

No room at the inn for inept acquisition

Hotel acquisition, as the name suggests, refers to property investments that lead to the acquisition, running and operation of hotels. Many aspects of property acquisition in general are similar, but as with other acquisitions and their particular challenges, hotel acquisitions pose their own problems. The key challenges in hotel acquisition are those arising from leveraged assets, the costs of due diligence to confirm good title to land, obtaining and renewing licences and third-party consents needed by the hotel, and any restrictions contained in hotel management agreements (HMA). These challenges are analysed below.

Leveraged assets are, as the term suggests, assets whose costs are generally extremely high and have been funded through debt. It is imperative to note that all hotel properties in India are heavily leveraged. Hotel properties are so highly valued that acquiring them requires considerable funding which is only possible by taking on debt. Such debt must later be repaid from revenue generated by the hotel business. The recovery of such costs represents a huge risk and is a major deterrent to hotel acquisitions. This is therefore a major challenge to hotel acquisitions, since the repayment of the debt is linked directly to the performance of the hotel. A situation such as the pandemic, in which the hotel industry faced huge losses, is an example of why a highly leveraged asset is a risky call.

The second and a most significant challenge in hotel acquisitions, is due diligence and obtaining licences and third-party consents for the hotel. Challenges arise from the multiplicity of land laws and the historical nature of land holdings and titles. Carrying out proper due diligence in the acquisition of hotel property requires adequate time and resources to confirm good title to land, this being the sole responsibility of the acquirer. The outcome of such diligence may raise difficult issues for the acquirer in deciding whether to purchase or invest in the hotel property.

The acquirer must ensure that to operate smoothly, the hotel has in place all the licences and approvals that it needs on the date of opening. Licences include project approvals and approvals for the hotel's height, completion and occupancy certificates, registration under the

shop and establishment act of each state, restaurant and eating house licences, fire no objection certificates, licences from the Food Safety and Standards Authority of India, water and air pollution permits, permits under weights and measures legislation such as the Legal Metrology Act, 2009, goods and services tax registration, import and export licences and water supply connections. These approvals must be obtained or renewed in time for the scheduled opening of the hotel. Other key challenges for an acquirer are the existing HMAs and related contracts. These may contain restrictions on the transfer of shares and other restrictions imposed by the hotel operator on a new owner.

Beyond the funding and diligence stages of hotel acquisitions, other significant challenges include income and profit performance. This is a major factor in determining the growth of the business after acquisition, its ability to cover the costs of due diligence and its leveraged value.

Hotel acquisition faces challenges in the field of competition law, where large transactions are undertaken. This is usually the case with hotel acquisitions and the combination provisions of the Competition Act, 2002 (act) will be triggered. For example, any acquisition of control, shares, voting rights or assets and any mergers and amalgamations that cross specified jurisdictional thresholds must be reported to the Competition Commission of India (CCI). This will lead to delays in completing the transactions. Since the act implements a suspensory regime, a size of parties test may be adopted and transactions which meet any of the specified thresholds will have to be notified to the CCI.

Despite these challenges, the hospitality industry should be commended for continuing to grow. Indeed, the sector is flourishing. It must, however, be accepted that regulatory and other challenges complicate hotel acquisition. These obstacles cannot be done away with altogether, because although leading to delay, they are important in protecting the parties to transactions as well as the public.



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