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Who should "own" the hotel employees: No easy answers to that question

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Lawyers who provide employment counsel to hotel owners sometimes use a "legal audit checklist," to assist each with understanding nuances of employment-related legal requirements.

For Massachusetts hotel owners, the legal audit checklist is not short. Here's a sample of some of the areas that may be covered: the Massachusetts Wage Act; the Fair Labor Standards Act; requirements under collective bargaining agreements or "neutrality" agreements; the Massachusetts Domestic Violence Act; OSHA; state and federal non-discrimination laws (M.G.L. Chapter 151B, the ADA, the ADEA and Title VII); the Family Medical Leave Act; COBRA; state and federal payroll tax laws; the WARN Act; workers compensation; unemployment insurance; CORI checks; Massachusetts drug testing laws; Massachusetts mandatory health insurance laws; state and federal mandatory posting requirements; the Massachusetts independent contractor law; laws requiring notice to employees of negative material in personnel files; retirement or pension laws such as ERISA; and, effective as of July 1, 2015, the new Massachusetts Sick Leave Law.

Even for experienced hotel owner/operators, full compliance with so many employment legal issues is difficult - and the consequences of non-compliance can be dire. Union issues are highly complex and costly. Studies have shown that operating a unionized hotel may increase operating costs by as much as 38%. Employment litigation is also a major concern. Many employment laws have fee shifting provisions that allow successful plaintiffs to recover their attorneys' fees; and some, such as the Wage Act, require the payment of mandatory treble damages even for what may seem to be minor technical violations. Generally speaking, hotel owners may be perceived as having deep pockets. That fact alone may make them litigation targets, and such litigation may distract their attention from other business priorities as well as adversely affect operations as well as financing arrangements.

Yet, at this point, it is not possible to operate a hotel without at least a few employees. So what can a hotel owner do to mitigate risk of non-compliance? Obtaining employment practice liability insurance (EPLI) is a good start. There are also services available like ADP that can provide assistance with payroll related services and/or other employment-related compliance issues. However, the most common answer is to engage a separate entity-sometimes an affiliate, sometimes a bona fide third party-to "own" the hotel employees. Under such an arrangement, the property owner might believe that it has outsourced employment liability to an outside contractor. However, as with many things in life, the solution is just not that simple.

There is no such thing as a free lunch, especially when it comes to hotel management agreements. The typical hotel management agreement requires the hotel owner to pay base management fees between 2% and 5% of gross revenue, incentive fees between 10% and 20% of gross operating profit over certain hurdles and a variety of other fees (accounting, pre-opening, technical services, etc.). In addition, the owner usually reimburses the hotel management company for nearly all employment-related expenses (including in most cases the cost of employment litigation) attributable to the applicable property, usually out of a bank account pre-funded by the hotel owner. Frequently, the only expenses that the hotel management company must pay with its own funds are those directly attributable to the gross negligence or willful misconduct of a small group of high level employees of the hotel management company, most of whom work "off-site." In other words, in most cases, the owner will end up paying the same employment related costs, notwithstanding the fact that it has hired an outside management company.

In addition, many hotel owners are surprised to learn that courts and legislatures have taken a broad interpretation of the term "employer," the effect being that under many state and federal laws, a hotel owner may be considered a "joint employer" with the management company. The FMLA, FLSA, Title VII of the Civil Rights Act, the WARN Act, and many other applicable employment laws provide that if multiple entities share control over an employee, share in the benefits of the employee's work, or act in the interest of each other, all of such entities may be considered "joint employers." This thorny legal issue may very well result in a hotel owner being exposed to employment liability, notwithstanding all of the fees paid to the management company to "own" that risk.

Having a hotel management company "own" the employees may also present substantial logistical challenges when it comes time for the management agreement to be terminated. Even in situations where the hotel owner wants to have the employees continue working at the hotel post-termination, it is not uncommon for hotel employees to "rush to the exit" shortly before the termination. Some employees may feel loyal to the existing management company and want to move to another hotel managed by their "employer." Others might simply not understand that they will continue to have a job following termination of the management agreement because the hotel owner (or a buyer in the context of a sale of the hotel) may be prohibited from communicating with or soliciting the employees directly. In such instances, the employees' "rush to the exit" may cause a real problem for the hotel owner's ability to operate the hotel and/or maintain the value of its asset in the context of a sale.

In conclusion, there are no magic bullets. Employment related legal compliance is challenging for a hotel owner, regardless of who "owns" the employees. All options of dealing with such issues require careful consideration.

Joshua Bowman would like to thank Jennifer Ioli and Matthew Moschella for each of their respective assistance with this month's article.

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