



An Educational Primer



**A BEST-PRACTICE APPROACH TO DESIGNING,
DEVELOPING, AND IMPLEMENTING BEST-IN-CLASS,
MUTUALLY BENEFICIAL FRANCHISE SYSTEMS**

UPDATED IN 2022

The Updated 12 Points of Fair Franchising

In 1998, AAHOA identified certain best practices for the hospitality franchise system. AAHOA called those best practices the 12 Points of Fair Franchising (“12 Points”).

AAHOA has continuously updated the 12 Points to reflect business changes and the long-term, mutually beneficial relationship between industry franchisors and franchisees.

The revised 12 Points continues this mission as an educational primer for hospitality franchisors and AAHOA Members (current and future hospitality franchisees) to discuss and use to continue designing, developing, and implementing best-in-class, mutually beneficial franchise systems.

How to Use the 12 Points

- The 12 Points serve as an educational primer to help ensure all parties consider the major areas of franchisee-franchisor relationships, serving as a best-in-class approach.
- The 12 Points should be used to educate hospitality franchisors and AAHOA Members (current and future hospitality franchisees) on some of the most important areas of franchise relationships and agreements.
- The reader should rely on his/her own experts to seek advice related to franchisee-franchisor agreements and relationships.
- Franchisors can use the 12 Points to better understand the needs of their industry partners and franchisees.
- As with any legal-related matter, AAHOA strongly recommends all persons and AAHOA Members consult an outside lawyer and obtain professional advice and representation that is appropriate to their particular situation.

Good Faith As Contract's Core Value

Every contract imposes upon each party a duty of good faith and fair dealing in its performance and enforcement. Good-faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party. Bad faith [may include] abuse of a power to specify terms or to determine compliance or to terminate the contract.

**RESTATEMENT (SECOND) OF
CONTRACTS § 205 CMT. (A, D, E) (1981).**

12 Points Overview

A HIGH-LEVEL SYNOPSIS OF THE 12 POINTS



TERMINATION RIGHTS AND LIQUIDATED DAMAGES

A best-practice approach to voluntary buyout or involuntary termination, liquidated damages, windows provisions, early termination, and Franchisee termination rights



IMPACT, ENCROACHMENT, AND CROSS-BRAND PROTECTION

How to establish a fair and reasonable formula to protect a Franchisee's assets



MINIMUM PERFORMANCE AND QUALITY GUARANTEES

Minimum brand performance and quality guarantees from franchisors related to public image and reputation



QUALITY ASSURANCE INSPECTIONS AND GUEST SURVEYS

Ensuring consistent, unbiased, and reasonable standards for quality assurance inspections and accuracy of QA reports



VENDOR EXCLUSIVITY, REBATES, AND AFFILIATED COMPANIES AS VENDORS

Ensure competitive pricing



FULL TRANSPARENCY OF FRANCHISEE-FUNDED PROGRAMS AND FEES

The disclosure and accountability for the expenditure of marketing, loyalty, and reservation fees



MAINTAINING AND BUILDING RELATIONSHIPS

Establishing fruitful, long-term business relationships through recognition of value and effective communication



DISPUTE RESOLUTION

Creating a commitment to establish an independent and fair process for the resolution of disputes related to agreements or relationships



VENUE AND CHOICE-OF-LAW CLAUSES

Any party pursuing claims in a court of law should do so in the county and state in which the subject facility is located



FRANCHISE SALES ETHICS AND PRACTICES, PROPER DISCLOSURES

The mandate of fair and honest selling practices among Franchisor salespersons and agents



TRANSFERABILITY

When it comes to transferability, parties should not delay or act unreasonably



SALE OF THE FRANCHISE SYSTEM HOTEL BRAND(S)

Giving notice of a sale to existing Franchisees and pledging to a smooth transition between existing and new Franchisor owners

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



A. Voluntary Buyout or Involuntary Termination, and Liquidated Damages

Currently, if either a Franchisor or Franchisee seeks to terminate a franchise agreement, most Franchisors assess liquidated damages (“LD”) that penalize the Franchisee.

