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The Biggest Hospitality Cases Of 2014: Midyear Report

By **Natalie Rodriguez**

Law360, New York (July 15, 2014, 7:16 PM EDT) -- In the first half of the year, courts have issued a host of rulings that will shape legal strategies in the hospitality industry, delivering cautionary tales on guest privacy practices in a battle between Wyndham Worldwide Corp. and the Federal Trade Commission and reaffirming marketing guidelines for hotel-condo developers with a Supreme Court snub.

Several high-profile cases in the beginning of 2014 put new spotlights on the liabilities hotels can face over guest data and broken management agreements. And others reassured restaurant owners, tribal casino operators and more that status quo practices would not be upended.

No Escape for Wyndham in FTC Data Security Suit

When Wyndham Worldwide Corp. in April failed to shake a Federal Trade Commission suit over allegedly lax data security practices at its franchises, the ruling sent a warning signal throughout the industry.

“I think it highlighted in a material way for hotel management and franchise companies that they must be very careful in managing guest data,” said Cecelia L. Fanelli of Steptoe & Johnson LLP.

In refusing to toss the groundbreaking suit, New Jersey's U.S. District Judge Esther Salas rejected Wyndham's contention that the unfairness prong of Section 5 of the FTC Act did not permit the agency to regulate data security, among other arguments.

“Interestingly, the court rejected Wyndham Hotels and Resorts' argument that the case should be dismissed because its privacy policy excludes Wyndham-branded hotels from the policy's data security representations. Wyndham had asserted that such an exclusion of responsibility over franchisee's actions was consistent with franchise law generally,” Fanelli said.

While no final decision on liability has yet been made, the suit is high on attorney's radar screens, as further decisions in the case will likely reverberate through the industry.

Wyndham is represented by Jennifer A. Hradil and Justin T. Quinn of Gibbons PC, Eugene F. Assaf and K. Winn Allen of Kirkland & Ellis LLP and Douglas H. Meal and David T. Cohen of Ropes & Gray LLP.

The case is Federal Trade Commission v. Wyndham Worldwide Corp. et al., case number 2:13-cv-01887, in the U.S. District Court for the District of New Jersey.

Soda Ban Fizzles in NY Appeals Court

New York's highest court struck a blow to former Mayor Michael Bloomberg's so-called soda ban in June, ruling that New York City's health board exceeded its authority by imposing sugary drink portion limits on the businesses it regulates.

With the decision coming down on the side of the business-oriented plaintiffs, local restaurateurs and other venues sidestepped having to come into compliance with new rules, but the hospitality industry also may have won a small battle in a larger, multifront war over employment and operational policies, according to some.

“I think the recent New York Court of Appeals decision striking down the so-called large soda ban was a very significant decision for the hospitality industry, not just because it preserved my right to drink an extra-large Diet Coke at a Knicks game, but because it sets the possible stage for a showdown with municipalities like New York City as they continue to legislate in areas traditionally left to the states and federal government — areas like minimum wage, tips, paid time off and beyond,” said Carolyn Richmond, a co-chair of Fox Rothschild LLP's hospitality practice.

Richmond noted that hospitality companies are seeing increased municipal activism that is making business increasingly difficult for multiunit operators and franchisors that operate across jurisdictions.

For the city, however, the ruling was a blow to its efforts to reign in growing obesity levels, according to its corporation counsel.

“We are disappointed in the court's decision. We feel that this initiative was a valid exercise of the Board of Health's authority. Given the magnitude of this epidemic, we have no doubt that the board will continue to address the obesity crisis and the role of overconsumption of sugary drinks,” Zachary W. Carter of the New York City Law Department Corporation Counsel said in a statement.

The city is represented before the appellate court by New York City Assistant Corporation Counsel Richard Dearing. The plaintiffs challenging the ban are represented by Richard P. Bress of Latham & Watkins LLP.

