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FRANCHISING, MANAGEMENT CONTRACTS, AND SIMILAR

RELATIONSHIPS WITHIN THE HOTEL AND CATERING INDUSTRY

A thesis submitted by

Janet Housden

in fulfillment of the requirements

for the award of the degree of Master of Philosophy,

in the Department of Hotel, Catering and Tourism Management,

University of Surrey

1978
PREFACE

Grateful acknowledgement is made to British Vending Industries who provided financial support for this study, and to Professor S. Medlik who, as research supervisor, contributed advice and encouragement throughout. Thanks are also due to Philip Nailon, Reader in Management Studies, who provided constructive criticism in the final stages, to Alison Hepworth, who typed the manuscript, and to my husband and children who showed great forbearance during the preparation of this thesis.

Janet Housden
University of Surrey
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May 1978
SYNOPSIS

This thesis examines four types of contractual arrangements within the hotel and catering industry: franchising, hotel management contracts, catering contracts, and tied house tenancies. It aims to portray the operating and financial characteristics of such arrangements and their participants, to indicate their significance, to assess their functional value as methods of marketing, financing, management and purchasing, and to suggest the probable development of franchising in the provision of hotel, catering and related services and the consequent implications.

Chapter one details objectives, scope and methodology. Selected literature is critically reviewed in chapter two. Detailed definitions of the arrangements are provided in chapter three and distinguished from other similar relationships. Chapter four is devoted to a survey of the historical background and reasons for growth of the arrangements, including (where applicable) the American as well as the British background.

A profile of those involved in the four types of relationship, a detailed analysis of terms governing them, and an assessment of the extent to which obligations are performed and rights enforced are based on empirical findings and included in chapters five, six, seven and eight which relate respectively to catering contracts, hotel management contracts, the tied house system and franchising. In chapter nine an assessment and comparison is made of external and internal factors influencing the arrangements and an analysis is made of the dynamics of each relationship.

The advantages and disadvantages of franchising to the franchisor, franchisee, consumer and national economy are assessed in chapter ten, and recommendations made for the optimal organization of franchise schemes. Chapter eleven explores the applicability of franchising in the light of social and economic trends. Its probable development within sectors of the hotel and catering industry and implications for those in the industry, its suppliers and consumers are suggested in chapter twelve.
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CHAPTER 1

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1.1 REASONS FOR THE STUDY

This study, one of several undertaken within the Department of Hotel, Catering and Tourism Management (1) during the last ten years, was sponsored by British Vending Industries, an important supplier to the hotel and catering industry. A choice of three subjects was offered for the BVI Research Fellowship, being of mutual interest to the hotel and catering industry, the Department and the sponsor. That on 'Franchising' was selected by this researcher and subsequently extended to include a wider context of other, similar contractual relationships within the hotel and catering industry.

The need for an empirical study on this subject was perceived to be threefold. Firstly, a survey of literature on franchising, management contracts and similar business arrangements indicated a dearth of information on the subject, particularly in relation to the British environment, both in respect of general commercial activity and specifically as regards the hotel and catering industry.

Secondly, two of the four types of contractual relationship examined in this study (that is, catering contracts and the tied house system) are already in wide use in two major sectors of the British hotel and catering industry. Thus an assessment of the characteristics and of the dynamics of these two relationships is thought to be of interest and value to both current and potential participants, both inside and outside the hotel and catering industry.

Thirdly, the other two types of contractual relationship studied (franchising and management contracts) have considerable growth potential within certain sectors of the industry, although they are not yet widely used in this country. A better understanding of the purpose and dynamics of these two relationships, and their functional and economic significance and value, is considered to be an important aid towards the improvement of existing relationships and should be of benefit in predicting future trends within the industry.
1.2 OBJECTIVES OF THE STUDY

Six main objectives were determined:

(1) To identify the distinguishing characteristics of a franchise, hotel management contract and other similar business relationships.

(2) To examine the characteristics of the two parties involved in such arrangements, the operating and financial characteristics of their units, and to assess the current significance of such arrangements.

(3) To analyse the contractual and financial terms governing the two parties and to assess the performance of such terms by each party.

(4) To consider and compare the development, role, operation and dynamics of the arrangements, as methods of marketing, financing, management and purchasing.

(5) To assess the functional value of franchising and its economic significance, and to indicate in the light of current economic and social trends, its probable growth and development in the provision of hotel, catering and related services.

(6) To suggest the consequent implications of (5) for the hotel and catering industry, its suppliers and consumers.

1.3 SCOPE OF THE STUDY

1.3.1 Conceptual Dimension

This study is concerned with contractual business arrangements (but not involving agency or partnership in the legal sense), made between two distinct parties where there is a separation of ownership or other legal title to the premises or of the registered user rights to a product or service, from the actual management and operation of such premises, product or service.

The research focusses on such arrangements wherein there is an active and significant contribution to the business by both parties on a continuous basis. In arrangements where one party is actively engaged in a managerial and operational capacity and the other party has a passive role (eg. as a provider of finance and/or owner of the premises), the study
includes only such arrangements in which the active party comes within the sectoral scope of the research, and in which the passive party participates to a significant extent in the financial trading outcome of the venture and in the monitoring of the business. Hence arrangements are excluded which involve, for example, the letting of premises to a tenant, or conceding of rights to operate in a particular location, or the allocation of a licence to use a specific formula, unless the passive party has an additional significant financial interest and involvement in monitoring the activity.

1.32 Sectoral Dimension

For the purposes of this study, the hotel and catering industry is defined as including those commercial units in which the main business activity is the provision of accommodation and/or food and drink for consumption on the premises. Hence the context of the research is based on the classifications of the industry as determined by the Standard Industrial Classification, and includes hotels and other residential establishments, restaurants, cafes and snack bars, public houses, clubs and catering contractors (2).

In addition commercial units engaged in the preparation and/or service of food for consumption off the premises (i.e. 'take-away' outlets), are included within the survey. Reasons for their inclusion hinge on the significance of such outlets, (both in their own right and in their effect upon other catering units), their identification as part of the catering industry (by the general public and by the industry itself (3)), and the practical consideration that in some instances it is impossible to classify an establishment as predominantly selling either 'on' or 'off' the premises.
This study aims to explore the internal and external functional characteristics of such contractual relationships and the effects of such functions: internal as regards the parties to such relationships, and external as regards other participants in the same system, field of activity or economic sector of which the arrangement is part.

Thus the research focusses on the role and significance of the contractual arrangements as channels through which the functional activities of marketing, financing and purchasing, as well as those of management and operation may be achieved. An examination is made of the allocation of such functions between the two parties to each arrangement and of the effects upon them of such allocation, and also of the wider effects of such functions upon system members and those indirectly involved with the contractual arrangement. In addition an assessment is made of the effect of franchising upon the consumer and upon the wider economic environment.

To provide information on these internal and external functions, the study includes a brief survey of the historical development of the four contractual arrangements, examines the characteristics of the two main parties to each type of arrangement, analyses the contractual and financial terms governing them and examines the relationship between them over a period of time.

The research is focussed on Great Britain, and includes contractual arrangements operational in this country between both British and foreign-based parties (including those in an active, operational capacity and those in a passive role as client-owners). In addition the contractual arrangements entered into by some
British companies, in respect of units located overseas, are included where deemed appropriate (such being indicated in the text).

Although the study is centred on the British situation, the predominance of foreign (particularly American) literature on some aspects of the research, together with the increasing multi-national involvement in certain contractual arrangements within Britain and of the expansion of British interests overseas, makes it necessary that account be taken of international business and economic factors, in order to make comparisons and to predict future trends.

1.35 Summary of Scope of Research

This study is thus concerned with those contractual arrangements within the British hotel and catering industry, in which there is a separation of ownership from management and operation. Table 1.1 lists the sectors of the industry included within this research and summarizes the type of contractual arrangement (with which this study is concerned) found to exist in such sectors. Four similar types of contractual arrangement exist within the industry: franchising, hotel management contracts, the tied house system and catering contracts. No indication was found of relevant contractual arrangements existing within the club sector (5). These four types of relationship are considered separately in the context of the particular type of arrangement rather than of sectoral activity; for example franchising within hotels, restaurants and 'take-away' outlets is considered as one topic; hotel management contracts is another.

