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Labor Issues Still Plague Hotel Industry Post Pandemic

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As COVID-19 cases continue to fall and the U.S. economy regains its footing, the hotel industry is cautiously hopeful that leisure and business travel will swiftly rebound. While the recovery in the U.S. remains fragmented, with some areas such as Florida exceeding pre-pandemic RevPAR (revenue per available room) levels, and others such as San Francisco, New York City, Boston and Washington, D.C. remaining well below 2019 levels, the trend is undeniably positive in virtually every market.

Even with these reasons for optimism, the restarting of an entire industry is not without complications. Labor issues have always been at the forefront of the hotel industry, especially in places like New York City with an active union for hotel employees, and the pandemic has raised additional issues that have the potential to cause significant near- and long-term changes to the ways hotels do business.

Most immediately, many who have stayed in hotels in recent months can attest firsthand that staffing shortages plaguing many businesses is not sparing the hotel industry. As hotels reopen and try to prepare for an expected surge in bookings fueled by pent-up travel demand, hiring enough housekeepers, front desk and kitchen staff, and other hourly workers to operate hotels is an ever-present issue. The result of a lack of staffing is that hotels are left unable to keep pace with increased occupancy levels, forcing them to choose between leaving rooms unoccupied to keep guest numbers down at manageable levels, or risk having guests become dissatisfied by subpar service levels.

Given the nascent and uneven nature of the recovery, and the uncertainty regarding when and if staffing shortages will recede, making such choices is a day-by-day exercise for hotels. This is already causing friction between hotel owner and managers, with owners expecting managers to live up to their contractual obligations regardless of the staffing environment, particularly after almost 18 months of little to no revenues.

While it remains to be seen whether the staffing shortage is a short-term issue, other labor-related industry changes brought on by the pandemic are poised to be even more enduring and impactful. As one significant example, in late 2020 the New York Hotel Trades Council; AFL-CIO commenced an arbitration seeking to require a hotel lender to sign an assumption agreement agreeing to be bound by the Industry-Wide Agreement (the "IWA").

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Pursuant to an arbitral award issued on March 10, 2021, the owner of the hotel in Lower Manhattan was found to be in "technical violation" of Article 59 of the IWA by virtue of two agreements the hotel owner previously entered into in connection with its mortgage on the hotel property. Article 59(b) of the IWA requires that a signatory such as a hotel owner "make it a written material condition of any transaction of any kind whatsoever which transfers majority ownership, management or operational control of the Hotel…such that the party ("transferee") assuming such majority ownership, management or operational control must assume and be bound in writing to this Agreement."

The two agreements at issue were a mortgage agreement between the hotel owner and its lender and a subordination, assignment, non-disturbance and attornment agreement ("SNDA") between the hotel owner, its lender, and the hotel manager—both exceedingly common agreements used in hotel lending transactions. As articulated in the arbitral award, the dispute concerned whether an "unrealized security interest in the property" which allows the lender, in the event of default by the hotel owner on the loan, to take possession and control of the property (mortgage agreement) and remove the hotel manager (SNDA) violates Article 59 of the IWA because it does not expressly state that the lender or replacement manager must assume the IWA.

As argued by the hotel owner in opposing the union's claims, such agreements are commonplace in the hotel industry, and an adverse ruling may subject virtually every hotel owner and hotel manager to potential exposure for violating Article 59 of the IWA.

Acknowledging that the claimed violations purportedly arise from industry standard lending documents, the arbitral award did not direct immediate monetary relief for this "technical violation," permitting the hotel owner and hotel manager a "reasonable period of time to correct the violation," subject to a renewed application by the union for damages "if the violation is not corrected." Nevertheless, the award concluded by stating that "[t]he Hotel, and the rest of the Industry are on notice of the problem."

The arbitral award created immediate uncertainty in the hotel industry concerning, among other things, whether to "correct the problem" a lender will need to be bound to the IWA, and whether the Chairperson's placing the hotel industry on "notice of the problem" meant that all hotels bound to the IWA that have a loan or mortgage are now automatically in breach of Article 59 and liable for damages until the problem is "corrected."

On March 31, 2021, acting on a request initiated by the Hotel Association of New York City, Inc. for itself and on behalf of its constituent members, the Chairperson issued a clarification attempting to address some of this uncertainty caused by the arbitral award. While the Chairperson stated that the arbitral award "does not by itself bind lenders to the IWA absent special facts and circumstances," nor "mean that all Hotels bound to the IWA that have a loan or mortgage are now automatically in breach of Article 59," this clarification has done little to ease industry concerns.

In June, the hotel owner commenced an action in the United States District Court, Southern District of New York seeking to vacate the arbitral award. In its moving papers, the hotel owner laid out, in its view, some of the potential ramifications of the arbitral award:

The Impartial Chairperson's decision carries with it enormous consequences for the city's hotel industry. Never before has the IWA been interpreted to require a lender to join an industry-wide collective bargaining agreement based solely on its financing arrangement with a borrower. But now, hotels will be forced to pay monetary fines for a situation they are powerless to cure because they have no authority to force lenders to join the IWA. This leaves hotels with no choice but to either pay the Union not to file a grievance or pay the lender to join the IWA. And new loans may be difficult or impossible to obtain, given lenders' understandable reluctance to shoulder the obligations of the IWA when lending to hotels. With hotels already cratering under the financial pressure from COVID-19, the Impartial Chairperson's decision to disregard the plain text of the IWA comes at a time when the hotel industry can least afford it. Already, two hundred of the city's seven hundred hotels are shuttered—some permanently—and the industry is bleeding money by the day.

While it remains to be seen whether the hotel owner's prognostications are accurate, there is no doubt that hotel industry stakeholders are paying careful attention to how this dispute plays out. Not only could this arbitral award have a direct and lasting impact on the hundreds of hotels in New York City that are encumbered by a loan or mortgage, but it could result in vastly fewer market participants if financing hotel purchases is made more difficult.

In any event, this exemplifies one way in which the norms of the hotel industry may be changed forever by the pandemic. Stakeholders would be wise to take nothing for granted as the industry emerges from the pandemic, and that the pre-pandemic way of doing business may no longer be possible or make economic sense. This is particularly true in the always changing hotel labor market.

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