For example, many franchise agreements provide that LDs will be calculated based on one of the following formulas: (1) by assessing a rate of \$1,000 to \$2,000 for each guest room of the Facility, or (2) by multiplying the average monthly Gross Room Revenues by the Royalty Fees payable in the remaining months of the franchise agreement, multiplied by the number of months until the Franchisee could have terminated the agreement without penalty, not to exceed 36 to 60 months.

Fair franchising should require a Franchisee to pay a reasonable termination fee, not a penalty. In the interest of fair franchising, a Franchisee should pay only six months of royalty fees for early termination. Specifically, the Franchisee should be required to pay as LDs, and not as a penalty, the product of the average monthly Royalty Fees paid by the Franchisee during the prior 12 full calendar months (or the shorter time that the Facility has been in the system), multiplied by six (6) months or \$500/room maximum or a negotiated lesser amount, including the opportunity to pay zero LDs if the Franchisee signs a new franchise deal with Franchisor.

Further, in the event of an early termination, if a Franchisor has paid any “incentive” or “key” money to a Franchisee under the franchise agreement (including, for example, a development incentive advance, loan, or grant), the incentive money should be amortized over the total number of months of the term of the franchise agreement, and the repayment of any incentive money should be based on the number of months remaining under the agreement.

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



A. Voluntary Buyout or Involuntary Termination, and Liquidated Damages

Commentary

The current provisions relied on by Franchisors for assessing LDs are punitive in nature and not based on a reasonable estimate of the Franchisor's probable losses from the early termination of a franchise agreement. Regrettably, most Franchisors have been unwilling to negotiate or change such provisions to provide for a fair and reasonable method of assessing LDs based on, among other things, the actual amount of monetary losses Franchisors have experienced in the past as a result of an early termination, or the average amount of time it will take a Franchisor to replace the terminated Facility.

AAHOA's proposed method of limiting the LDs to six (6) months of average monthly Royalty Fees, excluding system assessment fees, for the subject Facility is fair and reasonable because it does not provide one side with a windfall or an unfair advantage over the other, and it compels both Franchisors and Franchisees to work together to avoid an early termination. Indeed, under AAHOA's method of assessing LDs, a Franchisor will have six (6) months to locate a replacement Facility of the same or similar brand name as the terminated Facility before it faces the prospect of suffering any losses arising from an early termination. Moreover, a Franchisee will still be required to pay a significant sum of LDs but will not be unduly penalized in connection with a voluntary buyout or involuntary termination of its franchise agreement.

If a Franchisor has given any "incentive" money to a Franchisee, that should not be used as a means of penalizing a Franchisee in the event of an early termination.

Rather than requiring a full repayment, the amount should be amortized over the term of the agreement, and any monies that must be repaid should be based on the remaining months under the agreement.

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



B. Windows Provisions

Most franchise agreements contain “window” or “additional termination right” provisions, which allow the parties to terminate the agreement on specified anniversary dates (e.g., on the fifth, 10th, or 15th anniversaries) after the opening date of the Facility, without having to pay LDs.

Regrettably, many Franchisors have included “gotcha” clauses in their franchise agreements. These clauses preclude a Franchisee from terminating early if the Franchisee encountered monetary or operational problems at any time after the opening of the Facility, which resulted in an alleged uncured default or low scores on quality assurance (QA) inspections on two consecutive occasions.

Such “gotcha” clauses should be eliminated from franchise agreements. A Franchisee should have the ability to terminate its agreement, with or without cause, as a matter of right, on the specified anniversary dates by giving at least six (6) months' prior written notice to the Franchisor. The only contingency for the exercise of the early termination rights should be that at the time of the proposed termination, the Franchisee is not in default and has paid all fees due under the franchise agreement.

Additionally, Franchisors should provide Franchisees at least sixty (60) days' notice of an approaching “window” opportunity (date).

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



B. Windows Provisions

Commentary

In franchise agreements containing “windows” or “additional termination right” provisions, the types of “gotcha” clauses that are most unfair are those that explicitly state a Franchisee’s rights will automatically terminate, without notice, if:

- 1. The Franchisee fails to cure any default under the franchise agreement within the time permitted, if any, in the notice of default sent by the Franchisor, or*
- 2. The Facility receives a poor score on a QA inspection and then does not receive a higher predetermined score set by the Franchisor during a re-inspection of the Facility.*

Consequently, in many situations, the fact that a Franchisee experienced financial or operational difficulties that resulted in a notice of default or low QA scores in the first few months or years after the opening of the Facility will forever preclude the Franchisee from being able to exercise its early termination rights without penalty.