1.4 METHODOLOGY

Two main methods were used for this study: desk research and personal interviews. Each contributed to the two basic requirements of (1) establishing a body of knowledge on the subject of the research, and (2) identifying the prevalence of, and participants in those contractual arrangements within the survey which were not necessarily readily recognized as such (i.e. franchising and hotel management contracts).
Table 1.1  Summary of Occurrence within all Sectors of the Hotel and Catering Industry of those Contractual Arrangements with which the study is concerned

<table>
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<th>SIC definition</th>
<th>Relevant Contractual Arrangement</th>
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<tr>
<td>Hotels and other residential: 884</td>
<td>Hotels, motels, holiday camps, guest houses, boarding houses, hostels and similar establishments providing furnished accommodation with food and service for reward but excluding licensed or residential clubs.</td>
<td>franchising</td>
</tr>
<tr>
<td>Restaurants, cafes, snack bars: 885</td>
<td>All establishments supplying food for consumption on the premises to the general public, to which the supply of alcoholic liquor, if any, is ancillary. Included are restaurants, cafes, snack bars, milk bars, coffee bars, refreshment rooms, tea rooms, tea shops, function rooms as separate establishments, fish and chip shops and ice cream parlours.</td>
<td>franchising.</td>
</tr>
<tr>
<td>Public houses: 886</td>
<td>Establishments wholly or mainly engaged in supplying alcoholic liquor to the general public for consumption on the premises, to which the supply of food, if any, is ancillary. Included are public houses, beer houses and other similar establishments licensed for the sale of alcoholic liquor.</td>
<td>tied house system</td>
</tr>
<tr>
<td>Clubs: 887</td>
<td>Establishments providing food and drink to members and their guests including residential clubs. Sports clubs and gaming clubs are separately classified.</td>
<td>none identified</td>
</tr>
<tr>
<td>Catering contractors: 888</td>
<td>School canteens and industrial canteens and other catering establishments operated by catering contractors. Canteens run by industrial establishments for their own employees are classified with the main establishment.</td>
<td>catering contracts</td>
</tr>
<tr>
<td>Take-away outlets</td>
<td>No SIC definition. Defined for the purpose of this research as retail outlets in which there is an element of food processing (i.e. preparation and/or service). The sale of food is primarily for consumption off the premises.</td>
<td>franchising</td>
</tr>
</tbody>
</table>

Key:

* i.e. currently of significance within sector or perceived to be of potential future significance.

** some catering contracts were found to relate to situations in which accommodation as well as food and drink were supplied, e.g. in oil rig catering or labour camps. As such contracts were held by catering contractors they are included within that sector.
1.41 Desk Research

An initial survey was made of literature relevant to the original focus of the research: franchising in catering. This covered books, periodicals, and newspapers including those aimed at a general, trade, or subject readership, and of theses, official publications, and (where available) of privately-circulated documents (6). Subsequent upon the extension of the field of research, a further survey was conducted in relation to the other three contractual arrangements, and a continuous survey was maintained throughout the research programme over certain periodicals (7).

Whilst this literature search was of great benefit in establishing the current published body of knowledge on the subject of the research, two deficiencies were evident. Owing to the North American origin of much of the literature, and to the paucity of information on certain aspects of the research, there was a necessity for primary data to be obtained in respect of the British situation as well as in respect of those aspects which had not been previously examined. In addition, the published literature did not provide a comprehensive picture of the extent of, and parties to franchising and hotel management contracts.

In order to remedy the latter defect, two approaches were used. Written enquiries were made directly to some thirty prominent companies with hotel and restaurant interests whose involvement in franchising or hotel managements was uncertain. Owing to the reluctance of some hotel companies to respond, a further request was subsequently made to some of the companies who were initially approached and to additional companies with hotel interests, for copies of their previous three years' annual reports and accounts, in an endeavour to find out whether they were involved in management contracts (8). The other method used to detect the existence of such contractual arrangements was by contacting those who were thought likely to be aware of participants in franchising and management contracts. Enquiries were made to a number of informed individuals within the industry, including executives of operating companies, consultants, and those likely to have been involved in a professional capacity with the establishment of management contracts (9). Letters were sent to 30 heads of
catering colleges requesting their help in the identification of local or national franchisors.

To remedy the general lack of information relating to the British situation, contact was made with professional bodies, trade associations, government departments, other educational establishments (in which similar research or studies were being undertaken), and consultants or commentators with a knowledge of such contractual relationships.

In order to remedy the dearth of primary data, a decision was made to conduct personal interviews with a sample of participants in each of the four types of arrangement including representatives of both parties to the arrangement (10). Questionnaires were prepared as aids to semi-structured interviews (11). An attempt was made to compile dossiers on respondents, using references gleaned during the literature survey, information produced by the company itself (such as company accounts and promotional material), and other sources of financial data.

1.42 Personal interviews

Personal interviews were conducted with a total of some 200 respondents. The interviews were of two main types: those aiming at an overview of, or relating to a specific aspect of contractual arrangements, and those relating to the particular arrangement with which the respondent was involved.

The first type of interview was carried out mainly in the early stages of the research, with informed individuals within or closely associated with the hotel and catering industry (including figures in the industry, colleagues within the Department and the sponsors of the research).

The second type of interview was conducted over a period of nine months. These interviews were grouped (wherever possible) according to the type of arrangement and role of participants within such arrangements. Thus, for example, interviews with catering contractors were arranged for one particular period in the research programme, followed at a later state by interviews with their clients; those with franchisors were grouped separately, and were followed by interviews with franchisees.
By this means, greater attention could be focussed on each type of arrangement, and subsequent interviews with the second parties to the contractual relationship could be based on, or relate both to the particular responses of the relevant first party, and to the general response of all such parties. (Thus, for example, having interviewed executives from the sample of brewery companies, discussions with tied house tenants were based on or related to their own brewer's response as well as the generalized response from all the brewers interviewed).

As an aid to a more detailed knowledge of the contractual terms governing each particular arrangement, and thus to an assessment of the generally prevailing terms, a request was made during interviews with contractors, brewers and franchisors for a copy of their standard contract, and for any other relevant material (12). These documents were subjected to detailed analysis and the information used directly as a basis for discussion with the appropriate clients, tied-house tenants and franchisees, and subsequently as material contributing to this thesis.
An initial literature survey was carried out for a three-fold purpose: to provide background and specific information on the four major sectors within the study, to establish a basis on which the current research could be formulated, and to obtain an indication of those areas deserving more exhaustive treatment.

As the research was devoted to certain contractual arrangements within the British hotel and catering industry, attention was initially paid to such literature as originated in Britain, or related to the British situation. However, it soon became apparent that such publications were very few in relation to franchising and hotel management contracts, and that the literature on catering contracts and the tied house system within the brewing industry tended not to be related to those particular aspects which were central to this research.

The extensive American literature on franchising was then reviewed, and reference is made in the main body of the text and in the bibliography to many such publications. These tended to relate specifically to the American experience of that phenomenon, and varied widely in content and presentation from being explanations of the subject in a popular style, aimed at novice prospective participants, to more profound academic studies and theories on particular aspects of franchising. Such British literature as had been published on franchising was almost all of the former variety.

The topic of hotel management contracts, being a relatively new phenomenon even in the U.S.A., has not received comprehensive literary coverage in that country, and no publications on the subject were found to originate in Britain. What American literature there was tended to be of an explanatory nature and centred on the American experience.

Thus the extent of background and more specific information from publications varied with each of the four sectors.
Unfortunately three works that would have been most useful as a basis on which to formulate this research did not become available until this study was more than half completed (1). However, using the abundant literature on franchising as a guide to the many areas which required initial study in the British situation and further theoretical assessment in a more general context, a research proposal was formulated, and questionnaires designed to elicit information from franchisors and franchisees. Following discussion and further reading on the other three sectors within the research, adaptations and modifications were then made in order to align the research and questionnaires to particular aspects warranting further investigation within those other contractual arrangements.

The following books, reports and articles have been selected from amongst the large number of publications listed in the bibliography, on the basis: (1) that they provided particularly relevant information and/or were of use in formulating an approach to this study, or (2) that they were unique in their field or were widely regarded as being essential reading amongst student of the particular subject with which they dealt.

Curry J.A.H. (editor)
Partners for Profit: A Study of Franchising
This book, published by the American Management Association, was originally prepared as a research report for Harvard University Graduate School of Business Administration. It was based upon in-depth interviews with fifty franchisors and franchisees, completed questionnaires from franchisors (2), and a study of current literature. The purpose of the study was to analyse factors relevant to franchising and to describe the essential elements of the franchise arrangement including the continuing relationship between the two parties. Perhaps because it is the work of eight co-authors, this book is variable in content and presentation.

