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Anatomy of a UFOC

One of the most important decisions for a hotel owner is selecting a franchise affiliation. It costs hundreds of thousands of dollars to acquire and maintain a franchise over its 10- to 20-year term, but the franchise affiliation should generate even more money in new business through a reservation system, brand awareness and other benefits.

Unlike many business transactions, franchising is highly regulated, and franchisors must fully disclose all elements involving the contemplated franchise relationship. The document containing all this important information is called a Uniform Franchise Offering Circular (UFOC). Before you are allowed to sign a franchise agreement, you must be given ample time (10 days) to review the content of the UFOC. Most hotel UFOCs are highly detailed and fairly lengthy, but written in easy-to-understand language describing the franchisor's history and business dealings as well as the benefits and obligations involved with the franchise relationship.

A typical UFOC contains the following important disclosures:

• **Company history, identity and business experience of management.** Look for experience in areas such as marketing, sales, reservation technology and hotel operations. Beware of companies top-heavy with executives who are merely franchise salespeople.

• **Franchisor's litigation history.** How many and what types of lawsuits against the franchisor are outstanding? While litigation does not necessarily indicate wrongdoing, it does represent some level of dissatisfaction with the franchisor. Carefully evaluate the type of pending litigation and whether recurring disputes suggest internal problems.

• **Estimate of all fees and expenses of entering into and maintaining the franchise.** Most hotel franchisors levy an acquisition fee, plus ongoing fees and expenses during the term of the franchise, including royalty, accounting and auditing, advertising, expansion, transfer and training fees. The total can be substantial. The UFOC will also describe the fee to terminate a franchise early, a cost known as a "liquidated damage clause."

• **Franchisor obligations.** Obviously a franchise relationship is a two-way street. The franchisee must pay franchise fees and the franchisor must provide certain services. The UFOC contains a list of franchisor services, such as reservations, marketing and advertising, design plans and specifications, site selection assistance and so on.

Two other items not normally found in a UFOC, but critical to selecting an appropriate franchise, are the franchisor's policies on exclusive territories and impact. Some progressive franchisors solve this potential conflict up front by negotiating an exclusive territory with the franchisee before the franchise commences. Other franchisors use third-party impact studies to quantify the effect of the new competition on the existing franchisee. The latter solution is highly subjective and sometimes unreliable.

In today's competitive hotel market, a strong franchise affiliation has become key to success. Hotel owners need to adopt a "buyer beware" attitude and perform the necessary due diligence on the prospective franchisor before signing any agreements. LH

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