The case is Statewide Coalition of Hispanic Chambers of Commerce v. New York City Dept. of Health, case number 134, in the Court of Appeals of the State of New York.

High Court Snub Equals Hotel-Condo Win

After the U.S. Supreme Court refused in February to scrutinize a Ninth Circuit finding that a Hard Rock hotel's condominium sales failed to amount to securities deals, the condo-hotel development market let out a collective sigh of relief.

With the ruling, condo-hotel developers were finally given a concrete reassurance that condominiums at a hotel complex could be sold and then managed as rental units without running afoul of the U.S. Securities and Exchange Commission.

“In terms of evaluating whether these types of sales are securities, it's provided more clear guidance to developers,” said James D. Gassenheimer of Berger Singerman LLP.

Several buyers of condo units in the San Diego Hard Rock had sued hotel operator Tarsadia Hotel and broker Playground Destination Properties Inc., alleging they had violated federal and state securities laws by misrepresenting the revenues buyers would get from renting out their units.

But the Ninth Circuit found that an eight- to 15-month gap between the real estate purchases and the execution of a rental management agreement offering unit owners a percentage of rental income meant the transactions were distinct and thus didn't constitute the sale of a security. By letting that opinion stand, the Supreme Court gave developers extra comfort that they could move forward on these mixed-use projects.

“This is an important financing vehicle in our market. One of our big hospitality clients is working on two projects — one in Nashville, and one in Atlantic City — where selling condos is a key component to the strategy,” Gassenheimer said.

The plaintiffs are represented by Maria C. Severson, Michael Aguirre and Christopher Morris of Aguirre Morris & Severson LLP.

Tarsadia Hotel is represented by Lynn Therese Galuppo, Ali P. Hamidi, Jonathan S. Kitchen and Frederick Kranz of Cox Castle & Nicholson LLP.

Playground Destination Properties is represented by Daniel M. Benjamin, Chrysta Elliott and Thomas W. McNamara of Ballard Spahr LLP.

The case is Salameh et al. v. Tarsadia Hotel et al., case number 11-55479, in the U.S. Court of Appeals for the Ninth Circuit and case number 13-763 in the U.S. Supreme Court.

Setai Award a Cautionary Hotel Management Tale

In June, the International Chamber of Commerce's court of arbitration ordered Lehman Brothers Inc. to pay General Hotel Management Ltd. more than $10 million in a suit accusing the bank of improperly terminating the hotel management firm's contract during an alleged forceful takeover of luxury property The Setai Miami.

The ICC International Court of Arbitration's decision was a significant reminder to the hotel industry of the care that needs to be taken when dumping a management team.

“It's a reminder of the care that owners must exercise in appropriately terminating hotel management agreements, in view of the potentially significant damages awards that they may face for wrongful termination,” said Fanelli, who represents companies on both the owner and management side of the table. “However, sometimes those damages are viewed as a necessary cost to exit a problematic personal services contract, which a hotel management agreement is.”

As the first case to go to trial involving a "midnight raid" at a hotel, in which managers are ousted suddenly in the middle of the night, it was also a significant addition to the growing case law surrounding owner and operator relationships, according to attorneys.

"One of the significant findings is the tribunal found the operator was not an agent of the owner under Florida law," said Daniel F. Benavides of Kozyak Tropin & Throckmorton PA, an attorney for GHM.

He said the decision went against past cases and gave other hotel managers a new legal tool in fighting against midnight takeovers: "They can go in using this case as a precedent and [possibly] get an injunction to remain."

GHM still has additional claims in state and federal court that may result in additional damages, Fanelli noted.

Setai is represented by William A. Brewer III, James S. Renard, Jack G. Ternan and Jeremy Camp of Bickel & Brewer.

GHM is represented by Daniel F. Benavides of Kozyak Tropin & Throckmorton PA.

The case is Setai Owners LLC (USA) v. General Hotel Management Ltd. et al., case number 18610/VRO/AGF/RD, in the ICC International Court of Arbitration.