The first half of the book provides a perceptive and thought-provoking analysis of the dynamic relationship between franchisor and franchisees, which emphasizes the changing aspirations, needs, behaviour and strengths of the two main parties. Suggestions are made, in the light of such changes, for optimal methods and actions on the part of the franchisors to prevent or redress conflict of interests and to counteract negative attitudes and influences which might affect the success of the relationship.
Useful observations are made on the implications of different product-service mixes and the consequent required variation in quality control upon the franchise relationship and upon the needs of each party. Likewise, there is an interesting description of various methods of remuneration to the franchisor and of their effect upon franchisee motivation. The formal and implied obligations and responsibilities of each party, and the parallel elements of control and management services, are considered in relation to their effect upon the actions and status of the parties.

The final six chapters of the book which deal with broader issues including external influences on franchising and the role and future developments of both domestic and international franchising are given somewhat superficial treatment. Suggestions that are made for the improvement of the image of franchising and for the extension of communal services to franchisors appear to be impractical and optimistic. Because this book is a relatively early publication in the recent history of franchising, the authors do not deal with certain aspects which have later proved to be of fundamental significance. For example, the trend towards repurchase by franchisors of franchised outlets (being a manifestation of changed franchisor policy) is hardly mentioned; and the lack of any discussion upon the effect of multiple franchisees in relation to both the franchisor and other franchisees, is another serious omission.

However, Curry and his co-authors suggest a number of propositions which merit further consideration, and which have been used in the formulation of the attitudinal parts of this research.


This book was the first British publication devoted to the subject of franchising, and is presented as a simple guide, written from a legal viewpoint but in easily comprehensible style, with a readership of potential franchisors and franchisees very much in mind.
Mendelsohn defines and explains the concept, its advantages and disadvantages to the two main parties to the arrangement, suggests essential steps for setting up a franchise, and lists questions which should be put by prospective franchisees to their potential franchisors prior to entering into an agreement. One chapter is devoted to describing the types of franchise contract and the normal clauses therein, and another to examples of four British franchises together with promotional literature contributed by the four franchisors. The book ends with an assessment of the future of franchising in the U.K., and advice to foreign companies likely to enter the U.K. market through such a method.

For the purposes of this research, Mendelsohn's book provides general background reading of the explanatory type, rather than of the profound academic variety. Intended as a guide to novices, that is what it is, and it brings nothing new to the general body of knowledge on the subject; except in so far as it is in a British publication, aimed at the British reader and more particularly at the potential British franchisor and franchisee. As such it is of special interest and rarity.


This report is one of a series on marketing research and is aimed at actual and prospective managers of franchising systems. It was based on information obtained through a combination of personal interviews with, and questionnaires completed by over 220 franchisors and some 500 franchisees, together with responses from government officials, lawyers, economists etc. with particular interest in the subject. Approximately one-third of franchisors whose responses were included in the tabled data were fast food franchisors.
The report centres on managerial and organizational issues rather than on economic ones, and is a useful combination of explanatory text with substantiating tabled data plus a number of more profound observations on the nature of franchising and its actual and potential problems. A balanced picture is provided of the advantages and disadvantages of franchising to the two main parties, and particular emphasis is placed on the obligations and responsibilities of franchisors. Several chapters are devoted to detailed descriptions of services expected of the franchisor and to an outline of a number of problems encountered by franchisees.

The two chapters on 'Franchising and the Public Interest' and 'Trends in Franchising' are somewhat narrow. The former centres on fraudulent or ill-advised practices and schemes, and points to likely legal, administrative or accounting remedies. No attempt is made to assess the advantages of franchising in a free market economy, either in respect of entrepreneurs, the consumer or the general public interest. The latter chapter lacks depth, merely summarizing the more obvious factors.

However, the Conference Board report provides useful information from a wide and statistically valid survey (though now a little out of date) together with some useful pointers to further study.

Ozanne, Urban and Hunt, Shelby D., Economic Effects of Franchising, U.S. Senate, Select Committee on Small Business, September 1971, Bib.ref.(159).

This study, funded by the American Small Business Administration, was focussed on three areas of business activity: fast food, convenience grocery and laundry/dry cleaning. Its purpose was five-fold: to assess the economic effects of franchising in those three sectors; to provide a franchisee profile; to establish operating characteristics of franchise systems; to consider the role of minority groups in franchising; and to explore the nature of the relationship between franchisors and franchisees.
The authors based their findings on responses from 146 franchisors and 986 franchisees (being a response rate, respectively, of some 18% and 25% of a randomly selected sample). In addition they analysed some 150 franchise contracts and interviewed a number of specialists and others with an interest in, and knowledge of franchising.

This report is of considerable interest, mainly because of its combined economic and managerial focus, but also because it is based on a large response from both franchisors and franchisees. The section on fast food provides the major focus of the study, and contains extensive data on the overall dimensions of franchising, on demographic and financial operating features of franchisees, and on the power relationship between the two main parties.

Two basic findings of the study were concerned with the general and specific potentialities of franchising. First, Ozanne and Hunt seriously question the previously-held belief (based on widely-disseminated research findings) that franchising significantly reduces the possibility of business failure. Secondly, they point to the practice common amongst a large number of fast food franchisors of misleading potential franchisees as to the expected profitability of franchised units.

Ozanne and Hunt also produce conflicting evidence in connection with the role of franchisors and its effect upon franchisees' profitability. Two hypotheses were tested concerning the relationship of franchisor controls (or the degree of independence experienced by franchisees) and the financial success of franchisees, based upon responses by franchisees as to their perceived freedom. No statistically significant relationship was found to exist, except in respect of perceived franchisor control over the menu of fast food franchisees, which appeared to render such businesses more profitable.

The authors also explore the quality of assistance in eleven areas of managerial activity provided to franchisees by franchisors, as perceived by the former. They conclude that there was a statistically significant relationship between high quality control and franchisee financial success in all areas except the provision of supplies by the franchisor.
In a previously reviewed article, Curry and his co-authors demonstrate that franchisor control and franchisor assistance were two sides of the same coin; the difference being mainly the manner in which either function was administered and/or received. Despite this, plus the fact that seven areas of control assessed by Ozanne and Hunt coincide with four of the eleven areas of franchisor assistance which they considered, they came to two different conclusions in respect of the resultant contributions to franchisee profitability.

This would seem to add emphasis to a query about the validity of using franchisees' subjective assessment of their freedom from restrictions and about the quality of franchisor assistance, rather than an objective evaluation of these elements (though, admittedly, this would be more difficult to obtain). Franchisees' assessments may well have been influenced by their unrelated financial results, and thus their judgement of the issues under consideration and the effects attributed to such factors, may be erroneous.

Overall, however, this is a study of considerable value to those with a serious interest in franchising. Later publications by the same authors include a number of articles on specific aspects of franchising which use various sets of data from this study as a basis for their theories and assessments of the phenomenon.

Thompson, Donald N. *Franchise Operations and Antitrust*, Lexington, Massachusetts, D. C. Heath, 1971, Bib. ref (198).

Franchise Operations and Antitrust is a scholarly assessment of franchising primarily from an economic viewpoint, in relation to issues of public policy. Although it is based on the situation in the U.S.A. and concentrates on American legal case history and regulatory attitudes to franchising in that country, it is nevertheless a book of considerable interest to any serious student of franchising, and the economic analysis of the contribution of franchising within a free market economy is of relevance to the British situation.
Professor Thompson points to a wide variation in legal decisions in respect of franchising, and suggests that its essential values have not been recognized. He attempts to distinguish these values and to analyze and evaluate the various controls inherent in franchising from the standpoint of franchisors, franchisees and public policy. He draws on the findings of three previous studies (3) to determine the extent of contractual restrictions common in franchise agreements, to describe the nature and extent of franchisor controls, to assess the degree of conflict or cooperation within the franchised marketing channel and to evaluate the extent of channel dominance by franchisors.

A comprehensive summary is provided of franchise legislation and regulation in respect of the main areas of control imposed by franchisors on franchisees. This is followed by a discussion of business justifications commonly given by franchisors for such restrictions, and a rigorous economic analysis of the functions and effects of a number of such controls. Professor Thompson provides theoretical backing to the proposition that many such controls do have a sound business purpose, and that most contribute towards a procompetitive marketing environment. His suggested criteria for determining antitrust (or monopolistic) issues, which he terms a concept of 'least necessary restraint', are specifically intended as guidance for American legal practitioners and legislators. However, they are also of significance in a more global business context as measures by which an assessment can be made as to whether franchisors have overstepped acceptable limits in imposing restrictions on franchisees.

