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## Condotels Meet Investors' Business and Leisure Objectives, Offering First-Class Amenities and Share of the Revenues

By Julie Bennett

**Bob Waun is CEO of Vacation Finance, a mortgage brokerage and lending company in Birmingham, Mich. He owns two hotel rooms that pay him to stay away.**

Until recently, Mr. Waun owned a traditional vacation home, a cottage in upper Michigan. But after a particularly bad winter -- he arrived during a snowstorm to find that the plow service hadn't cleared the driveway and that the pipes had burst -- he sold the cottage and bought two condo hotel units instead.

Now, Mr. Waun and his family vacation in resort hotels in Michigan and Florida, and earn money when the rooms they own are rented out to other guests. Mr. Waun, his wife Lynn and their nine-year-old daughter spent the Memorial Day weekend in their unit at the Inn at Bay Harbor in Petoskey, Mich., a 152-unit condotel managed by Marriott's Renaissance brand.

"As we were checking out, someone else was checking into our room and I made \$60 that night," Mr. Waun says. "If Marriott rents out the unit during the Fourth of July holiday, I'll make enough money to take my family on a trip to Mexico."

Experiences like Mr. Waun's are driving the market for condotels -- condominiums you buy that can be rented out as hotel space. According to Smith Travel Research in Hendersonville, Tenn., almost 10% of all hotel rooms under construction in the U.S. are condotel units and there are plans for 232 condotel projects with 98,237 rooms that could be built within the next decade.

Condotels are also being developed in Europe, South Africa, the Middle East and the Caribbean. Joel Greene, president of the Condo Hotel Center in Miami, a real estate brokerage firm that deals mostly in pre-construction units, lists 115 projects on his Web site, including five in Dubai.

### A financing solution

Guy Maisnik, an attorney with the Global Hospitality Group of Jeffer, Mangels, Butler & Marmaro LLP in Los Angeles, says his firm has handled 65 condo hotel projects and "almost all the new projects we see have a condo hotel component. This is a concept that definitely has legs."

Condotels started in Europe and first appeared in south Florida in the 1980s, but did not become popular until the travel slump after 9/11 made it difficult for hotel developers to obtain conventional financing for new projects. They turned to the condotel concept, pre-selling rooms to individual investors, to raise equity.

In theory, the condotel meets two objectives -- that of the developer to get a project built and that of the buyer who, like Mr. Waun, wants a hassle-free place to vacation and the chance to make a little money on the side. Baby boomers are becoming active vacation homebuyers, says Mr. Maisnik.

"If you buy a condo in Aspen," he says, "you're not likely to use it more than 30 days a year. If you want to rent it out, you'll have to hire a management company and take your chances. The attraction of a condotel is that you can own a unit in a hotel with a well-known name, like Trump or Mandarin Oriental, enjoy first-class amenities and standards of maintenance, then let the hotel company arrange all rentals for a 30% to 60% share of the revenues."

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Deciding whether a condotel meets your objectives is more complicated. Condotels are expensive, costing 10% to 40% more than traditional condominiums in most markets. Monthly maintenance costs, to pay your share of the hotel's upkeep, can run as high as \$900 for your 600-square-foot unit. Special assessments (costs paid for one-time occurrences) are common -- Mr. Waun has just paid \$250 to upgrade the linen on his Marriott unit's "heavenly bed" -- and you must pay to replace the furniture every five to seven years.

Buying that unit makes you an investor in the highly cyclical hotel industry. Tom Engel, president of the TR Engel Group, a lodging advisory and investment services business in Boston, says the \$123-billion U.S. hotel industry is currently hot. "We have more heads than beds and the industry should remain healthy for 24 to 36 months because we don't have a lot of new projects coming into the market," Mr. Engel says.

Long term, if the economy softens again, or if all the proposed condotel projects actually open, that situation could change. "First and foremost," says Mr. Engel, "the project must work as a conventional hotel, with enough demand 365 days a year to justify its existence."

That means that some rooms must be available 365 days a year for transient guests, and not filled with their vacationing owners. If you want to put your unit into the rental program, most condotel developers, like Robert Falor, CEO of Falor Companies in Chicago, will limit the time you can use it yourself. Mr. Falor, who is converting a hotel on Wacker Drive in downtown Chicago into Solis Chicago, says the project's 454 owners, who will pay an average of \$485,000 for their units, will be limited to 45 days of use if they want a share of rental revenue.

Developer Bayard Spector, president of Spector Real Estate Investments in Dania, Fla., says he bypasses such restrictions by building projects only in communities that limit condotel use in their zoning ordinances.

Mr. Spector is building 419 suites at the Atlantic Village Hotel and Marina at Dania Beach, Fla. Buyers who enter the rental program can stay in their suites for a maximum 90 days a year. His one-bedroom suites, which sell for an average \$500,000, include a feature not found in comparable projects -- a locked owner's closet for storing summer clothes and other belongings.

To buy that locked closet suite, or any condotel unit, you must get a mortgage and most traditional lenders shy away from the condo hotel marketplace. Chicago mortgage broker Oren Orkin of Perl Mortgage says the few lenders he works with require units to be at least 600 square feet in size (the average hotel room is 350 square feet) and to include a kitchen.

In his professional capacity, Mr. Waun says he's arranged a few hundred condotel mortgages, even for small units without kitchens, mostly with small private banks. "When you're condotel shopping, ask the salesperson which lenders have already written mortgages for the property," he says.

But don't ask how much money you'll make from the rental program. While the condotel you buy may generate some money, salespeople sell the units only as vacation homes. Developers are so skittish about discussing revenue -- thus invoking stringent regulations from the Securities and Exchange Commission -- that they've completely separated the sales and rental program functions.

Ray Velazquez, director of sales for St. George Residences & Condo Hotel, works from an office near the future luxury project's site, in Coral Gables, Fla. But he refers all rental program questions to the Fort Lauderdale office of Rich Richardson, owner relations manager for Hilton Hotels, which will manage the 200-unit property.

Mr. Richardson can give no specifics -- the project won't even open until summer 2008 -- and tells prospective buyers to check out the rate and occupancy levels of hotels in the area that are open now. Hilton, like all condotel operators, has devised a system so that all rooms in the rental program receive their fair share of paying customers. "Room allocation rotates like a carousel," Mr. Richardson says.

Mr. Waun says he purchased the least expensive condotel units available in his selected resorts, spending less than \$200,000 for his Michigan unit and about \$250,000 last November for a one-bedroom unit in the Mayfair Hotel & Spa in Coconut Grove, Fla. He says rental revenue from his Mayfair unit more than covered his mortgage payment and maintenance fees for December through March, but dropped off in April.