates new thresholds based on inflation, and the agency has announced that the new threshold for pre-merger notification will be $63.1 million.

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Post-Trial Briefs: Reviving a Trade Name Damaged in Litigation

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Have you ordered a bowl of chili from Wendy's since the infamous finger in the chili incident in March 2005? Have you ordered a taco from Taco Bell since the fall of 2006? Have you ordered a spinach salad lately? Consumer reaction to incidents of food borne illness costs the hospitality industry millions of dollars each year.

Food borne illnesses are a serious concern for all businesses involved in the hospitality industry, both directly and indirectly. Directly affected customers (or their estates)

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Negotiating Lease Terms with the Bottom Line in Mind

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With the commercial real estate market softening and vacancy rates climbing, lenders are taking a more conservative approach in deciding which real estate development projects to finance. Coupled with tight credit markets and tougher underwriting standards, lenders are demanding more financial covenants and pre-leasing requirements from the developer/borrower as a condition to financing. As a result, the leverage in lease negotiations between the developer/landlord and the tenant is shifting.

During the real estate boom of the past few years, lenders were lenient in their credit decisions. The name of the game for the lenders was "book the loan and get

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Welcome to *Hospitalitas*

Welcome to our inaugural issue of *Hospitalitas*, the Baker Donelson newsletter for our clients and friends in the hospitality industry – hotels, restaurants and their suppliers. We plan to publish several times a year when we believe we can deliver first class, useful information for your business. Please send us your feedback and ideas for topics you would like to know more about. True to our Southern heritage of hospitality, we'll work hard to make each visit with us something special, and worth repeat-

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FTC Announces New Thresholds for Pre-Merger Filing, *continued*

Deals valued at less than $63.1 million are not subject to the pre-merger notification requirements of the Act; deals valued above that amount usually are.

Certain types of transactions are exempt from pre-merger notification, including acquisitions of real estate and hotels. Acquisitions of hotel chains, however, including acquisitions of trademarks, reservations systems, etc., are not exempt, although the value of real estate being purchased may be deducted from the value of the deal for purposes of determining whether the pre-merger notification threshold has been met. The new threshold went into effect in March. For more information, please contact John Calender or Phillip Zane in Washington.

Mr. Zane is an attorney in our Washington, D.C. office.

Negotiating Lease Terms with the Bottom Line in Mind, *continued*

the fees." But lately lenders are being more diligent and are no longer willing to make loans for speculative real estate developments. As a result, developers are making more concessions in the negotiation of leases for their proposed developments to increase their pre-leasing and meet one of the lender's conditions to financing.

Many developers continue to favor mixed-use developments, which contain a combination of retail and office space, with many also including a hotel. Restaurants are an integral part of the tenant mix for these developments and are positioned to demand more favorable lease terms. Below we offer six ideas on lease terms that have the potential of either increasing the restaurant tenant's prominence in the marketplace or increasing the restaurant tenant's profitability and return on investment.

1. Exclusivity – Developers/landlords have been reluctant to include an exclusivity provision that restricts the developer's/landlord's leasing options in the future. This covenant, by definition, will preclude the developer/landlord from leasing space to a competitor of the restaurant tenant within the proposed development or within a certain radius of the proposed development. Developers are now more willing to include such a provision in a lease if necessary to get the restaurant tenant's signature. This provision must be carefully drafted in order for the restaurant tenant to realize the maximum benefit, particularly if the landlord wants to tailor the clause to a restaurant niche like casual dining.

2. Opening Co-Tenancy – Leases typically disclaim developer/landlord representations to the proposed tenant and state that the proposed tenant is not relying on any representation from the developer/landlord, other than those specifically provided in the lease. The Opening Co-Tenancy provision allows a restaurant tenant to pay the developer/landlord reduced rent (sometimes significantly reduced depending on the circumstances) if certain other tenants, which the developer/landlord has told the restaurant tenant will open in the development, have not opened when the restaurant tenant opens for business. Inclusion of the Opening Co-Tenancy provision can financially benefit the restaurant tenant if all of the pieces of the developer's/landlord's puzzle don't fall into place when promised.