Professor Thompson points to the likelihood that unless there is greater understanding of franchising and more discrimination in the enforcement of antitrust law, this method of business may well give way to ownership integration, thus hindering the growth and development of the small business sector of the economy.
IzraeI, Dov Franchising and the Total Distribution System, 

This book is of considerable interest as one of the very few British 
publications dealing with this subject, and particularly as an auth­ 
oritative, theoretical assessment of the phenomenon, both as it occurs 
in the U.S.A. and in Britain, and of its future possibilities in this 
country.

However, the title of this book is somewhat misleading in that it 
suggests that franchising is the focal issue of the work, whereas the 
central theme is the author's suggested organizational model for an 
integrated distribution system, centred on the grocery trade. Fran­ 
chising is suggested as an effective method and aid towards imple­ 
menting his model, and thus the emphasis is placed upon franchising 
as a contributory element, rather than as a business system in its 
own right.

Dr. IzraeI devotes about one third of his book to a description and 
careful analysis of franchising and of its environment including soc­ 
ial, economic and legal factors, mainly in the U.S. context, but also 
including one chapter on franchising in Britain. He distinguishes 
two main types of franchising: 1st generation and 2nd generation; the 
former being exemplified by the tied-house system (as a form of dis­ 
tribution supplementary to an existing method); and the latter occur­ 
ing where franchising is used as a method specifically to initiate 
a distribution system. He further categorizes three types of 'fran­ 
chise package' depending upon comprehensiveness, each of which he 
suggests may be suitable for different circumstances. IzraeI ana­ 
lyses and suggests improvements upon six main elements of franchise 
contracts which govern the relationship within each franchise system.

In the final part of the book, IzraeI proposes a theory of task­ 
environment, which is the amount of authority required by different 
participants in an organization to deal with particular tasks in each 
sub-environment. He also outlines a range of integrative devices 
which he relates to the degree of interdependence of one task with
another. It is a pity that the author did not proceed to formulate a model relating these theories to the structure of an optimum franchise organization and to the maximisation of successful initial and continuing relationships between the main parties within the franchise system. However, his ideas (which he uses to produce a model or organisational structure for a distribution system encompassing different channel levels and institutions) suggest avenues for future research into franchising. His book, backed by his wide experience and academic standing, has also been of particular use to this researcher in relating the American experience to the British situation, and on making predictions as to the future of franchising in this country.


This book is one of the most up-to-date publications on franchising dealing comprehensively with the subject as a whole. Written by the Head of the Center for Study on Franchise Distribution at Boston College, it draws mainly on material put to seven annual conferences held at the college from 1965 to 1971 (the proceedings of five such conferences subsequently being published in full). Dr. Vaughn also refers to his own research through telephone interviews with 116 fast food franchisors, and to other surveys and research carried out in the U.S.A. and to publications and articles on franchising in general.

Some of the research to which he refers was based on responses from and studies of franchisees, but the book reflects an imbalance in that much appears to be based on the views of a substantial number of protagonist franchisors and specialists attending the Boston conferences. Only one reference is made to literature specifically representing the franchisee viewpoint.

Much of the content, though providing an interesting overview of the subject for prospective franchisors, franchisees or those from other disciplines, is somewhat superficial. Despite the fact that the author is an academic and well-known source, it lacks appropriate reference to theoretical or empirical studies. Some of the advice
and assessment contained in such chapters as those dealing with estab-
lishing a franchise system, raising finance for franchisors and
franchisees and on the 'real estate program' could equally apply to
business in general and not specifically to franchising. Likewise,
some of the content in the sections on recruitment, selection and
training of franchisees is relative to employees rather than franchi-
sees in particular, and does not provide specific insight into fran-
chising per se.

However, chapters concerning the advantages and disadvantages of fran-
chising to the two main parties, and on the relationship between fran-
chisors and franchisees, and that dealing with international franchi-
sing, are of more particular value and include a number of interest-
ing observations and propositions, which unfortunately are not fol-
lowed through by Dr. Vaughn.

U.S. Dept. of Commerce Franchising in the Economy: 1975 - 1977,
December 1976, Bib. ref. (209).

This is a report of the sixth annual survey into franchising conduc-
ted by the Bureau of Domestic Commerce. It is based on all known
franchisors in the U.S.A. and summarizes responses from 1,115 fran-
chisors representing an estimated 99 per cent of franchised units
and sales.

A comprehensive macro-picture is provided of the sales, number of
outlets, number of employees and ratio of franchisor-owned:franchised
units. Statistics are also included of terminated franchise systems,
intra-system change of ownership (company-owned to franchised and
vice versa), and mergers. A comprehensive micro-picture is also
given of major business sectors, including fast food restaurants and
hotels and motels, with data showing the size by turnover, number of
units, sales by franchisors to franchisees, distribution by size of
groups and by major activity (eg. predominant menu in the case of
restaurants).

Additional information is given which indicates the growth and trends
within the above-mentioned sectors as well as in relation to franchi-
sing generally, including sections on legal and regulatory trends and
on international franchising by American companies.
Although the report relates entirely to U.S. companies and is centred on the American domestic situation, it is of interest as indicating the size, growth and trends of franchising and hence is valuable as an indicator of the possible future status of franchising in this country. As such it has been of use in this research.

Oxenfeldt, Alfred and Kelly, Anthony,

Hunt, Shelby D,

Parker, Lawrence L.,

These three articles are reviewed together because the last two are based on the former, and all three reach a similar conclusion though by a different approach.

Oxenfeldt and Kelly propound the hypothesis based on theoretical analysis that a combination of push-pull forces affect franchisors and franchisees at both an initial and later stage in their respective life-cycles, which makes inevitable a trend towards full company ownership and operation of franchised units within successful franchise systems.

They explore the changing goals, opportunities, capabilities and problems of the two parties over a time span and suggest a number of different combinations of factors rendering more or less likely the probability on the part of each party to buy or sell a franchised unit. From this a matrix is constructed to depict the likelihood of a consensus of action (to buy or sell), and the relative bargaining positions of the two parties.

The authors point to the difficulty of generalizing in vacuo without specific circumstances of each case, and also stress that the very short history of franchising, together with its rapid growth, makes impossible a long-term assessment of the viability of the franchising
method. Nevertheless they suggest that their hypothesis has substance, although this does not imply that franchising has no future role; merely a different role from that generally ascribed to it.

Hunt supports the theory of Oxenfeldt and Kelly and suggests that the results of fieldwork (published in Economic Effects of Franchising (4)) provide practical evidence of this. He states that between 1968 and 1971 there was a disproportionate increase in the percentage of company-operated : total system units amongst larger and/or older franchise systems. However, he notes that the main source of expansion in company-operated units was through newly constructed units, and that the net re-purchase of franchised units accounted for only 30% of the increase in company-operated units.

He points to the improbability of former franchise systems becoming wholly-owned and operated chains, but suggests a continuing upward trend in the ratio of company-operated units, because of greater profitability to franchisors, more flexibility and control and elimination of actual or potential legal costs and problems. He quotes from the study that according to franchisors, the ideal proportion of company-operated units is 42 per cent whilst the current actual proportion in 1971 is 11.3 per cent. Hunt proposes that the use of franchising as a medium-term vehicle for expansion (rather than a long-term business method) is not undesirable in the public interest, provided that franchisees are treated fairly by franchisors.

Parker similarly supports Oxenfeldt and Kelly but does so from a theoretical analysis of franchising in its context of a vertically integrated marketing channel, whose characteristics he compares with those of a business enterprise in an open system. He suggests that in order to survive, a franchisor must interact successfully with the environment, and this, he maintains, can be achieved with certainty only through complete control of all distribution outlets, that is by corporate ownership and operation.

Parker describes the changing goals of both franchisors and franchisees as the relationship matures, and suggests that the length of life of every franchise system is dependent upon the achievement of a desired level of market penetration by the franchisor, after which corporate ownership of outlets will ensue.
He points to inadequacies in franchisee recruitment literature and advertisements put out by franchisors, which ignore the essential or normal characteristics of franchising. Thus he maintains, franchisees' expectations are raised and no hint is given of performance restrictions, power differentials, areas of conflict or a probable life-cycle of the enterprise. He suggests that a more equitable arrangement would arise were franchisors to divulge long-term policies during initial negotiations.


Departmental Committee on Liquor Licensing, Report by the Rt.Hon. Lord Erroll of Hale (Chairman), H.M.S.O., Cmnd 5154, Dec 1972, Bib. ref. (51).

