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Hotel Franchising

Why is a Hotel Franchise Worth Having?

Wednesday 16 June 2021

Bird & Bird & Is a hotel franchise worth having?

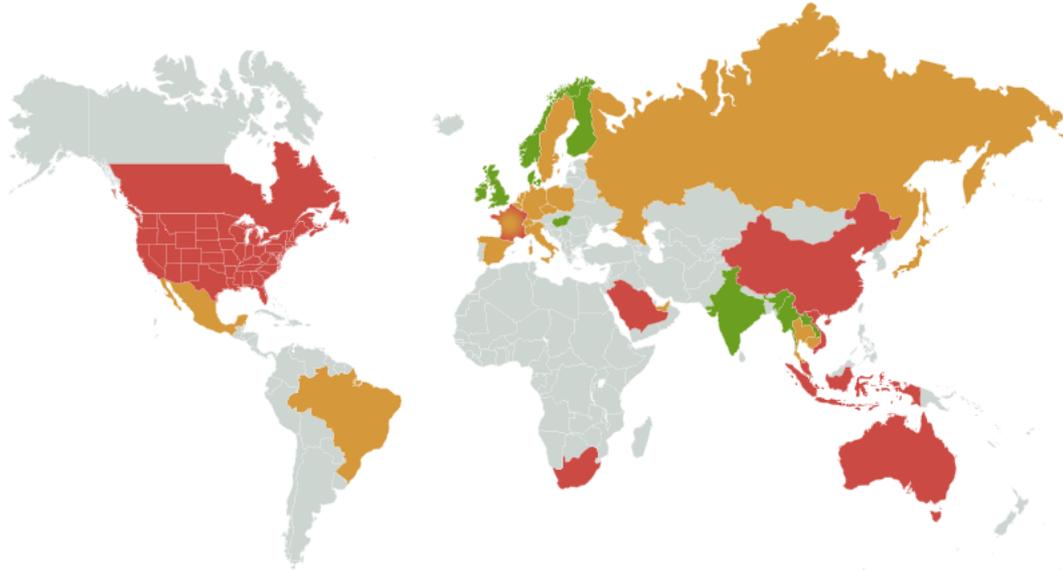


International Expansion



Bird & Bird &

International Franchise Laws Tracker



Key

Status

-  Light franchise regulation
-  Some franchise regulation that will need to be considered
-  Heavily regulated market for franchising

<https://www.twobirds.com/en/in-focus/international-franchise-laws>

The UK Franchise Landscape

UK 

Franchise regulation

No specific franchise regulation.

Pre-contractual disclosure requirements

No

Registration

No

Other issues

The laws of misrepresentation will apply to any pre-contractual disclosures made by the franchisor, and thus the franchisor should ensure that all such disclosures are complete and accurate, and accompanied by disclaimers where appropriate.

Difficulty Rating/Comments



Netherlands: The new Dutch Franchise Act



- The Dutch Franchise Act entered into force on 1 January 2021
- The overall aim of the Dutch Franchise Act is to strengthen the position of franchisees:
 - during the pre-contractual phase
 - during the term of the franchise agreement
 - to balance between protection and freedom of contract
 - post-term protections
- The legislation is similar to other European countries



Franchise Agreements



- For franchisees *established in the Netherlands*, the provisions of the Dutch Franchise Act cannot be derogated from (to their detriment), irrespective of the law governing the franchise agreement
- For franchise agreements concluded prior to the effective date of the Dutch Franchise Act (1 January 2021), certain requirements (goodwill, non-competition and consultation requirement) will only become applicable two years after the entry into force date of the Act