3. Operating Co-Tenancy – The Operating Co-Tenancy provision protects

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Convention Reports

Your intrepid reporter attended the American Lodging Investment Summit (ALIS) in January and the International Franchise Association Convention in February. Much energy was devoted to strategies for maintaining positive growth in harder times with more demanding underwriting terms for financing and more challenges to operating efficiencies. Here are some observations on matters of interest to the hospitality world:

- Consumer spending fueled by perceptions of household wealth, spending against home equity and wage growth has ended. The economic stimulus package will not cure the underlying issues in the economy. Until all of the pain from the credit crunch and its fallout is known and absorbed, uncertainty will prevail. But uncertainty creates opportunity.

- Conventional financing is likely to return as the collateralized debt obligation (CDO) market continues to find turmoil. Underwriting criteria will be tighter but optimism about underlying values is rampant. Smaller transactions (less than $1B) are likely to be the focus of activity. Cap rates are increasing; interest only periods will be short and smaller loan pools will be created rather than larger so investors will better understand risks.

- Tourism and hospitality activity cannot be exported, but the U.S. does a poor job of serving foreign visitors. Exchange rates favoring foreign visitors cannot be exploited efficiently because of the paucity of in-bound marketing efforts. Homeland security concerns slow entry of visitors, and language barriers remain in all environments, even in gateway cities.

- If the trial lawyers succeed in getting Congress to pass the so-called Arbitration Fairness Act, the option to select arbitration for dispute resolution in consumer, employment and franchise disputes will disappear. There is no plan for additional courts at the federal and state level to handle the increase in litigation that could occur. Years of efforts creating skilled arbitration panels to handle routine disputes efficiently will be for naught.

- The industry has an opportunity to attract talented people but weak support of entry level recruiting and training means the best and brightest will continue to look elsewhere.

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Negotiating Lease Terms with the Bottom Line in Mind, *continued*

the restaurant tenant if the development does not meet the projected lease-up and opening success. This allows the restaurant tenant to pay the developer/landlord reduced rent (sometimes significantly reduced depending on the circumstances) or, in extreme cases, terminate the lease if the restaurant tenant has opened for business in the development and either (a) certain projected tenants do not open in the development or (b) a certain minimum percentage of the square footage of the development does not contain tenants (sometimes named tenants) which are opened to the public. Again, this is a sensitive provision for the developer/landlord, but one that the developer/landlord may concede, depending on market conditions and the negotiating acumen of the restaurant tenant.

4. Percentage Rent – Most restaurant leases contain a provision that requires the restaurant tenant to pay to the developer/landlord a certain percentage of the restaurant tenant's gross sales once the restaurant tenant has exceeded a natural break point in sales. Restaurant tenants are now in a better position to negotiate either the percentage to be paid to the developer/landlord or the amount of the natural breakpoint in sales. The definition of "gross sales" is a relatively standard definition, but the restaurant tenant must ensure that certain receivables are excluded from the definition. Otherwise, the restaurant tenant may be paying the developer/landlord more in percentage rent than industry standard.

5. Leasehold Mortgage – Most developers/landlords have been reluctant to include a Leasehold Mortgage provision in leases, usually because the developer/landlord simply did not want to complicate the negotiation process by having its (the developer's/landlord's) lender review and approve the Leasehold Mortgage language. The Leasehold Mortgage provision is a viable financing tool for the restaurant tenant, and one that should not be categorically dismissed and excluded from a lease.

6. Rent Abatement – Developers/landlords rarely, if ever, considered a Rent Abatement provision in the past several years, even in commercial circumstances which would warrant such a concession. Now that the market has turned, developers/landlords will include abatement, although such provisions are narrowly tailored to address specific matters such as interruption in traffic flow due to construction in the development.