Departmental Committee on Scottish Licensing Law, Report by Dr. Christopher Clayson (Chairman), H.M.S.O., Cmnd 5354, Aug 1973.

Taken together, these four government reports provide a wealth of data on the brewing industry and licensing systems in England, Wales and Scotland. Though none specifically centres on the relationship between brewers and tied trade tenants, information of varying relevance to this aspect is contained in each report, particularly within that of the Monopolies Commission.

The 1966 National Board for Prices and Incomes Report examines the structure of the brewing industry and analyses the financial performance of the breweries. In the course of its enquiries the NBPI considers the tied house system, and in particular comments on the disadvantages resulting from the dual method used by breweries for obtaining remuneration from their tenants.
Resulting from recommendations in the previous report, the Monopolies Commission was asked to examine whether the existing system of supply of beer for retail sale in licensed premises in the United Kingdom was for or against the public interest. As an integral part of the established channels of supply, the tied house system is thus examined in considerable detail. The report assesses the existing extent of restrictive trading practices including the tie on sources and on choice of supplies exercised over tenants by their breweries, and the stipulated wholesale prices and restrictions on retail prices imposed by the latter. Whilst this section of the report is of direct relevance to this study, its primary purpose is to consider the implications of the brewer:tenant relationship for wholesalers of liquor products, for consumers and for the general public interest, rather than assessing the internal business relationship between brewers and tenants, or the advantages and disadvantages accruing to either party. No profile of tenants is given, although one section is devoted to reporting the attitudes of tenants towards the terms of their agreements, including their anxieties over various financial and operating obligations, and lack of security of tenure.

The Monopolies Commission in concluding that the disadvantages of the tied house system outweigh the advantages, and in recommending that the licensing system should be modified, led to the initiation of two enquiries and reports by Departmental Committees, otherwise known as the Erroll report (in respect of England and Wales) and the Clayson report (in respect of Scotland).

These reports are both wide-ranging, taking into account the legislative environment, patterns of consumer demand, social factors and public issues, and the interactions between these factors and existing or potential liquor licensing legislation. The Erroll report specifically excludes from its brief a re-assessment of the tied house system, other than in respect of its specifically social implications (which are relatively few). The Clayson report only briefly touches upon it, tied houses being far less frequent in the Scottish pattern of retail trade. Apart from the valuable background infor-
mation for this study provided by both reports, they are of consider-
able direct significance. Were the recommendations of the Erroll
report for changes in the licensing laws to be implemented, there
would be resultant alterations to the tied house system and to the
position of tenants. The Clayson report has led to the enactment
of the Licensing (Scotland) Act 1976, which is likely to cause chan-
ges to the position of tenants in that country.

In total these reports provide an authoritative picture of the
brewing industry which is useful both as a basis for assessing chan-
ges within the industry during the intervening years since the pub-
lication of the reports and as a guide to future developments.

Hawkins, Kevin, Brewer-licensee relations: A case study in the

This is a brief article which reviews the forces that have led
to a change in the relationship between brewers and their licen-
sees (including both tenants and licensed house managers) and out-
lines changes taking place in the organization of collective bargain-
ing structures within the brewing industry. The former concept of
'co-partnership' between brewers and tenants is seen to be challen-
ged, although Hawkins points to the adaptation made by some major
brewers in accepting a new negotiating role by tenants, and in
adopting changed policies towards them, as evidence of a new and
more realistic relationship between the two parties.

Hawkins article is of direct relevance to this research in its con-
text of examining brewer:tenant relationships and is of benefit in
being a relatively recent publication. A brief summary is provided
of economic factors affecting the relationship, together with exam-
ples of three 'package deals' negotiated between major brewers and
their tenants. Reference is made to a small study undertaken at Bradford University in 1968/69 on the attitude of publicans to their jobs. This included responses from 40 tenants and 10 public house managers, mostly licensees of one brewery in the Bradford area. Hawkins suggests that a number of problems are revealed by the findings, not specifically relating to the brewer:tenant relationship, but in a more general context with regard to motivation, expectation and job content, which could affect that relationship.

Because of its brevity and focus on collective bargaining, this article ignores operational aspects of the tied house system and only briefly touches upon behavioural characteristics of tenants and upon the franchise contract or legal instrument governing the relationship.

Koudra, M., Industrial and Welfare Catering Services in Britain: 1970 - 1980, M.Phil thesis, University of Surrey, 1974; Bib.ref. (114), see also refs. (112) and (113).

This thesis is one of the few publications on this subject and provides an opportunity to gain a comprehensive picture of the economic aspects of the industrial and welfare catering sector. It centres on employee feeding services but also includes all the sub-sectors within the field, and distinguishes between modes of operation, i.e. direct management or catering contractors. Conceived as an economic study, it was not designed primarily to assess the relationships between parties to contractual arrangements, nor to determine the advantages and disadvantages accruing from such arrangements to contractors, client-owners or consumers.

However, in his chapter on catering contractors, and elsewhere in the text where an assessment is made of catering contracts versus direct management, and of the penetration achieved by catering contractors, Koudra describes the perceived advantages to clients of employing catering contractors, touches upon attitudes adopted by various parties involved in such arrangements, and thus introduces the subject which is of most relevance to this researcher. Unfortunately his
treatment of this particular aspect is somewhat perfunctory and pro-
vides neither detailed information of specific relevance nor suggests
particular avenues for further investigation. In total, the chapter
on catering contractors does provide some useful general information,
although the section on historical background is weak, and despite
a detailed analysis of the four major contractors, certain omissions
occur.

Eyster, James Jeffries, The Negotiation and Administration of Hotel
Management Contracts, Cornell University, 1977; Bib. ref. (65).

This study is a rare academic treatment of one aspect of what is a
relatively new phenomenon in the U.S.A. (and elsewhere) and as such
makes a valuable contribution to the existing body of knowledge on
this subject. It is a concise and well-written study, based on inter-
views in the U.S.A. with some forty contractors and approximately
three hundred clients (i.e., hotel and motor inn owners) and focusses
on problems occurring within the relationship between contractors
and clients.

Eyster assesses the contributions usually made to the relationship
by each party and identifies the economic and business factors which
have caused or permitted the growth of such contractual arrangements.
He develops a model of the bargaining strength continuum of both par-
ties, reflecting their status and need for one another, influenced
by internal and external factors including the period in which each
arrangement was initiated.

He suggests that the relative bargaining strengths of the two parties
affect the preliminary negotiations and subsequent relationship, by
influencing the contractual terms of the hotel management contract
and subsequent adherence or non-adherence to such terms. Through a
detailed analysis of 39 management contacts, he ascertains the fre-
quency of various contractual provisions and gives a ranked assess-
ment of the degree of concern expressed by both parties over the
major provisions. He then proposes a model to demonstrate the normal
pattern of escalation of such concern and the consequent effect upon
the relationship.
A third model (or series of models) is proposed of the tri-partite working relationship and division of responsibilities between the hotel management contractor head office, the hotel general manager and the owners, and of the effects of shifts in the balance of power and responsibilities upon that relationship. Eyster suggests that the rapid development and lack of general experience of the management contract institution, or of the proper evaluation of the arrangement, have caused many of the problems. He further proposes that these have been exacerbated by general economic factors of the recent recession. He points to a trend towards more equitable division between the two parties of operating and financial responsibilities, and suggests other future changes within the relationship and within the structure of the management contract sector of the hotel industry.

Unfortunately the publication of this work was too late to influence the formulation of this researcher's studies on hotel management contracts, but it provides a valuable additional insight into the expectations and inter-actions of the parties involved in such arrangements and gives supportive data to that which had been accumulated by this researcher.

As Eyster focusses on the problems encountered, he does not make any attempt to assess the advantages of the system, either as it affects the two (or three) main parties, or in the more general context of its benefits (or otherwise) to the hotel industry or to the consumer or the national economy.
CHAPTER 3

DESCRIPTION AND DEFINITION OF FRANCHISING

MANAGEMENT CONTRACTS AND SIMILAR CONTRACTUAL RELATIONSHIPS

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3.2 DEFINITION OF FRANCHISING

3.21 From Quoted Sources

3.22 Working Definition for Thesis

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3.1 DISTRIBUTION SYSTEMS
Goods and services may be distributed through a variety of different channels ranging from free, independent channel members (comprising manufacturer or provider, wholesaler and retailer) to totally integrated, wholly-owned chains encompassing successive stages of production, distribution and retailing (1). Mid-way between these two extremes are contractually integrated systems whose members are controlled to a varying extent by contractual arrangements. There is a wide spectrum of relationships within such arrangements, including distributorships, voluntary trading groups, concessions, management contracts and franchises.

