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**United States Department of Agriculture  
Rural Development  
California  
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## **B&I Program Insights # 4: MOTELS & HOTELS Business & Industry (B&I) Guaranteed Loan Program**

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### **Can the B&I program be used to finance motels and hotels?**

Motels and hotels play an important role in the economic development of rural communities, especially because recreation and tourism are often a key rural business sector. They also provide important revenues from occupancy taxes that support local rural governments.

Motels and hotels became eligible for B&I assistance when the B&I regulations were rewritten in December 1996. Prior to that, they had been ineligible for B&I assistance.

In light of recent adverse changes in the recreation industry, motel and hotel projects are being underwritten more closely.

### **What are the B&I program's underwriting standards for motel/hotel projects?**

Motels & hotels must meet all the normal B&I standards -- e.g., rural location. In addition, because they are single-use, special purpose facilities which are particularly vulnerable to economic downturns caused by high gas prices, etc., added strength is generally required as outlined below:

#### **Collateral**

65% LTV (max) on Real Estate is the normal standard because they are special purpose facilities.

70% LTV (max) on franchised Real Estate is acceptable because of the added benefits of the franchise.

25% LTV on the Furnishings, Fixtures, & Equipment (FF&E). Motel FF&E is very depreciable and has limited salability if removed during a liquidation.

Loans on motels/hotels should always be collateralized by both the real estate and FF&E, since the two are integrally related. A first lien position on both is important. If another lender holds a prior lien on either the real estate or the FF&E, additional discounting of the LTV is appropriate.

#### **Equity**

New or not-yet-established businesses -- 25% tangible balance sheet equity at guarantee closing.

Established, profitable business – 10% tangible balance sheet equity at guarantee closing.

#### **Appraisals**

Collateral analysis should use the current, "as improved" fair market value of the property.

A future, projected, "as stabilized" market value should not be used in the collateral analysis, since the property will not be "stabilized" in the event of a liquidation.

The value of the FF&E should be broken out separately from the value of the Real Estate.

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## **Feasibility Study**

Feasibility studies are required on all new motel and hotel projects. These must be separate and distinct from the real estate appraisal.

Feasibility studies should be prepared by independent consultants with an established expertise in the hospitality industry. See [www.hotel-online.com/Neo/Trends/](http://www.hotel-online.com/Neo/Trends/) for a list of some hospitality industry consultants.

The International Society of Hospitality Consultants (1-901-683-1806) may be a good resource. Appraisers with extensive motel credentials may be acceptable.

Information in the feasibility study should include detailed documentation & discussion of:

Supply -- including details on the regional and local market over the past 3-5 years, evaluation of existing competitors, and prediction of the entrance of new competitors.

Demand analysis -- including details on the market segments (vacationer, destination resort, business traveler, trucker, group meeting, etc.) that comprise historical and projected demand.

Occupancy & average rate analysis -- Average daily rate, % occupancy, and RevPAR.

Net income forecast -- including a detailed projection of income and expenses, with a discussion of the basis for expense figures.

## **Loan Term**

Loans for Real Estate purposes may extend up to 30 years.

Loans for FF&E should not exceed the useful life of the furnishings -- 7 years.

A blended term on a blended loan is permitted.

## **Income Statement Analysis**

In the hospitality industry, depreciation is a real expense, so adequate provisions should be made for regular repairs and upgrades.

## **Loan Agreement**

If the motel/hotel is a franchise, the loan agreement should require the borrower to maintain the franchise flag. Loss or termination of the franchise without the lender's consent would constitute a non-monetary default.

## **Loan Conditions**

If the motel/hotel is a franchise, a "comfort letter" should be obtained from the franchisor stating that the franchise will maintain its flag on the property during a liquidation.