Mr. Turner is an attorney in the Nashville office.

Convention Reports, *continued*

- Green is here to stay; customers expect sustainability as a key brand strategy.
- Strong brands that add value will be more significant to maintaining and gaining market share as the pie shrinks or stops expanding; focused investments by brands will reward the brand and its affiliates.

Yet Another Government Form...

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As foreign investors populate transactions in the hospitality space, one reporting requirement applies directly to the service sector. The International Investment and Trade in Services Survey Act ("IITSSA", found at 22 USC §3101) is administered by the Bureau of Economic Analysis of the Department of Commerce. IITSSA requires reports of all foreign investment in a U.S. business enterprise in which a foreign person owns 10% or more of the voting interest, unless the investment is less than $1 million, is under 200 acres, or is real estate intended for personal use.

Commerce will use this form to determine if it will require further survey information. In the alternative, assuming the asset value is less than $3 million or the land purchase is of less than 200 acres, investors still have to file what is called a "B13-c Exemption Claim," which still requires some accounting disclosures but is far less burdensome. This is usually completed by the investor's accountant. See the information at the web site of the Bureau of Economic Analysis at:

http://www.bea.gov/surveys/fdiusurv.htm and http://www.osec.doc.gov/ogc/occic/invest.html.

Post Trial Briefs: Reviving a Trade Name Damaged in Litigation, *continued*

have claims for losses arising from illness and possibly death. Unfortunately for the business, the affected customer is only the beginning of the problems. Many individuals and business owners do not recognize or appreciate indirect, secondary concerns and the financial significance of these secondary effects. Media reports of food poisoning dissuade potential customers from patronizing the affiliated establishments, even though no patron has been harmed.

Trade name restoration (TNR) insurance helps to minimize the impact on restaurants and other businesses in the hospitality industry when a food borne illness problem occurs. Business interruption insurance generally does not provide protection against the financial losses incurred after a food borne illness incident because the business did not sustain any physical harm or damage and it is able to continue to operate. TNR insurance provides protection by bridging this gap in insurance coverage.

TNR insurance protects against the loss of business income even if there is no interruption in the operation of the business or restaurant. This insurance policy operates by examining the business' historical operating income to determine the loss caused by the food borne illness incident. The insurance policy is triggered once a drop of more than 10% in the normal gross revenues occurs and is sustained for a period of seven days. After being triggered, the policy replaces lost revenue for a period of 18 months or until gross revenues are restored to within 10% of normal gross revenues, whichever is earlier.

In addition to protecting the revenue and income of the business, TNR insurance provides valuable services to help the insured handle a food borne illness incident. This insurance policy provides crisis management services to help the business confront the problem and deal with it effectively. The insurance provides assistance in handling the relevant government agencies, health departments, media and employees. The insurance also provides coverage for the expenses incurred in response to a food borne illness incident including the expenses of a food recall.

Not all food borne illnesses arise from an accident or conventional negligence. The insurance provider recognizes this and in addition to the above listed benefits, an insured business is covered for malicious contamination of its food or drink product. This protection even extends to protect a business against extortion and allows a business to make the necessary extortion payment in order to avoid a food borne illness incident.

TNR insurance protects against many food borne illnesses including Norovirus, E Coli, Salmonella, and Hepatitis A, among others. TNR insurance does not protect against three of the more notorious food borne illnesses that have received recent media attention: Hoof and Mouth disease, Creutzfeldt-Jakob disease and Bovine Spongiform Encephalopathy (more commonly known as "Mad Cow" disease.) These types of diseases rarely affect humans, but they can be disastrous to the hospitality industry through food recalls, fears, and/or food shortages.

TNR insurance can be very beneficial to many businesses in the hospitality industry, particularly larger businesses that are recognized primarily by their name and marks. QSR chains of national stature can benefit from this insurance because a food borne illness incident will create national media coverage and normally produce an immediate drop in sales.