Key provisions

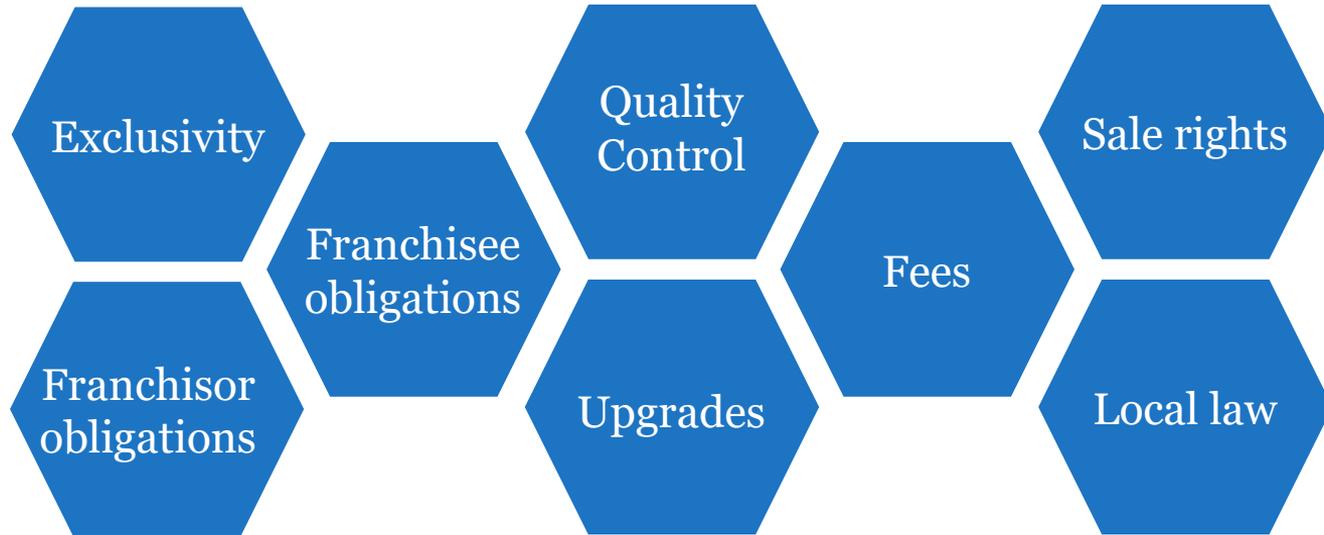


- **Pre-contractual disclosure obligations** on the franchisor, in addition to:
- A **standstill ('cooling off') period of 4 weeks** between the moment the franchisee receives all required information and the moment of signing the franchise agreement → There are **restrictions** during this period.
- Setting conditions for making **amendments to the franchise formula** which could have substantial (financial) consequences for the franchisee
- Requiring parties to capture in the franchise agreement, the right of franchisee to **receive reasonable goodwill**, if any, following the termination of the franchise agreement
- Limiting **non-competition restrictions** to a maximum of 1 year following the termination or expiry of the franchise agreement and the territory of operation of the franchise formula by franchisee

European Comparative Analysis

Country	Registration	Pre-Contractual Disclosure	Other specific franchise provisions	RAG Status	
Belgium	✗	✓	✗	Yellow	
Czech Republic	✗	✓	✓	Yellow	
Denmark	✗	✗	✗	Green	
Finland	✗	✗	✗	Green	
France	✗	✓	✓	Yellow	Red
Germany	✗	✓	✓	Yellow	
Hungary	✗	✗	✗	Green	
Ireland	✗	✗	✗	Green	
Netherlands	✗	✓	✓	Yellow	
Norway	✗	✗	✗	Green	
Poland	✗	✗	✗	Green	
Spain	✗	✓	✗	Yellow	
Sweden	✗	✓	✗	Yellow	
Switzerland	✗	✓	✗	Yellow	
UK	✗	✗	✗	Green	

Franchise Agreement – Key Terms



Franchise Model: Benefits & Risks – A Lawyer's View

Party	Benefits	Risks
Franchisor	<ul style="list-style-type: none">• Faster route to brand growth• On-going revenue with less capital at stake• Lower level of financial and operating risk• Leverage Franchisee's local market knowledge• Strong contractual rights	<ul style="list-style-type: none">• Less control over the operation of the hotel and compliance with brand standards• Increased risk of brand/reputational damage• Upside limited to receipt of franchise fees
Franchisee	<ul style="list-style-type: none">• Less risky form of market entry• Established brand & operating system• Operational support from the Franchisor• Control over the operation of the hotel (subject to brand standards)• Higher upside (after payment of franchise fees)	<ul style="list-style-type: none">• Higher level of financial and operating risk• Bound by brand-wide initiatives• Risk of breaches by other franchisees affecting performance of hotel

Thank you & Bird & Bird

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Why is a Hotel Franchise Worth Having?



Greater freedom or just a
different set of rules – is
franchising the way
forward for owners?

Bringing together the interests of hospitality real estate owners,
investors and developers around the globe

www.hoftel.com

HOFTEL's perspective comes from being an alliance of over 70 hotel owners, including all types of investor



Covid has accelerated changes already under way in the structure of hotel contracts



- Most hotel owners/developers like the idea of working with the big brands – but few of them like the standard HMA structure
- Management companies have varied in their approaches to the pandemic – and some owners have felt their reaction times have been too slow
- Franchising has emerged as a strong alternative, both for self-managed and white-label operated hotels and is growing fast around the world
- But owners need to be aware that there are still issues to overcome in getting this to work for them



Hotel management agreements are among the most one-sided contracts anywhere in the business world



Owner gives full control over operations, sales, hiring etc to the management company for a long-term contract....

