Fair Franchising Is Not An Oxymoron: No. 2
AAHOA's 12 Points of Fair Franchising

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In 1998, the Asian American Hotel Owners Association identified a set of standards called the 12 Points of Fair Franchising by which to judge the actions of franchise companies. Now, nine years later, AAHOA has updated the 12 points and has embarked on a survey of franchisors to assess their compliance with these fair franchising standards. In each of my next Hotel Interactive articles, I will highlight the 12 points.

Point 2: Impact/ Encroachment/ Cross Brand Protection:
Franchisors should establish a fair and reasonable formula to protect a franchisee's assets, and the formula should be included as a contractual provision in their franchise agreements. The formula should include the following important terms:

> A. Franchisors should grant each franchisee contractual rights to a protected area or geographic "area of protection" (AOP) in which the franchisor will not allow another facility with the same or similar brand name as the franchisee's hotel to operate. For example, if the franchisee owns an ABC Hotel, the franchisor will not allow another facility with the same name (i.e., ABC Hotel) or a similar name (i.e., ABC Hotel & Suites) to operate in the protected area or geographic AOP.
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> B. Franchisors should be prohibited from licensing not only other franchised hotels with the same or similar brand name to operate in the protected area or geographic AOP, but also company-owned hotels.

C. The franchisee's protected area or AOP should be maintained and recognized until such time as the franchise agreement between the franchisor and franchisee has been legally terminated.

D. In the interest of providing fair impact rights, franchisors should adopt a reasonable and unbiased formula to determine which of the brand name hotels within the franchisor's system are competing in the same marketplace. The formula for determining which hotels are competing in the same marketplace for purposes of determining impact rights should be based on objective market criteria developed and relied on by reputable national organizations, such as Smith Travel Research (STR).

E. Upon receipt of an application for a proposed facility, franchisors should give written notice to franchisees of all brand name hotels within the franchisor's system that are (i) competing in the same marketplace as the applicant's proposed facility – even if these other hotels are not the same brand name as the applicant's proposed facility and (ii) within a 15- mile radius of the proposed facility.

F. To the extent a franchisee has a brand name hotel that is both (i) competing in the same marketplace as an applicant's proposed facility and (ii) within a 15-mile radius of the proposed facility, the franchisor should permit such a franchisee to request an impact study, so long as the franchisee(s) requesting the study have not been subject to a notice of termination within six months of making the request.

G. Any franchisee who requests an impact study should be allowed to choose the person or company who will be conducting the study. The selection should be from a list of at least five individuals or companies that have experience in the hospitality industry conducting such studies.

The list should be jointly compiled and agreed upon by the franchisor and the franchise advisory councils for the various hotel brands.

H. The costs of the impact study should be split equally between the franchisor and the franchisee(s) requesting the study (i.e., with the franchisor paying 50 percent, and the franchisee(s) requesting the study paying 50 percent), regardless of the outcome of the impact study.

I. To the extent an impact study concludes that the applicant's proposed facility will result in an incremental impact of three percent or more on a franchisee's existing hotel during the first three years of projections, franchisors should respond by (a) denying the application for the proposed facility, (b) offering the existing franchisee a first right of licensing for the proposed facility, and thereby allow the existing franchisee an opportunity to open a facility with the same or similar brand name in the same or similar brand name in the same or a nearby location, (c) offering reduced rates to the existing franchisee impacted by the proposed facility, or (d) allowing the existing franchisee to exit the system without paying LDs.

J. If the impact study concludes that the applicant's proposed facility will result in a less than 3 percent incremental impact on an existing franchisee's hotel during the first three years of projections, but within three years after opening date of the proposed facility, the existing franchisee is able to establish that it has, in fact, experienced an incremental impact of three percent or more on its hotel, the franchisor should respond by offering reduced rates to the franchisee impacted by the new facility or allowing the impacted franchisee to exit the system without paying LDs.

Turkel Comment:

Chain hotel companies (franchisors) try to convince hotel owners (franchisees) that they are partners in business. Their advertisements try to make owners believe that they are in the same business as franchisees. Never forget that franchise companies are in the business of selling franchises while franchisees are in the business of renting rooms to hotel guests. The reality is that they are in vastly different businesses.

Franchise companies make more money with two franchises in the same market area operating at 50% occupancy each than one operating at 75%. Just look at the calculation:

	One 100 Room Franchise	Two 100 Room Franchises
Available rooms	36,500	73,000
Occupancy %	75%	50%
Average daily rate	$100	$100
Room Revenue	$2,737,500	$3,650,000
5% Royalty Fees	136,875	182,500

In this example, with two 100 room franchises, the franchise company earns $45,625 (or 33.3%) more royalty fees every year in addition to the extra initial fee and all the ongoing fees including reservation costs, marketing expenses, frequent traveler programs and other miscellaneous fees such as software, purchasing, consulting and additional advertising services. No wonder most franchise companies provide no areas of protection.

Most franchisees do not receive any area protection from franchise companies who reserve the right to place a similar or sister brand hotel in the same market area. Some chains try to mitigate the effect of this competition by allowing existing franchisees to hire an outside consultant to measure the impact of the proposed new franchised property on the existing franchise. Stephen Rushmore, president and founder of HVS International says,

> "The process of quantifying economic impact is so subjective and fraught with bias, any hotel chain that relies on this approach in an attempt to appear fair and reasonable is shirking its responsibility to protect the interests of its existing owners. A much more equitable approach would be to negotiate a geographic area of exclusivity with the prospective franchisee that would require (franchisees) approval prior to granting a new franchise within the territory."

My book-in-progress "*Great American Hoteliers: Pioneers of the Hotel Industry*" will be published at the end of 2007 by McFarland & Company, Publishers, Jefferson, N.C. You can reserve an autographed copy by sending me an email at stanturkel@aol.com.

Stanley Turkel, MHS, ISHC operates his hotel consulting office as a sole practitioner specializing in franchising issues, asset management and litigation support services. Turkel's clients are hotel owners and franchisees, investors and lending institutions. He will review your proposed franchise license agreement and the uniform franchise offering circular and make written recommendations for beneficial changes in the license agreement. You can contact Stanley at 917-628-8549 or email stanturkel@aol.com.