In order to clarify the distinctions between the various types of contractually-integrated systems, this chapter is concerned first with defining franchising and management contracts, and then with delineating other similar arrangements.

3.2 DEFINITIONS OF FRANCHISING
3.21 From Quoted Sources
A very general definition is given in an early American study: "In modern commercial usage a franchise is a right to do or use something which is granted by one party (the franchisor) to another party (the franchisee) for a consideration " (2).

Another definition is given below (3) which broadens the concept by including the essential particularity of the goods or services and the restrictions imposed within the franchise on their distribution. It introduces the proposition that branding is nearly always implicit in franchising, but ignores the issue of whether payment for the franchise rights is essential.
"Franchising is a contractual bond of interest in which an organisation, the franchisor, which has developed a pattern or formula for the manufacture and/or sale of a product or service, extends to other firms, the franchisees, the right to carry on the business, subject to a number of restrictions and controls. In almost all the cases of significance, the franchisee operates using the franchisor's name as a trade name."

The definition below of franchising, used by the U.S. Department of Commerce introduces but does not define the term 'licensing' to describe the arrangement. One particular restriction on distribution is mentioned as well as the reiteration of the essentiality of distribution control and branding (4). "Franchising is the form of licensing by which the owner (the franchiser (sic)) of a product, service or method obtains distribution at the retail level through affiliated dealers (the franchisees). The holder of the right is often given exclusive access to a defined geographical area. The product, method or service being marketed is identified by a brand name and the franchiser maintains control over the marketing methods employed."

The widely-used definition of the U.S. International Franchise Association (5) given below, highlights the necessary continuing input by the franchisor to the franchisee, and proposes a requirement for investment by the franchisee (although whether such investment be personal labour or capital is not stated). The issue of payment for the franchise is ignored, and the legal rights of both parties are not stated. Some form of branding is thought to be essential.

"A franchise operation is a contractual relationship between the franchisor and franchisee in which the franchisor offers or is obligated (sic) to maintain a continuing interest in the business of the franchisee in such areas as knowhow and training; wherein the franchisee operates under a common trade name, format and/or procedure, owned or controlled by the franchisor, and in which the franchisee has or will make a substantial investment in his business from his own resources."
In order to cover the various aspects of franchising, a number of longer definitions have been proposed. One such (6), given below, sets franchising in its context as a method of distribution, touches on the legal relationship and contract, and introduces the concept of mutual co-operation and interdependence of both parties. It mentions restrictions on distribution (and on the time-span of the relationship) and states that branding is an essential constituent of franchising. A new concept is introduced in that the author attempts to distinguish a franchised business from other similar contractual arrangements, by suggesting that a franchised business should be a separate business entity, usually requiring the total business involvement of the franchisee. In this it is pointing to the separation of franchising from, for example, a distributorship of a single product line.

1. The relationship between the two parties is contractual, and an instrument of agreement, confirming the rights and responsibilities of each party, is in force for a specified period of time.

2. The continuing relation has as its purpose the efficient distribution of a product or service - or an entire business concept - within a particular market area (7).

3. Both parties contribute resources towards the establishment and maintenance of the franchise. In the case of the franchisor, its contribution may be a trademark, a company reputation, products, procedures, manpower, equipment, a process etc. The franchisee usually contributes operating capital as well as the managerial and operational resources required for the initiation and continuation of the local franchised business.

4. The contract between the parties outlines and describes the specific marketing practices to be followed and details the contribution of each party to the operation of the business. It also sets forth certain standards of operating procedure to which both parties agree to conform.
5. The establishment of the franchised business creates a business entity which will, in most cases, require and support the full-time business activity of the franchisee.

6. Both the franchisee and franchiser (sic) participate in a common public identity. This identity is achieved most often through the use of common trade names or trademarks and is frequently reinforced through advertising programs designed to promote the recognition and acceptance of these within the franchisees market area."

In an addendum to this definition, the author suggests that payment by the franchisee (either as an initial sum and/or as a royalty) is not essential to a franchise; he draws attention to the practice by many franchisors of deriving their sole income from the franchisee from the supply of goods to him.

The only definition of franchising produced by a British source (8) is written from a legal standpoint, and thus places emphasis on the legal standing and restrictions placed on both parties, including matters of ownership and payment. The author proposes that substantial capital investment and ownership of the business by the franchisee are essential to a franchise. Franchising is not placed within a distributional context in this definition, and the operating relationship of the two parties is barely mentioned.

The author differentiates between a 'pure franchise' and other franchises, as being one which not only permits rights to a trademark or invention but also includes a blueprint for the total, successful operation of a franchised unit i.e. a total business package. A 'pure business' franchise is thus defined as having the following necessary requirements:

"1. Ownership by a franchisor of a name/idea/secret process/piece of equipment.

2. Grant of a license or franchise by franchisor to franchisee permitting the exploitation of such name, idea, process or equipment = modus operandi.

3. Existence of a contract between the parties, including regulations relating to the operation of the franchised business.

4. Initial and continuing support by the franchisor with regard to expertise in the operation of the franchised business."
5. payment by the franchisee of a royalty or other consideration for the rights that are obtained.
6. substantial capital investment by the franchisee from his own resources, and ownership of his own business."

In another British publication (9), an American definition of franchising is taken and used as being the best available, having a broad scope but yet being the most detailed and precise (10).

"1. (The term) franchise shall mean a contract or agreement, either expressed or implied, whether oral or written, between two or more persons;
2. Wherein one person, hereinafter called the franchisee is granted the right to offer, sell and distribute goods or services manufactured, processed, distributed or (in the case of services) organized and directed by the other person, hereinafter called the franchisor;
3. Wherein the franchisee as an independent business constitutes a component of a franchisor's distribution system;
4. Wherein the operation of a franchisee's business franchise is substantially associated with advertising or other commercial symbol designating the franchisor; and
5. Wherein the operation of the franchisee's business franchise is substantially reliant on the franchisor for the continued supply of goods or services."

Whilst admirable in its succinctness this definition does not include the issue of payment for the franchise rights or capital involvement by the franchisee, and does not specifically point to the interdependence of both parties.

Two further definitions are worthy of brief mention for the specific points they make. In the first, attention is drawn to the independent financial status of the franchisee, and his consequent right or liability to retain all profits or sustain all losses (11).

"Franchising is a system for the selective distribution of goods and/or services under a brand name through outlets owned by independent businessmen called 'franchisees'. Although the franchisor supplies the franchisee with know-how and brand identification on a continuing basis, the franchisee enjoys the right to profit and runs the risk of loss. The franchisor controls the distribution
of his goods and/or services through a contract which regulates the activities of the franchisee, in order to achieve standardisation."

In one other definition (12), or rather in the addendum to the definition, quoted below, the proposition is made that central to franchising is the creation of franchised units for the express distribution of the franchised product; thus separating franchising from such contractual arrangements as single product distributorships or concessions. Whilst narrowing the extent of franchising in this way, the definition is expressly expanded to include such integrated trading arrangements as voluntary trading groups. The legal independence and economic dependence of the franchised units is stressed.

"An integrated and organised adaptive distribution system composed of marketing, production and/or research units, established and administered by a franchisor (or a group of franchisees in the role of a franchisor) as a medium for expanding and controlling the exclusive distribution of a good or service."

He adds:

"1. Units are legally independent, but economically dependent.
2. There must be a formal franchise agreement which identifies and establishes a continuing relationship.
3. The franchisee operates his business with the advantages of the name and standardisation of the franchisor.
4. The 'exclusive distribution' refers to the total and express purpose for which the franchised unit was created."

From the original, general definition of franchising the subsequently quoted seven definitions have approached the concept of franchising from different standpoints, and have included various important specific aspects. None has included economic, legal, financial and operational aspects within one definition whilst placing franchising within the general context of distribution and at the same time encompassing the specific relationship between the two parties.
3.22 Franchising: Working Definition Formulated for the Study

The following definition is suggested as a synthesis of the main points, which it is hoped is sufficiently brief for general use and readily comprehensible.

A franchise is a contractual business relationship between two separate parties, exclusively formed for the distribution of goods and/or services through selected outlets for a specific or indefinite period of time. It is based upon an agreement wherein, for a consideration, one party (the franchisor) grants to another party (the franchisee) the right to use the franchisor's commercial methods of operation, and to sell and distribute goods (and/or services) which are supplied (or organised) by the franchisor, and which are identified by a brand name or trademark. Both parties are financially and economically inter-dependent, though legally and financially independent business units. Essential to a franchise is the initial and continuing contribution by both parties including, from the franchisor, expertise in business organisation, particularly in marketing, and/or the supply of goods; and from the franchisee, operational management and capital. Mutual control over operating procedures and products to protect the brand name is necessary.