This is true even if the Franchisee subsequently pays all its fees on a timely basis, and receives excellent QA scores for many years, before attempting to exercise its early termination rights. These “gotcha” clauses give the Franchisors an unfair advantage and should be eliminated from all franchise agreements.

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



C. Early Termination for Underperforming Properties

As discussed in Point 3 of the 12 Points of Franchising below, Franchisors should issue minimum performance guarantees to Franchisees regarding the occupancy levels of their brand-name hotels.

To address this issue, some Franchisors have adopted a “policy” that allows a Franchisee to terminate its franchise agreement without penalty if the Facility is underperforming and certain conditions are met. At a minimum, Franchisors should include the provisions of their fair franchising “policies” as contractual terms in their franchise agreements.

These specific contractual terms should provide that the Franchisor will allow a Franchisee to terminate the franchise agreement without penalty if the property has achieved below a pre-negotiated RevPar for a period of twelve (12) months or more or an occupancy rate (total occupied rooms divided by total available rooms) that is below fifty percent (50%) for a period of twelve (12) months or more. There should be no restrictive or unnecessary conditions placed on a Franchisee’s ability to terminate the agreement early for low occupancy rates.

EARLY TERMINATION, TERMINATION RIGHTS, AND LIQUIDATED DAMAGES



D. Early Termination by Franchisor and Franchisee Termination Rights

No franchisor may terminate a franchise agreement prior to the expiration of its term, except for good cause.

Good cause shall be limited to the Franchisee's failure to substantially comply with the agreement's requirements. Ninety (90) days prior to any proposed early termination, the Franchisor shall provide the Franchisee with a written termination notice setting forth each basis for termination and providing the Franchisee with an opportunity to cure the default.

The termination notice shall also provide the Franchisee a full and fair opportunity to contest the termination.

IMPACT, ENCROACHMENT, AND 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), which should be at least a minimum of three (3) miles in all directions of the subject property within 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. In addition, the franchisor will not allow another Facility operating under its umbrella of brands to operate in the protected area if that brand has similar characteristics, segments, and amenities to the franchise in question.
- (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).

IMPACT, ENCROACHMENT, AND CROSS-BRAND PROTECTION



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(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 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 (6) months of making the request.

(g) Any Franchisee who requests an impact study should be allowed to choose the person or company that will conduct the study. The selection should be from a list of at least five (5) 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 fifty percent (50%), and the Franchisee(s) requesting the study paying fifty percent (50%), regardless of the outcome of the impact study.

IMPACT, ENCROACHMENT, AND CROSS-BRAND PROTECTION



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(i) To the extent an impact study concludes that the applicant's proposed Facility will result in an incremental impact of three percent (3%) or more on a Franchisee's existing hotel during the first three (3) years of projections, Franchisors should respond by offering the Franchisee the opportunity to choose the following: (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 a nearby location; (c) offering reduced rates to the existing Franchisee impacted by the proposed Facility; and/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 three percent (3%) incremental impact on an existing Franchisee's hotel during the first three (3) years of projections but within three (3) years after the 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 (3%) or more on its hotel, the Franchisor should respond by (a) offering reduced rates to the Franchisee impacted by the new Facility; or (b) allowing the impacted Franchisee to exit the system without paying LDs.

MINIMUM PERFORMANCE AND QUALITY GUARANTEES



Franchisors should issue minimum-performance guarantees to Franchisees regarding the occupancy levels of their brand-name hotels, and the number of reservations that will be delivered through the Franchisors' reservations systems.

Franchisors also should commit to maintaining a certain level of quality in the franchise system, including, for example, the key characteristics of each brand name, the public image and reputation they will develop for each brand name, the minimum number of hotels they will maintain under each brand name, and the amount and type of advertising they will employ for each brand name.

Thus, if a Franchisee's hotel is not able to maintain certain occupancy levels over a designated period of time as discussed in Point 1 of the 12 Points of Fair Franchising above, or if the Franchisor allows the quality of a particular brand name to decline, the Franchisee should be able to terminate the franchise agreement without penalty.

