



Broker Real Estate Licensure Emerging as Crucial Issue in Hotel Transactions

Since late 2008 the transaction environment in hotel real estate, as well as all other real estate classes, has been a challenging one. Worldwide hotel transaction volume decreased 64% in 2009. Year to date 2010 has fared better, but industry performance and lack of financing is continuing to constrain transaction volume.

As we enter the remaining months of 2010, investor confidence is rising and equity rich buyers are reentering the market, albeit at a cautious pace. Industry analysts predict a rebound in lodging demand through the remainder of 2010, and stakeholders in the hotel investment process, including brokers, are optimistically predicting an increase in transaction volume in 2011.

While the industry is navigating the market's financial and operational challenges, hotel sellers should be aware of an additional development creating more complexity and potential risk in hotel transactions: the increasing role of state regulatory issues relating to real estate brokerage licensure. Many states are increasing their efforts in license enforcement. Hotel sellers need to be knowledgeable of real estate brokerage licensing laws, and how this knowledge can reduce economic risk in their real estate transactions.

When it comes to real estate licensing issues, "*Caveat Venditor*" (Latin for "let the *seller* beware") is becoming an emerging doctrine for hotel transactions. Hiring a competent hotel broker with appropriate state real estate licensure is essential to a legal and successful hotel asset transaction. When sellers are better educated about real estate licensing laws, they are better to work with their broker as a team and create value in the transaction.

Real estate brokerage is big business. The National Association of Realtors represents more than 1.2 million members in North America. New York State, for example, alone regulates the licensure of more than 110,000 licensed real estate brokers and salespeople. The greater New York City metro market boasts more than 48,000 real estate professionals.

Individual states police broker licensure and their real estate regulatory bureaucracies exert potent positional power and regulatory authority in all aspects of real estate transactions, with brokerage regulation at the top of their priorities. Why is licensure compliance emerging as such a more crucial and enforceable element in their regulatory activities?

The simple answer is money. Due to the lower economic activity and diminishing revenue receipts, many states are facing widening fiscal deficits. State real estate regulatory entities are under growing pressure to raise revenues via toughening regulatory enforcement, which is fueling their efforts to generate additional fines and fees.

1420 NW Vivion Road
Suite 111
Kansas City, MO 64118 USA
+1.816.505.4315
Fax +1.816.505.4319
www.hbihotels.com

"According to statistics supplied by the American Hotel & Lodging Association, the licensed brokers of HBI have earned the legal right to broker 94% of all hotels (comprising 94% of all guest rooms) in the United States."
Joe McCann
President
Optimum Hotel Brokerage LLC

Concurrently, as the economy has adversely affected the real estate market, many real estate brokers (both residential and commercial) are facing greater competition for listings and clients. In this fight for survival, some brokerage organizations are likely to solicit and accept listings in states where they do not have legal licensure. Compounding this situation is the fact that individual state's resident brokers (commercial and residential), objecting to competing with out-of-state interlopers, are reporting these unlicensed brokers to their respective state's real estate license authorities. Licensed residential brokers are by far the largest source of complaints to licensing authorities for licensing violations. New Jersey, for instance, reports that 90% of all real estate regulatory complaints are filed by in-state brokers against other brokers.

The risks for sellers who hire inappropriately licensed brokers are worth considering. Should an unlicensed broker be reported or sanctioned during a property's listing period, the real estate commission will typically issue a "cease and desist" order (with appropriate fines and penalties) against the broker. While legal liability might not extend to the seller, this action will obviously have a disruptive, if not fatal, effect on the property's marketing process. And, even if an illegal listing flies "under the radar" of licensing authorities, a seller could be scrutinized (by buyers and their counsel) as an example of the seller not applying reasonable care in the proper marketing and conveyance of the property. Buyers are naturally looking for advantages in their negotiating posture with a seller, and material issues such as legal licensure could also affect a seller's position in negotiation. Licensing issues can sometimes survive a closing, as a seller's lack of reasonable care in determining proper broker licensure might reflect on his or her handling of other aspects of the transaction, should any contentious issues arise post-closing.

Some brokers, motivated to seek unlicensed out-of-state listings, offer glib assurances that state licensing laws can be circumvented by paying a third party broker or attorney to act as the legal licensee in a potential listing. This assurance may give a temporary measure of comfort to the seller, but many states have very strict rules applied to co-brokerage and license fees. Regulatory authorities exert very specific rules for real estate listings. Most states stipulate that the licensing broker must be properly identified in all communications, including listing agreements, print advertising, web advertising, brochures and flyers, cover letters and emails, contract, confidentiality agreements and offering packages. Some states require that only brokers licensed in state can conduct physical property tours. New Jersey, for instance, requires the listing broker to have a physical business address within New Jersey, and that the licensed New Jersey broker is the only party permitted to legally collect a commission from the seller. Regulations can vary from state to state; all the more reason to hire brokers licensed and knowledgeable in the hotel's resident state's real estate laws.

Just because a large brokerage firm has multiple offices in multiple cities does not necessarily mean the firm would have current licensure in every state. However, it appears that Hotel Brokers International, a membership organization with member offices throughout the United States, offers the hotel industry the most comprehensive real estate licensing coverage (91 total licensees) of any hotel brokerage concern. According to statistics supplied by the American Hotel & Lodging Association, the licensed brokers of HBI have earned the legal right to broker 94% of all hotels (comprising 94% of all guest rooms) in the United States.

How can sellers of hotels reduce their licensing/regulatory risk when taking a property to market? Obviously, the best answer is to hire a competent hotel broker with current and proper licensure in the state where the property is located. There are, of course, practical advantages in taking this legal approach, as a hotel broker with a strong local/regional customer base could likely attract more customers and buyer competition to the property. This can be done while still attracting a national audience through database marketing, advertising and affiliation with national hotel brokerage membership organizations. Sellers can also stipulate in their listing agreements that the broker possesses proper state licensure and that proper licensure will be material in his or her right to earn a commission.

As the lodging industry emerges from its latest down cycle and transactions begin to accelerate, sellers of hotel real estate (including banks and financial institutions) should be cognizant of the legal and regulatory issues involved in relationships with their brokers. The hotel transaction environment today is challenging enough. Proper broker licensure is just another important element in making the transaction process a win-win-win deal for buyers, sellers and brokers.

About the Author:

Joe McCann is president of Philadelphia-based Optimum Hotel Brokerage LLC and is Vice President of Hotel Brokers International and president of the Penn State Hotel and Restaurant Society. Optimum Hotel Brokerage is licensed in the states of New York, Pennsylvania, New Jersey, Connecticut, and Massachusetts.

