

Hotel owner-level accounting: What you need to know

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Had I told the founders of my company 20 years ago that a quarter of the employees at their hotel asset management company would be accounting personnel someday, they would have said I was crazy. In fact, the accounting strategy for the very first portfolio we asset managed was to outsource it all—the portfolio accounting and internal recordkeeping.

That strategy lasted about four months. Just as we got ramped up, the assigned staff member from the firm we had hired walked out the door, along with all the deal knowledge on the accounting side. We were back to square one.

Over the years, we have gradually expanded our asset management team to include an increasing number of accounting professionals to assist hotel owners with this very important role—hotel ownership-level accounting—which, in most instances, are services not covered by management, nor contemplated by investors until well after a transaction has occurred. Whether a hotel asset management firm, or an accounting firm specializing in hospitality accounting, there are distinct benefits to having ownership-level accounting services provided by a qualified hotel expert, as opposed to a generalized accounting firm. Not only have owners found this to be more reliable, efficient and cost effective, especially if the group is already involved in an oversight capacity, but have also realized benefit through close collaboration with the operating team allowing for better planning, management, forecasting and distribution of cash flow.

How do you know if you need hotel owner-level accounting services?

The operator handles everything, right? Well, not exactly, but no two operators are alike. Some operators do provide a certain level of services for those items that fall below EBITDA after replacement reserves. Some will make debt payments, handle loan compliance and there are even a few that do fixed asset accounting. However, in the large majority of deals, property managers account for current assets and current liabilities and take the P&L through EBITDA less FF&E reserves. In order to comply with loan covenants, and to file proper tax returns, the hotel real estate owner needs to complete the financials.

In general, the operator will not adjust its accounting for the legal structure created by the owner's lawyers, and you wouldn't necessarily want them to either. Property controllers and directors of finance are very good at hotel operations and processes and procedures prescribed by their corporate offices. They do not typically have a lot of experience in complicated tax structures, loan calculations or financial reporting that are required in hotel deals—and you don't necessarily want them distracted from driving top-line revenue and managing labor while they learn how.

I would go so far as to argue that even if the management company agrees to do the work, owners should keep hotel financials completely separate from ownership entity financials. When it comes time to sell or refinance the hotel, the relevant information is contained within the hotel operating statement, and activity specific to the ownership entity should not be included.

What are the specific activities that comprise hotel owner-level accounting?

In general, hotel owners need to ensure the following key accounting activities are being handled on behalf of the ownership entity:

- Calculate and book interest, income taxes, depreciation and amortization (the ITDA of EBITDA)
- Reclassify expenses as needed to comply with the legal structure
- Calculate and book inter-company activity
- Move cash as needed by ownership and/or the legal structure
- Pay owner bills (not all costs can be paid by the property)
- Loan compliance reporting and calculations
- Audit coordination, schedule preparation and financial reports
- Income tax coordination, schedule preparation and review and filing of returns
- Refinancing, acquisition and disposition calculations and accounting

Owner-level hotel accounting requirements vary significantly depending on loan requirements, legal corporate structure and the amount of renovation activity at the property. For example, a select-service property held in a single LLC with minimal renovation activity may require very little attention. However, a big-box convention center hotel, with multiple layers of debt, held in a multi-entity REIT structure, that is also due for a renovation, will require significant hours each month to oversee and book activity. Further, some of the activities are routine, while others require detailed understanding of various legal documents and GAAP or IFRS, so it is important that owners retain the right skill set when selecting an accounting professional or team.

What are the key benefits of having a hotel specialist handle owner-level accounting?

Outside of the obvious expert guidance on loan and tax compliance, there are some distinct benefits and additional upside for hotel owners working with a hospitality accounting specialist. A few examples:

- Understanding seasonality and impact on cash flow for planning purposes whether to manage distributions or negotiate loan documents.
- Knowledge of hotel CapEx reporting, terms and useful lives and the know-how to use the data to efficiently code, place in service or dispose of items.
- Familiarity with brand protocol and reporting.



- Knowledge of common industry adjustments to DSCR and Debt Yield Calculations.
- Understanding of property tax and insurance accounts and how they are to be treated under the various organizational structures.
- Experience with REIT operating lease calculations.
- Ability to use accounting information to collaborate with management and owner representatives to improve performance.
- Expertise in hotel specific financial reporting (e.g. union pension fund and related party footnotes).
- Knowledge of what is missing (i.e. knowing what has not been provided).

Today, there is significant demand for hotel owner-level accounting services, both from international investors looking for guidance on U.S. GAAP accounting practices and compliance, as well as from U.S.-based hotel ownership groups who have experienced first-hand the value that hospitality experts can bring to this function.

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