QUALITY ASSURANCE INSPECTIONS AND GUEST SURVEYS



Franchisors should have the same standards for each of their Facilities operating under a specific brand name in the franchise system.

Franchisors also should conduct their quality assurance (QA) inspections in a fair, reasonable, and unbiased manner, and use their best efforts to prepare QA reports that are accurate and complete.

If a Franchisee fails a QA inspection and is given a punch list of items to repair, correct, or change, the Franchisee should strive to complete all of the items on the punch list in a timely manner and be given an appropriate cure period. During the subsequent re-inspection of the Facility, the Franchisor should seek only to confirm that, in fact, the Franchisee has completed all of the items on the punch list. If so, the Franchisor should give the Franchisee a passing grade. During the re-inspection of the property, the Franchisor should not create an entirely new punch list of items that were not previously mentioned or give the property a failing score for items that were not included on the original punch list.

In the event of a dispute concerning a QA inspection or low scores arising from guest survey cards, Franchisors should establish an appeal process whereby a Franchisee can appeal the decision of an inspector or challenge the low scores it received from the guest survey cards. In connection with the appeals process, the Franchisee should be able to present evidence that it's in compliance with the standards of the hotel brand or request that the director or supervisor of the Franchisor's quality assurance department personally visit the property and reinspect the Facility to ensure it is satisfying the necessary standards.

Guest surveys, online comments, or other guest rating systems should never be used as a basis for default, penalty, or termination.

QUALITY ASSURANCE INSPECTIONS AND GUEST SURVEYS



Commentary

Franchisors should use their best efforts to work with, educate, and train Franchisees who have received one or more failing QA inspections or low scores arising from guest survey cards to ensure the Franchisees understand and are doing whatever is necessary to cure the failing QA inspections and/or improve the scores and thereby avoid problems in the future.

In the interest of fair franchising, a Franchisor should not terminate a Facility based on one or more alleged failing QA inspections or because of low scores from guest survey cards unless and until each of the following has occurred:

- *The Franchisor has thoroughly analyzed the facts and circumstances concerning the failing QA inspection reports and/or the low scores from the guest survey cards and evaluated whether there are any valid reasons why the property received such failing grades or negative comments on the survey cards at the time they were issued; and*
- *The Franchisee has been given a reasonable opportunity and an adequate amount of time to cure any failing QA scores, problems with the property, and/or improve the guest survey scores; and*
- *The director or supervisor of the Franchisor's QA department has personally visited the property and has issued a written statement verifying that the Facility is not in compliance with the standards of the hotel brand and should be terminated.*

VENDOR EXCLUSIVITY, REBATES, AND AFFILIATED COMPANIES AS VENDORS



In general, Franchisees should be free to buy conforming goods from any vendor, not just those mandated by the Franchisor.

To the extent a Franchisor believes it is necessary to mandate vendors for the purpose of establishing standards and specifications for the hotel brands, the Franchisor should strive to ensure that the Franchisees are receiving competitive prices or best-price guarantees by providing a list of three (3) or more approved vendors from which Franchisees can purchase conforming goods or by allowing the Franchisees to take advantage of the volume discounts arising from the Franchisees' group purchases of goods and services.

But if the three (3) or more approved vendors do not provide the Franchisee with competitive market pricing, the Franchisee should have the option to apply for a waiver if/when the Franchisee locates products that do provide competitive pricing and the products' specifications meet the Franchisor's requirements. In addition, goods or items that do not affect the guest stay should not be mandated by the Franchisor.

In addition, since the Franchisors receive a significant amount of revenues from the mandated vendors in return for requiring all Franchisees to purchase certain goods and services only from such vendors, Franchisors should return these revenues to the Franchisees for the good of the franchise system. Ideally, Franchisors should not receive commissions from vendors.

VENDOR EXCLUSIVITY, REBATES, AND AFFILIATED COMPANIES AS VENDORS



Commentary

In the interest of fair franchising, Franchisors should strive to ensure that the Franchisees are receiving competitive prices on all goods and services that they are required to purchase from mandated vendors.