....but remains on the hook for all costs and almost fully liable for whatever the operator does

Brands have consistently increased programmes involving central or regional charges or recharges

Termination, while possible in theory, is virtually impossible unless brand agrees to depart – termination clauses are usually un-failable

Operator can make money even while owner is going bust

“Standard” agreements are a myth – brands offer vastly different terms depending on scale/power and experience of partner and desirability of location

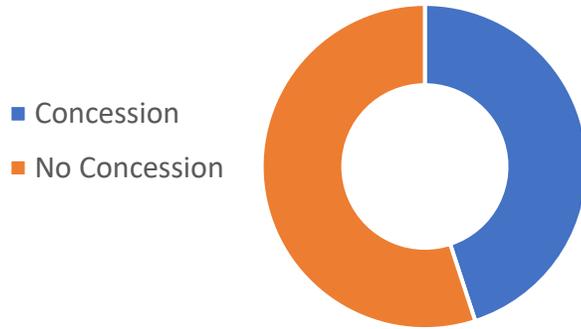
For new owners, contract terms are getting worse – no right to approve budget- in extremes: operator ability to force owner into cluster/complex; FF&E reserve expanded to all capex; only sequential choice of GM candidates



The recent crisis has focused owners on the degree to which their fate is not in their own hands

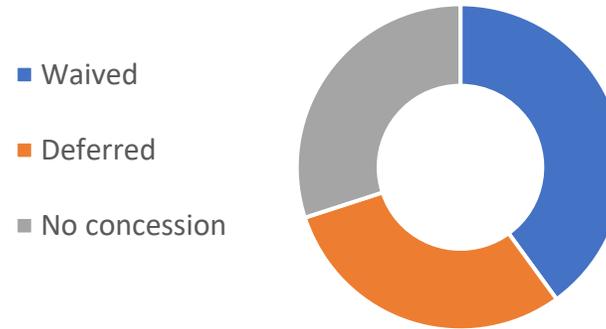


Management Fees



At the height of the pandemic, 55% of owners reported no concessions on management fees – while 45% benefitted from fee deferral, waiver or temporary reduction

FF&E Reserve



On FF&E reserve, over 40% were able to waive contributions, just under 30% to defer them and just under 30% has no concessions

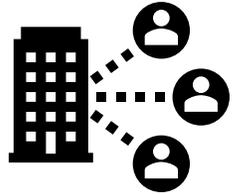
Sales and Marketing Fee (on Covid-related business)



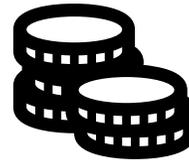
Around 40% were charged a sales and marketing fee on Covid-related business which did not originate from the Operator (quarantine, key workers, homeless or asylum seekers etc); but 60% were not.

The clear lack of consistency added to a desire to take more control and reduce expensive operator recharges

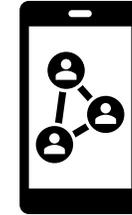
Franchising is emerging as a global alternative to the old HMA structure



Owners left in control of hiring, sales and revenue management, cost control, procurement



Recharges greatly reduced; ends fractious annual budget round



Still benefit from brand, lower OTA commissions, global distribution, standards



Rise of white label operators – Aimbridge, RBH, Pyramid, Valor etc – gives them an alternative to setting up their own management team (which may be hard to justify for single hotel or small portfolio)



In 2018, in Europe, according to HVS research, IHG franchised 56% of its hotels, Accor 48% Marriott 39% and Radisson 34%



In the USA the % of branded hotels under franchise rose from 70% in 2010 to 80% in 2019, according to JLL

However, it's not always as simple as it looks

Franchises have some contractual disadvantages relative to HMAs:

- No performance clauses
- Stricter rules on PIPs/brand standards
- Some fees upfront just for signing

Conversion discussion from HMA to franchise can be difficult:

- Compensation to brand for loss of fees – eg via lengthening contract
- Potential for unexpected PIP at the time of conversion
- Lender approval needed
- Issues around key staff retention

Are white label operators still “on the side” of the owner?

- Pipeline increasingly depends on being an approved brand partner – that relationship may matter more
- Institutionalisation – stories that white label operators also not sharing information fully with owners eg benchmarking
- Where are contract terms going – length, alignment?

Thank you for listening



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