

Part Two in a Three-Part Series

Pacific Landmark Hotel, Ltd. v. Marriott Hotels, Inc. (Series 2)
Government Guarantee Fund of the Republic of Finland v. Hyatt Corporation (Series 2)

PUNITIVE DAMAGES AFFILIATED WITH HOTEL MANAGEMENT AGREEMENTS

A Case Study of Agency Law, Hotel Management Agreements, and Punitive Damage Awards
Citing the Cases of

Woolley v. Embassy Suites (Series 1)
Pacific Landmark Hotel, Ltd. v. Marriott Hotels, Inc. (Series 2)
Government Guarantee Fund of the Republic of Finland v. Hyatt Corporation (Series 2)
2660 Woodley Road Joint Venture v. ITT Sheraton Corporation (Series 3)
P.T. Karang Mas Sejahtera v. Marriott International Inc., et al. (Series 3)

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Series Two (continued)

The next case discussed is *Pacific Landmark Hotel, Ltd. v. Marriott Hotels, Inc.* [Renard and Kristi]. This case is unique in that the management agreement specifically stated that Marriott's agency was "coupled with an interest and may not be terminated by owner until the expiration of the term of the agreements." The stated term of the management agreement was sixty years. At about the same time that the management agreements were put in place, the owners of the hotel secured loans with several of Marriott's subsidiaries totaling approximately \$23 million. The lenders secured these loans by deeds of trust and collateral assignments of the management agreements. In effect, the security for these loan transactions may have created an "interest in the hotels," thereby preventing termination of the management agreements. The trial court did find, in part, that "Marriott was an agent coupled with an interest" and that the owners could not terminate the agency. The court denied the owners' motion for a preliminary injunction. The owners appealed. The specific issues before the California Court of Appeals were whether the owners had the statutory power under California Civil Code § 2356 (a)(1) to terminate Marriott as their agent or whether Marriott's agency was "coupled with an interest in the hotel", thus making the management agreements irrevocable (Renard and Motley). The court relied on the *Woolley* decision in holding that the management agreements created an agency relationship between the owners and Marriott and that the owners retained the power to revoke the agency, unless the agency was coupled with an interest. As mentioned earlier, the management agreements specifically stated that Marriott's agency was "coupled with an interest and may not be terminated by owner." However, the court again looked to *Woolley* for the definition of "an agency coupled with an interest." The court found that the parties had not created an agency with an interest, despite the provisions of the management agreements. The court held that "even if the parties intended to create an irrevocable agency, one coupled with an interest, unless they do so and such an interest does in fact exist, the statutory power to revoke may be exercised." Marriott had argued that the prior loan agreements with its affiliated companies did, in fact, create an "interest." The court held differently, however, in ruling that Marriott itself did not have an interest that would have created an irrevocable agency.

This next case, *Government Guarantee Fund of the Republic of Finland v. Hyatt Corporation*, is a federal appellate decision that brought agency law into the federal arena (U.S. Court of Appeals for the Third Circuit, No. No. 96-7288). The owners of the Hyatt Regency on St. John, U.S.V.I., entered into a management agreement with the Hyatt Corporation in March 1990. Hyatt Corporation agreed to manage

the resort in exchange for a share of the long-term profits. The initial management agreement was for a 30-year term which included restrictive cancellation provisions. Prior to the execution of this agreement, the owners of the hotel obtained a loan for approximately \$120 million from Skopbank, a Finnish corporation (Renard and Kristi). Hyatt Corporation also entered into a subordination agreement (providing for continued occupancy should a subsequent owner take over) with Skopbank in the event the hotel owners defaulted on the loan. The owners, in fact, did eventually default on the loan, and Skopbank filed a foreclosure action in the District Court of the Virgin Islands in 1991. Subsequent to the foreclosure filing, Skopbank itself began to fail. Government Guarantee Fund acquired a controlling interest in Skopbank as part of the Finnish Government's bailout plan.

On February 1, 1995, the District Court put the hotel up for judicial sale. On March 20, 1995, 35 Acres Associates acquired the hotel. The new owners (35 Acres Associates) then informed Hyatt that its management agreement was terminated. Hyatt refused to vacate the hotel and surrender the keys. In March 1995, Government Guarantee Fund and Skopbank filed suit against Hyatt alleging breach of the management agreement and other causes of action. The plaintiffs sought declaratory judgment giving them possession of the hotel. Later, in November 1995, Government Guarantee Fund and Skopbank amended their complaint and included 35 Acres Associates as plaintiffs. Hyatt countersued 35 Acres Associates, Government Guarantee Fund and Skopbank. The District Court consolidated the two cases for trial. The court, in a non-jury trial ruled in favor of the plaintiffs and granted 35 Acres Associates possession of the hotel. Hyatt appealed to the Third Circuit Court of Appeals. "The Third Circuit held that a contractual provision created to prevent early termination is effective only to create liability for such wrongful termination". It further held that the "only exception to the principal's ability to terminate an agency relationship at any time (as expressed in *Pacific Landmark*) is when the authority granted to the agent is a power given as a security."

Essentially, the court said that the agency relationship itself does not establish or create an interest. "The agency merely serves to protect the separately granted or created interest when the two are coupled." After establishing that 35 Acres Associates rightfully terminated the agency relationship with Hyatt, the district court held that Hyatt could not continue to manage the hotel. The court did not address the issue of "wrongful termination" for which Hyatt could have been awarded damages.

(To be continued)