In fact, during most franchise sales presentations, a prospective Franchisee is told that a benefit of buying the franchise is the group purchasing power of the franchise brand. This can be accomplished in a variety of ways.

For example, Franchisors should identify three (3) or more approved vendors from whom Franchisees can purchase the goods or services. Franchisors also can pass on the volume discounts on prices arising from the purchasing power of the Franchisees.

Franchisors should not be allowed to pocket the entire amount of revenues they receive from mandated vendors and/or affiliated companies in return for requiring all Franchisees to purchase certain goods and services from such vendors and/or affiliated companies. Franchisors should retain only that amount of revenues necessary for the Franchisors to cover the administrative costs of managing the mandated vendor program.

All other revenues and related benefits received from mandated vendors should be invested in programs that benefit the Franchisees, including allocating the money to marketing and advertising campaigns for the hotel brands or reducing the Franchisees' royalty fees.

Vendor competition to provide goods and services to franchisees should be based on who provides benefit to the franchise system, which includes the franchisors and the franchisees.

FULL TRANSPARENCY OF FRANCHISEE-FUNDED PROGRAMS AND FEES



There should be full Franchisor disclosure and greater accountability concerning the expenditure of marketing, loyalty, and reservation fees collected from Franchisees.

This full disclosure and accountability, however, should exclude corporate overhead for employees unrelated to the above-mentioned programs.

On an annual basis, Franchisors should disclose how the technology, marketing, loyalty rewards program, and reservation fees are collected and spent, including identifying the specific products and services that are paid for with the fees.

A Franchisor should not profit directly from the marketing, Master Service Agreements (“MSA”), technology, loyalty rewards program, and reservation fees it collects from the Franchisees or use such fees to pay for marketing and advertising related to a Franchisor’s sale of hotels.

Franchisors should have their books and records audited on an annual basis, by an independent accounting firm, concerning the collection and disbursement of marketing, loyalty, and reservation fees, and should share the results of the audits with all franchisees.

A Franchisor should not profit directly from the expiration of loyalty reward fees and/or any liquidation of points from a sale it may have collected from the Franchisees. Instead, such benefits and profits should remain in the program and be used to reduce future program costs. Franchisors should not create loyalty points. Rather, loyalty points should derive from guest stays only.

Franchisees also should have the option to voluntarily participate in any programs and not be mandated by the Franchisor.

MAINTAINING AND BUILDING RELATIONSHIPS WITH FRANCHISEES



Franchise agreements establish fruitful, long-term business relationships between Franchisors and Franchisees. Franchisors should strive to build on and maintain these relationships with the Franchisees by (1) tangibly recognizing their value, and (2) effectively communicating with their Franchisees.

A. Maintaining the Relationship

Franchisors should recognize the value of the long-term Franchisee relationship.

Many Franchisees successfully remain in the Franchisor's franchise system through the term of their license. This long-term successful relationship provides significant benefit to the Franchisors, which should be acknowledged and managed accordingly. But unfortunately, when a long-term Franchisee seeks relicensing, the Franchisor often seeks relicensing fees up to \$150,000 and personal guarantees.

Re-licensing fees, however, should be waived for the long-term Franchisee. Likewise, personal guarantees should not be required for Franchisees who have performed well and according to the franchise agreement, or alternatively, personal guarantees for these Franchisees should be for a very limited time period – determined by the parties – after reasonable review and negotiation.

In short, waiving re-licensing fees and personal guarantees is integral to recognizing the Franchisee's contribution and loyalty to the Franchisor's franchise system and maintaining a fruitful, continued business relationship.

MAINTAINING AND BUILDING RELATIONSHIPS WITH FRANCHISEES



Franchise agreements establish fruitful, long-term business relationships between Franchisors and Franchisees. Franchisors should strive to build on and maintain these relationships with the Franchisees by (1) tangibly recognizing their value and (2) effectively communicating with their Franchisees.

B. Building on the Relationship – Franchise Advisory Councils and Franchisee Associations

Franchisors should strive to build on their relationships with the Franchisees by actively seeking feedback from the Franchisees themselves and by working with the various councils and associations that represent the Franchisees, including the brand Franchisee Association, Franchise Advisory Councils (FACs), and AAHOA.