Supreme Court's Casino Ruling a Win for Tribes

The U.S. Supreme Court handed a tribal casino operator an unexpected win in May by refusing to use the Indian Gaming Regulatory Act to rein in its sovereign immunity rights.

Affirming a Sixth Circuit ruling that Michigan could not use the IGRA to force Bay Mills Indian Community to shut down its off-reservation casino, the Supreme Court's 5-4 decision bolstered at least one other proposed casino's legal efforts and generally affirmed tribal sovereign immunity from state action.

"I am especially happy the court simply applied the statutory framework Congress has laid out in the Indian Gaming Regulatory Act," Matthew L.M. Fletcher, a law professor and director of Michigan State University College of Law's Indigenous Law & Policy Center, told Law360 at the time. "It's a flawed statute and a product of compromise, but that's politics. And when the court interjects itself into such a statute, it creates more problems than it solves."

The case had raised concerns that the court, which has a history of ruling against tribes in the cases it takes up, might cinch in sovereign immunity rights — which would have had serious negative repercussions for the $28 billion Indian gaming industry that many tribes rely on, according to several attorneys.

Despite the win for the tribe, however, the court did affirm that the state had a host of legal tools it could use to block the casino's operations, such as denying it a license or suing tribal officials or employees after operations begin.

"In remand, the state will continue its suit to close down the illegal casino. While the district court will not be able to order the tribe as an entity to refrain from breaking state law as [Michigan Attorney General Bill] Schuette had originally requested, it will be able to order specific tribal officials to follow state law," the attorney general's office has said.

Bay Mills is represented by tribal attorneys Kathryn L. Tierney and Chad P. DePetro and Neal Katyal, Jess

Ellsworth, Amanda Rice, Jonathan Schaub and former associate David Ginn of Hogan Lovells.

The petitioner is represented by Attorney General Bill Schuette, Michigan Solicitor General John J. Bursch, Louis B. Reinwasser and Margaret Bettenhausen.

The case is Michigan v. Bay Mills Indian Community, case number 12-515, in the U.S. Supreme Court.

Hilton Called Back On Call-Recording Class Action

In March, a divided Ninth Circuit reinstated a class action accusing Hilton Worldwide Inc. of violating California privacy law by recording incoming customer service phone calls. The decision, which revived plaintiff Rick Young's claims, knocked a district court for glossing over an added legal protection that cellphone calls are afforded over landline calls.

“It basically highlights the fact that it's easier to bring and maintain a claim for cellphone callers, rather than landline callers, to the extent that confidentiality is not required to be proven for a cellphone call,” said Richard M. Segal of Pillsbury Winthrop Shaw Pittman LLP.

Hilton escaped the case again Friday, when the lower court concluded that the statute only restricts third-party interception of cellphone calls and does not extend to recordings done for service monitoring purposes. But the case could still remold the litigation landscape over this issue.

"The district court's dismissal of the case on remand will be a very important decision if upheld because it finds that the cellphone statute covers only third-party interception of calls, rather than the recording of calls by the parties themselves," Segal said.

Even with the second dismissal, the case highlights the need for attorneys to make sure they advise hospitality clients to have a message at the start of calls that can't be bypassed and warns that the call may be recorded, according to Segal.

“It's essentially a get-out-of-jail-free card,” he said.

Young is represented by Ellyn Moscowitz of the Law Offices of Ellyn Moscowitz PC, Daniel F. Gaines of Gaines & Gaines PLC and Eric A. Grover of Keller Grover LLP.

Hilton is represented by Angela C. Agrusa, Allen P. Lohse and Randall J. Sunshine of Liner LLP.

The case is Young v. Hilton Worldwide Inc. et al., case number 12-56189, in the U.S. Court of Appeals for the Ninth Circuit.

--Additional reporting by Allison Grande, Pete Brush, Lisa Ryan and Andrew Scurria. Editing by Kat Laskowski.