A new restaurant may not be an ideal candidate for TNR insurance for several reasons. A new restaurant concept does not have an established, widely used trade name that needs protection. Like Valujet's renaming itself AirTran after an airplane crash in Florida, a small brand affected by food borne illness can be renamed. Its investment in brand goodwill has not accumulated and become too expensive to reconstruct. Finally, a new restaurant concept may not have the track record to demonstrate normal operating income in order to prove a loss if an incident occurs. The use of normal operating income as the benchmark for determining if the insurance protection arises may prevent a newly opened restaurant concept from taking undue advantage of this insurance.

TNR insurance can be beneficial to companies that have a proven track record with a significant goodwill investment in the brand's trade name and marks. This insurance allows insureds to weather a food borne illness incident, be it accidental or intentional, and address the problem with a crisis management team when a brand name change is not a realistic option. While this insurance does not absolutely protect the business which falls victim to a food borne illness incident, it helps bridge the gap of general business interruption insurance and minimize the secondary effects on the financial health of a business in the hospitality industry.

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Hospitalitas

When is a Release a Release?

Signed releases of all claims aren't always enforceable

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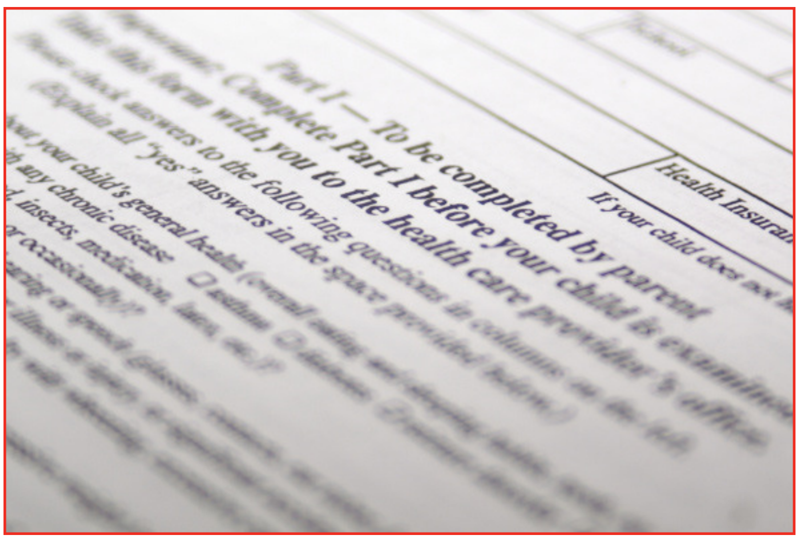
Businesses that provide recreational activities or other services where injuries are not uncommon often require that participants sign a release of all claims ("general release" or "release") before allowing them to engage in the activities. As a general rule, releases are valid and enforceable, but a release's enforceability will be dependent on many factors.

In three personal injury lawsuits against a Tennessee adventure camp/retreat center, a release was or could have been a defense to some or all of the claims against the retreat center. However, the "release" defense prevailed in only one of the three lawsuits. These three cases reflect the current law in Tennessee and, further, they provide some practical advice for any business offering recreational services.



Case No. 1: Retain a Copy of the Signed Release

In the first lawsuit, a woman who was participating in a hayride at a church retreat sued the retreat center for personal injuries when she shattered her ankle as she jumped from the hayride wagon. The retreat center had required all participants to sign a general release acknowledging that the participants were agreeing to release and indemnify the retreat center for all claims, damages, etc. "arising out of" participation in activities at the retreat center. The center's potential "release" defense vanished when they were unable to produce a copy of the woman's signed release. The lesson here is the importance of keeping good records and retaining the original, or a copy, of all signed releases in a safe place. In Tennessee, the delay between the event and the filing of a lawsuit can be as much as one year, so keeping the releases in a place where they can be readily retrieved is crucial.