Additionally, Franchisors must recognize a franchisee may freely associate with other franchisees or associations without interference, retaliation, contingencies, or limitations.

Franchisors should encourage and support the establishment of independent and democratic FACs or Franchisee Associations, which are comprised of a representative group of Franchisees elected by the Franchisees themselves and who can advise the Franchisor on matters of importance to the franchise system.

MAINTAINING AND BUILDING RELATIONSHIPS WITH FRANCHISEES



Continued...

B. Building on the Relationship – Franchise Advisory Councils and Franchisee Associations

At least six (6) months before implementing any changes to the franchise system, Franchisors should seek feedback from the FACs and/or Franchisee Associations, and use their best efforts to follow the recommendations proposed by the franchisee representatives on such matters.

- **Amenity Creep.** Amenity creep is a recognized problem in the hotel industry, and Franchisees are concerned that they are not being heard on such issues. Franchisors should regularly seek input from the FACs and/or Franchisee Associations concerning whether specific amenities should be added, eliminated, or changed for the brand-name hotels. Prior to mandating the addition of a new amenity, when the costs are solely incurred by the Franchisee, Franchisors should submit the issue for a vote to the Franchisees themselves and obtain at least a sixty-six percent (66%) vote of approval from all Franchisees who vote on the matter.
- **Marketing and Advertising.** Franchisors should regularly seek input from the FACs and/or Franchisee Associations concerning how best to market and advertise the various brand name hotels and their services. For example, Franchisors should consult with the FACs concerning the annual marketing and advertising budgets, the annual marketing and advertising plans, the format and scope of the directories of hotels in the franchise systems, the franchise system internet websites, and the operational plans for the franchise central reservation system. As discussed in Point 6 of the 12 Points of Fair Franchising above, there should be greater Franchisor disclosure and accountability concerning the expenditure of the marketing and reservation fees, including annual audits that are shared with the franchisee representatives or their audit committees.

MAINTAINING AND BUILDING RELATIONSHIPS WITH FRANCHISEES



Franchise agreements establish fruitful, long-term business relationships between Franchisors and Franchisees. Franchisors should strive to build on and maintain these relationships with the Franchisees by (1) tangibly recognizing their value, and (2) effectively communicating with their Franchisees.

C. AAHOA Relations

Franchisors should strive to work closely with AAHOA and its members to promote fairness in the franchise system and to enhance their respective business interests.

Franchisors also should seek ways in which they can:

1. Increase and improve their communications with AAHOA and its members,
2. Obtain input and feedback from AAHOA and its members on issues concerning the franchise systems,
3. Educate and train AAHOA and its members on matters that will improve the individual hotels and strengthen the franchise system on a global basis.

Franchisors should attempt to meet with AAHOA personnel on a regular basis to discuss these and other related issues that are of importance to the AAHOA Franchisee Members.

MAINTAINING AND BUILDING RELATIONSHIPS WITH FRANCHISEES



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C. AAHOA Relations

AAHOA Certificate in Hotel Ownership® (“CHO”)

The AAHOA Certificate in Hotel Ownership® (CHO) is an innovative professional development program specifically designed for hotel owners. The CHO program involves a comprehensive course listing of twelve (12) modules developed by world-class instructors. Attendees will complete two courses of their choosing under each module and will take a post-course exam. Franchisors should recognize and support the AAHOA CHO as a hospitality professional accreditation program, and CHO graduates should be given credit for successfully completing the CHO program in the same manner that, for example, the Certified Hotel Administrator (CHA) and Certified Lodging Managers (CLM) training courses have been supported and recognized by Franchisors in recent years.

Commentary

The CHO Program was designed to recognize and certify the expertise of AAHOA’s member hotel owners and is the first program of its kind in the country.

The CHO program covers a variety of topics, including

- *Front Desk Operations and Reservations*
- *The Laws of Innkeeping*
- *Leadership*
- *Hotel Sales*
- *Marketing and Public Relations*
- *Hotel Accounting and Business Ownership Structure*
- *Technology for the Lodging Industry*
- *Human Resource Management*
- *Housekeeping, Laundry, Engineering, and Maintenance*



The CHO program has several recognized sponsors, including Best Western International, Inc., and was developed by Kapoor & Kapoor Hospitality, Inc.