The essential features of a franchise can thus be listed:

Summary of Essential Features of a Franchise

Economic:

1. a system of distribution for goods and/or services;
2. established for exclusive and selective distribution (i.e. set up essentially to provide new outlets for franchised goods/services in selected areas);
3. entailing control on products and/or operating procedures;
4. resulting in economic interdependence of two parties;
Legal:
5. a contract between two separate legal entities;
6. based upon an express or implied, verbal or written agreement;
7. concerning the extension of rights from the owner of a product/method of doing business to a separate party;

Financial:
8. involving two parties of independent financial status;
9. requiring capital contribution by the franchisee for the franchised unit;
10. including the payment of a consideration by the franchisee (either in the form of initial franchise fee and/or continuing royalty and/or premium on goods and/or services supplied);
11. retaining each party's right to financial independence of the separate business units;
12. whilst creating a degree of financial inter-dependence in trading results;

Operational:
13. necessitating an initial and continuing contribution by the franchisor (either in the planning and organisation of the franchise, or in the supply of equipment, goods or services);
14. requiring an initial and continuing contribution by the franchisee (in labour, and supervision of the franchised unit);
15. including mutual control over the products and operating procedures of the franchised units.

3.3 DEFINITIONS OF HOTEL MANAGEMENT CONTRACTS AND CATERING CONTRACTS

3.31 External Sources of Definitions

Byster, J.J. suggests (13) that a management contract is:
"A written agreement between an hotel-motor inn owner and an operator in which the owner employs the operator as an agent (employee) to assume full operational responsibility for the property and to manage the property in a professional manner. As an agent the operator pays in the name of the owner all property operating expenses from the cash flow generated from operations, retains its management fees, and remits the remain-
ing cash flow, if any, to the owner. The owner provides the hotel-motor inn property to include land, building furniture, fixtures, equipment and working capital and assumes full legal and financial responsibility for the project”.

He commences the definition by putting the contract in the context of the legal instrument governing the relationship rather than as a description of the relationship itself. He touches briefly on the legal and operational responsibility of the two parties and describes more fully the financial contribution and method of financial management of the system.

3.32 Hotel Management Contract: Working Definition
An hotel management contract is a contractual arrangement between two separate parties, formed for the provision of organizational and operational expertise in the planning, production and sale of goods and services such as accommodation, food and beverages and other ancillary hotel services. It is based on a legal instrument wherein one party (the client-owner of the property or principal) agrees to engage the services of another party (the hotel management contractor or agent) for a specific period of time at an agreed remuneration. Incumbent upon the client-owner is the provision of capital, the sustaining of all or a substantial proportion of financial loss and the total or major participation in any profits. Operational responsibility devolves upon the contractor, and frequently includes branding the hotel with the contractor's tradename or trademark.

3.33 Catering Contract: Working Definition
A catering contract is a contractual arrangement between two separate parties, formed for the provision of organizational and operational expertise in the planning, production and sale of catering and ancillary goods and services. It is based upon a contract (whether written or verbal) wherein one party (the client-owner of the facilities) agrees to engage the services of another party (the catering contractor) for a specific or indefinite period of time at an agreed remuneration. Incumbent upon the client-owner is the provision of capital for the building and fixed equipment, and the underwriting of any such subsidy as is agreed between the two parties as being necessary
for the provision of the agreed services. The contractor
normally provides the capital for, and retains ownership of,
certain items (such as light equipment and fixtures, fittings
and furnishings), and is responsible for the operation of the
services.

3.4 DEFINITIONS OF TIED-HOUSE SYSTEM

3.41 External Sources of Definition
The Brewers Almanack (14)(the official handbook of the Brewers
Society), contains a description of the historical basis and
current working of the tied house system but no definition
suitable for use in this study. The four government reports
on the brewing industry similarly contain no definitions (15).

3.42 Tied-house System : Working Definition
The tied-house system is a method of distribution for beer and
other alcoholic or ancillary products and services through
tied outlets (i.e. on and off-licensed premises)(16). It encom-
passes a contractual arrangement between two financially and
legally independent parties - the brewery company and the tenant.
They are governed by a tenancy agreement wherein the brewery
company, as landlord, agrees to let specified licensed premises
to a tenant for a specified number of years at an agreed rent
and, the tenant agrees to purchase from the brewery company,
as supplier and/or wholesaler, all or specified liquor and
other supplies, at prices to be set by the brewer. Apart from the
major contribution of the premises and supplies the brewery
company provides operating guidance and (depending upon the
company) branding of individual and/or the total product. The
tenant provides a small capital contribution together with his
own or hired labour. Mutual control over the product and
premises is necessary to protect the liquor license and the
reputation of both parties, and the two parties are economically
and financially inter-dependent.
3.5 DESCRIPTION OF SIMILAR CONTRACTUAL ARRANGEMENTS AND TERMS
In order to define even more precisely the exact nature of franchising, hotel management and catering contracts and tied-trade tenancies, it is necessary to describe other, similar contractual arrangements, thus pointing to the differences. This procedure is particularly necessary because of the profusion of terms applied to commonly encountered business arrangements and to the frequent mis-use of such terms; such a situation being confusing and misleading, not only to the general public but also to practitioners and commentators (17).

3.51 License
A licensing agreement has been defined as "one which confers on the licensee and persons authorized by him, the right to manufacture, sell or otherwise make use of something which is exclusively the property of the licensor" (18). It is most frequently used in connection with the conferment of rights of a patent or trademark, although sometimes used synonymously with franchising (19). The difference between franchising and licensing hinges on the fact that a licensing agreement does not necessarily involve a close and continuous liaison between the two parties, and that a licensor seldom seeks or achieves the degree of operational control over the licensee as a franchisor attains over a franchisee (20). Thus the term 'licensing' could be applied to a franchising situation in which there is minimal back-up and operational control by the franchisor over the franchisee.

However, the definition of franchising proposed earlier (21), includes reference to the "initial and continuing contribution by the franchisor in the provision of business expertise, and the mutual control over procedures and products." Therefore, the term franchising as used throughout this study is distinct from the usually understood meaning of licensing. The 'initial contribution in business organization by the franchisor' refers to the provision of an entire business concept and a unique brand identification (corresponding to Mendelsohn's 'pure business franchise'). (22), and is therefore at the other end of the spectrum from a license issued for eg. the right to use a specific chemical formula.
Brief mention should be made of the terms 'Inward Licensing' and 'Outward Licensing'. The former is an arrangement to obtain expertise in setting up new ventures for expansion or diversification, and therefore approximates to the action taken by a franchisee. The latter is a method of selling permission, rights or assistance to manufacture or sell products, and is therefore similar to the role of the franchisor. Whether these terms relate to a licensing or franchising arrangement depends upon the degree of initial and continuing involvement of the licensor/franchisor.

The term 'license' is not only used in the above context of conferring the right to manufacture or sell a certain product or use a certain system, but in general commercial usage also refers to the right given to another party to operate a business on certain premises or within a prescribed area. In this context, 'license' and 'concession' become interchangeable.

3.52 Concession

The term 'concession' is normal commercial usage refers to two arrangements. The first occurs when one party offers the right to another party to produce and sell goods and/or services within a prescribed area. Thus the term 'concession' is used in regard to catering rights at a theatre, public park, motorway service area or airport; or in respect of the right to provide television and broadcasting services within a specific region. Both the terms 'franchise' and 'license' are frequently used in this context.

In order to distinguish catering concessions from hotel management or catering contracts, a closer analysis must be made of the contractual terms of such arrangements. Catering concessions commonly include a variety of arrangements which range from the concessionnaire being merely a tenant paying a fixed rent for the privilege of operating in the premises, to the concessionnaire being paid by the owner for his services. In between these extremes are arrangements whereby the concessionnaire pays a fee calculated as a percentage of turnover for the right to operate within premises or a prescribed area; and arrangements
whereby the concessionnaire and owner jointly participate in the trading outcome of the venture. Various degrees of owner-involvement in the policy-making and control over the business are common.

The suggested definitions of hotel management and catering (24) contracts include as essential to the concept the bearing by an owner of all or a substantial financial trading loss or agreed subsidy, and consequent freedom of the contractor, from such financial risk. Situations in which concessionnaires have liability to sustain all or a substantial proportion of a trading loss are therefore outside the definition of management contracts. Also inherent in such hotel management or catering contracts is the owner's retained right of dictating overall policy and right to monitor performance. Where arrangements for concessions transfer totally or substantially such rights to the concessionaire, these too are considered to be apart from management contracts.