Case No. 2: Obtain the Signatures of All Parents and Guardians When a Minor is the Participant

In the second lawsuit, a child participating in a school weekend retreat suffered injuries while participating in a "giant swing" activity. The release signed on behalf of the minor was signed by only one parent. The other parent sued individually and on the minor's behalf. In this case, the release defense was effective only as to potential claims of the parent who actually signed the release. Tennessee courts had adopted the majority rule that parents may not waive the rights of their minor children; thus, a general release signed on behalf of a minor is sufficient to preclude only the recovery by the person signing the release. The lesson here is that the business offering hospitality services to minors should require that all adults responsible for the child — whether parents, guardians, or custodians — sign the release. In this case, having both parents sign would have precluded recovery for the child's medical expenses.

Case No. 3: Releases Should Be Unambiguous

In the third case, a man was injured while participating in a corporate leadership retreat that his employer sponsored at the retreat center. The man admitted that he signed a general release prior to participating in the leadership/team-building activities and that he did so willingly and without duress. The general rule in Tennessee provides that a release is valid and enforceable in the absence of fraud and overreaching so long as the release is unambiguous and the releasor signed it without duress. The court dismissed his lawsuit upon a finding that the release at issue was unambiguous and voluntarily signed.

When is a release "ambiguous"? Under Tennessee law, a release is ambiguous only when it is of uncertain meaning and may be fairly understood in more than one way. Courts will take the language at face value and will refuse to find ambiguity where none exists. For example, failure to include the term "negligence" or "negligent" will not render the release ambiguous so long as the person signing the release had actual knowledge of the release and personally signed it. Even so, it is advisable that a general release expressly provide that the releasor is foregoing all claims based on negligence.

How does the court determine the intent of the person signing

When is a Release a Release?, *continued*

the release? The intent of the releasor will be determined from the unambiguous language of the release and from that language alone.

How does the court determine the scope of a release? A release generally covers all matters that might have been within the contemplation of the parties (as expressed in the release) when it was signed.

What if the releasor later claims not to have read the terms of the release? In the absence of fraud or duress, the failure of a party to read a release before signing does not affect its validity.

The lesson here is this: Releases should be unambiguous and must be signed without duress. This case also brings to light another tip to keep in mind: If an employer sponsors a retreat for employees and attendance/participation is not a condition of employment, the employer should require every employee/participant to sign a release as a condition of participation.

Conclusion: Enforceable Releases

Courts in the majority of states, including Tennessee, have concluded that agreements releasing parties from future liability for personal injuries caused by their own negligent conduct are permissible in the context of recreational activities. Tennessee courts have upheld releases in a wide variety of circumstances: white-water rafting events; horseback riding; riding a mechanical bull at a social club; health clubs; speedway racing events; hair straightening services at a cosmetology school; a burglar alarm service; snow skiing; sky diving businesses and other private recreational businesses. In Tennessee, courts will enforce a release even if the injury occurred during an activity that was not foreseeable or associated with a risk "inherent in the sport" so long as the release sufficiently demonstrates the parties' intent to eliminate liability for negligence. Releases have been enforced when health club patrons were injured by an exercise machine collapsing and by the broken belt of a vibrating machine and when a white-water rafter slipped and fell while disembarking from a bus used to transport participants from the river.

Note, however, that a release may not be enforceable if the incident was not the type contemplated by the parties when the release was signed. For example, a summary judgment for a health club was overturned in a case where the patron's injury resulted from inhalation of dangerous vapors created when a health club employee negligently mixed cleaning compounds, because this was arguably not the type of injury that was foreseeable to the patron at the time he signed the health club's release.

The cases and examples outlined in this article offer general guidance on the enforceability of releases, but enforceability of any release will depend on the specific circumstances of the case and applicable law. Businesses that could be liable for damages resulting from injuries incurred by their patrons are strongly encouraged to seek counsel for specific rulings and law that would impact their business.