DISPUTE RESOLUTION



In all franchise agreements, Franchisors and Franchisees should commit to establishing an independent and fair process for the resolution of any disputes concerning the terms of a franchise agreement itself or the relationship between the parties.

Specifically, Franchisors and Franchisees should agree in good faith to participate in an informal, in-person meeting between the authorized representatives of the parties to resolve a dispute.

If the informal meeting is unsuccessful, the parties should agree to participate in non-binding mediation before a mediator who is neutral and mutually acceptable to the parties, including a mediator associated with the National Franchise Mediation Program.

If the mediation is unsuccessful, the dispute should not be submitted to binding arbitration unless and until all parties agree to do so, including mutually agreeing on the arbitrator who will hear the dispute, the location of the arbitration proceedings, and the corresponding rules and procedures for the arbitration.

Before all parties agree to arbitration, Franchisors must provide Franchisees written information that clearly advises the Franchisee it is relinquishing its right to a jury trial.

Absent an agreement by the Franchisor and Franchisee to use binding arbitration to resolve their dispute, any party should be entitled to pursue its claims against another party in a court of law. There should be no waiver of the right to a jury trial by any party. There also should be no caps or limits on the amount of damages that a party can seek or recover against another party, including a cap or limit on the amount of punitive damages that can be recovered against a party as allowed by law.

VENUE AND CHOICE-OF-LAW CLAUSES



In the event a dispute between a Franchisor and Franchisee has not been resolved by participating in an informal, in-person meeting with authorized representatives from the parties or by participating in mediation proceedings, the party pursuing its claims in a court of law should do so in the county and state in which the subject Facility is located.

Further, any lawsuit or claims should be governed by the laws of the county or state in which the lawsuit or claims are filed.

A Confession of Judgment clause should not be a part of any franchise agreement or corresponding contract, rider, attachment, or promissory note carried by the Franchisor.

FRANCHISE SALES ETHICS AND PRACTICES, PROPER DISCLOSURES



Franchisors should mandate fair and honest selling practices among their salespersons and agents.

Franchisors should use their best efforts to identify whether any of their sales agents or any persons acting on behalf of the Franchisors made any oral or written representations or promises to any Franchisee applicants or reached any agreements with any Franchisee applicants that are not contained in the required Federal Trade Commission's Franchise Disclosure Document ("FDD").

Franchisors should include contractual provisions in their franchise agreements that grant a Franchisee all rights, title, and interest in its own guest lists and in all related information for guests that have stayed at the Franchisee's particular facility, which survives the termination of the franchise agreement.

Franchisors should not use any database developed from one hotel brand to market or sell their other hotel brands to the detriment of the Franchisees.

Franchisors and their salespersons and agents should not engage in the practice of "churning" properties, i.e., seeking the early termination of an older hotel on the basis of low-quality assurance (QA) inspection scores or otherwise so the Franchisor can then seek and approve an application for the conversion of a newer hotel or the construction of a new hotel with a particular brand name in the same geographic region or area of protection (AOP) as the older hotel for which the Franchisor is seeking an early termination.

FRANCHISE SALES ETHICS AND PRACTICES, PROPER DISCLOSURES



Commentary

It is an unfortunate situation in franchising that many first-time or “rookie” Franchisee applicants do not fully understand that the salespersons or agents of the Franchisors may make oral representations or promises about the Facility, the franchise system, the franchise agreement, or the License that are not included in the FDD, and that such promises could be FTC Franchise Rule violations.

Regrettably, because these first-time Franchisee applicants trust and believe that the Franchisor’s salespersons or agents will honor their oral representations and promises, the applicants do not carefully read the lengthy and sometimes complex FDDs and franchise agreements to determine whether such representations and promises have been included in their own agreements.

In the interest of fair franchising, prior to the execution of the franchise agreement, a Franchisor should ask a Franchisee applicant to prepare a written document that identifies any oral or written representations or promises made by, or agreements reached with, the Franchisor, its sales agents, or any persons acting on behalf of the Franchisor, and that are not contained in the franchise agreement. This written document should be attached as an addendum or exhibit to the franchise agreement.

If the Franchisee applicant does not identify any such representations, promises, or agreements, the Franchisor should ask the applicant to carefully review and initial the paragraphs in the franchise agreement that explicitly state that (1) neither the Franchisor nor any person acting on its behalf has made any representations or promises on which the applicant Franchisee is relying that are not written in the agreement; and (2) the agreement, together with the exhibits and schedules attached, is the entire agreement superseding all previous oral and written representations, agreements, and understandings of the parties about the Facility, the franchise system, the franchise agreement, and the License.

TRANSFERABILITY



In situations in which a Franchisee seeks to transfer its property to an unrelated third party, the Franchisor should not delay, withhold its consent, or impose conditions on the transfer in an unreasonable, arbitrary, or capricious manner.

Transfer fees should be fair and reasonable (i.e., generally no more than \$1,500) and based solely on the estimated administrative costs to process the transfer.

Upon submission by the Franchisee to transfer the franchise, the Franchisor shall provide, in writing, the Franchisor's then-existing standards for the approval of a new or renewing Franchisee. The Franchisor, after receiving all required documentation for the transfer, shall, within a reasonable amount of time, approve or disapprove the transfer. If the Franchisor disapproves of the transfer, a written statement is required outlining the reasons for disapproval.

There should be no fees for a Franchisee's transfer to a spouse, child, parent, sibling, niece, nephew, descendant, spouse's descendant, or other family member if the transferee is legally competent to assume the Franchisee's obligations under the franchise agreement.

There also should be no transfer fees for a Franchisee's buyout of other shareholders or partners who had an interest in the Facility or for the addition of any shareholders or partners who will gain an interest in the Facility.

TRANSFERABILITY



Continued...

In the event of a requested transfer, Franchisors should not condition the granting of the request on a requirement that the Franchisee or new owner adopt an extensive renovation or modernization plan for the subject property. Any required renovations for the subject property in connection with a transfer should be limited to only those specific items identified in the past two (2) quality assurance (QA) inspection reports for the subject Facility that were issued prior to the requested transfer.

To the extent a Franchisor approves a requested transfer, the Franchisor should not seek liquidated damages (LDs) from the prior Franchisee or seek any increased fees from the new Franchisee owner of the subject Facility because the Franchisee sought to transfer its Facility prior to the scheduled termination date of its franchise agreement.

Within ten (10) days of the completion of an approved transfer of a subject Facility, Franchisors should automatically release the prior Franchisee from any and all obligations it had under the terminated franchise agreement and provide it with a written letter of release.

SALE OF THE FRANCHISE SYSTEM HOTEL BRAND(S)



If a Franchisor sells one or more of its various hotel brands to another entity, the Franchisor should promptly give notice of the sale to its existing Franchisees and pledge to work with them and the new Franchisor owner to ensure the transition is as smooth as possible.

To the extent possible, the prior Franchisor owner also should continue to honor its guest loyalty or rewards programs for the guests who stayed at the hotels it is selling to the new Franchisor owner. Alternatively, the prior Franchisor owner selling the hotels should transfer the points or rewards earned by such guests to another existing guest loyalty program of the prior Franchisor owner or a new program it establishes for the benefit of such guests.

The new Franchisor owner who purchased the hotel brand should similarly strive to ensure that the transition is a smooth one. Among other things, the new Franchisor owner should work closely with the existing Franchisee Association or Franchise Advisory Councils (FACs) for the hotel brand, or, if circumstances warrant, a newly created FAC to address all issues involving its purchase and ownership of the hotel brand. The new Franchisor owner should maintain the same or a higher level of quality and performance for the hotel brand as the prior Franchisor owner. If the new Franchisor fails to operate the hotel brand at the same or a higher quality level, the Franchisee shall have the right to exit the franchise system at no cost.

To the extent a new Franchisor owner desires to change any system requirements for the hotel brand, it should work closely with the FACs, Franchisee Associations, and the Franchisees themselves before implementing any such changes and offer to pay or reimburse the Franchisees for the costs of making such changes. The new Franchisor owner should also honor the guest loyalty or rewards programs for the guests who stayed at the hotels it's purchasing. Alternatively, the new Franchisor owner should transfer the points or rewards earned by such guests to another existing guest loyalty program of the new Franchisor owner or a new program it establishes for the benefit of such guests.



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