The second application of the term 'concession' is commonly found in circumstances where one party grants the right to another party to act as an agent to sell a particular product. Thus 'concession' often refers to an arrangement whereby a retailer is given the right to sell a particular product or range of products. This may either involve the retailer's total trade or be a subsidiary part of it, as in the concession for a department or a single product line or range of products within a department store. Such arrangements whether relating to the total or part of a business are frequently termed franchises. There is some debate over whether they should be included within the term (25), but using the definition proposed within this study, they are excluded in those circumstances where businesses were not exclusively formed for the transaction of the 'franchised' business.
Distributorships, Authorized Dealerships, Commercial Travellers, Agents and Representatives

The terms 'distributorships' and 'authorized dealerships' are often used to denote the type of arrangement outlined above, and are therefore used synonymously with both 'concessions' and 'franchises'. There is disagreement amongst academics and observers of franchising as to where the dividing line should fall. Those arrangements which involve the total business commitment of the distributor or dealer (i.e. only one manufacturer's or supplier's product or range of products is sold), or in which the distributor or dealer operates under the brand name or trademark of the supplier, with an accompanying standardization of product and procedure, are normally included within the definition of franchising.

Statistics of franchising in the U.S.A. normally include automobile sales and petrol service stations distributors and indeed such arrangements account for some 80% of U.S. franchising turnover. However, distinction is often made between 'first generation franchising' (which includes such distributorships and dealerships) and 'second generation franchising' (which term approximates to the 'total business package' type of franchise). In this thesis, contractual arrangements are excluded if simultaneous handling occurs of several manufacturers' or suppliers' products, or if the business has not been expressly formed to sell the goods or services to which the franchise relates.

Distributors and dealers are terms which are used synonymously with commercial travellers, agents and representatives. The implied difference between the latter types and distributors and dealers, is that of mobility as against fixed premises for business transactions. However, there are a number of mobile franchises which are considered to be franchises proper, and therefore a further distinction is necessary. This centres on the legal issue of principal and agent. Whereas the commercial traveller or representative is acting in the capacity of agent for the manufacturer or supplier (and does not
have ownership of the product being handled), a franchisee is acting on his own behalf as principal and does have (temporary) ownership of the product or service that he is selling or supplying.

3.54 Pyramid/Multi-level Distributors
These terms refer to a system of distribution which involves a pyramid-like structure of distributors. The manufacturer or supplier appoints distributors to sell a given product. For this right the distributor has to purchase an agreed amount of stock and/or make a cash payment to the manufacturer/supplier. In order to sell the stock and to recoup his investment, the distributor is expected and encouraged to recruit sub-distributors, who in turn pay the distributor for the privilege of joining the distribution channel and/or buy stock from him. Thus the distributor undertakes the role of wholesaler and the process is repeated at each subsequent level, with the result that the business becomes one of selling distributorships, rather than of selling the original products. In many pyramid-sales organisations it was possible for distributors to buy their way into the distribution hierarchy by cash payments or the purchase of stock. Pyramid selling or multi-level dealing had considerable currency in the U.S.A. and in Britain in the 1960's. Many thousands of investors participated in and subsequently lost money in such schemes, many of which were at best ill-conceived and at worst organized by fraudulent operators. Widespread publicity resulted in legislation being introduced which effectively brought an end to the use of such distribution methods.

Pyramid or multi-level selling is (or was) frequently termed franchising and in the minds of many people franchising still retains similarity to if not complete identification with pyramid selling. The two methods have certain similarities in that both are methods of distribution, using contractually integrated but independent components within the distribution channel. Both methods include restricted outlets for sales of products or services under a brand name of the manufacturer or supplier. The two parties in each case are economically inter-dependent but legally and financially independent. However, there (in general terms), the similarity ends. The
essential difference between franchising and multi-level selling is that an intrinsic part of the latter method is the wholesaling roles of successive levels of distributors. In franchising there is normally no such inherent function. A second difference is in the ability of multi-level distributors to buy their way into a pyramid hierarchy. A third difference is in the degree of the continuing relationship between the two main parties. Whereas a franchise involves the initial and continuing support of the franchisor, in matters of advice and operational support as well as (in some cases) an ongoing product supply, in the case of multi-level selling, the relationship between the manufacturer/supplier and distributor (and hence down the channel between distributors) is essentially one of supplier and wholesaler. One reason for an equation of franchising and multi-level selling in the minds of some people may be because both systems incurred public outrage following the activities of certain operators with an aim for their own short-term prosperity rather than the long-term mutual benefits of both parties. Hence a number of 'franchisers' without an adequately prepared franchise scheme, and mainly concerned with eg. initial sales of equipment, were bracketed with multi-level sales organisations.

3.55 **Party Plan Selling/Home Demonstrators**

This is another method of distribution involving distributors who neither operate from fixed premises, nor sell on a 'door-to-door' basis, nor from mobile vans. Distributors or demonstrators as they are called, are selected by the manufacturer or supplier, allocated a given area, and expected to locate a continual supply of home-owners who are willing to loan their homes, on a temporary basis, for a brief demonstration of the product or product range to be sold. Such home-owners or 'hostesses' as they are sometimes called, are expected not only to provide temporary premises but also a supply of potential customers. No retailing occurs at these 'parties' or demonstrations, but orders for products are taken by the demonstrator and later executed from the demonstrator's own supply, or collected from a central depot by the demonstrator and delivered to the customers.
Though sometimes labelled as franchising, party plan selling differs in various respects. The 'franchise' in this case is similar to a license or concession to sell a product line or range of products in a given area. In some franchises, there may be reliance on a temporary site for the sale of services, in particular (36), but there is no similar role undertaken by a third party to that of the 'hostess' in party-plan selling. She provides space for the demonstration and potential customers for no payment, other than payment in kind (a free gift of the product being sold) or a discount related to the magnitude of orders placed at the 'party', applied to the order of the 'hostess'. Although there is a varying degree of back-up provided to the demonstrator, party-plan selling does not involve the 'complete business package' of a true franchise.

3.56 Rack-jobbing Distribution

This is another form of distribution which is sometimes termed a franchise. It involves the selection by a manufacturer or supplier of certain retail outlets for the sale of a single product line or range of products, usually displayed on racks or stands (hence the name). It is similar to a concession for the right to handle certain goods (37), but involves the owner of the retail outlet in the provision of working capital and the assumption of risk. When the rack or stand is installed, the owner must pay for the entire contents, and similarly must immediately pay each time the rack is restocked by the supplier.

As in multi-level selling, this method of distribution was promoted by a number of operators, many of whom were either misguided or fraudulent. The long-term financial health of the scheme was often ignored, and retailers were left, in many instances, with racks of products that were not as readily saleable as they had anticipated (38). For reasons outlined above, this method of distribution cannot be termed a true franchise.
Voluntary Chains, Co-operatives and Consortia

These are affiliations of legally and financially independent units which voluntarily join together in economic interdependence to obtain economies of scale and greater leverage in the market place. Some include various levels of vertical integration, and all are horizontally integrated. Wholesaler-sponsored voluntary chains (39) were initiated by wholesalers (particularly within the grocery trade) who were anxious to retain or promote the loyalty of retailers to one supply. Such chains may include a number of wholesalers each with an initial satellite of retailers. Retailer-sponsored voluntary chains were likewise developed within the grocery trade, but were developed through vertical backward integration by retailers with existing wholesalers, or by forming their own wholesaling organisation (40).

Marketing or purchasing consortia are similar in concept, and were initiated recently within the British hotel and catering industry, by hoteliers and caterers.

Policies vary between different voluntary chains, co-operatives and consortia as to the level of standardization required of members and the amount of adherence to group policy. There is also a difference in the comprehensiveness of group services offered; some merely making one particular service available (eg. marketing) and others providing a wide range of functions including marketing, purchasing and operational and technical advice and services.

Both wholesaler sponsored and retailer sponsored voluntary chains are frequently included within the definition and statistics of franchising (41). However, their characteristics and those of consortia vary from being very loose affiliations of non-branded members joining together for one particular function only, to those of a tightly-integrated, branded and multi-functional group, with each member's behaviour controlled by group policy. In the latter case such arrangements closely resemble a franchise operation, with members acting jointly in the capacity of franchisor, and their exact classification as to whether they are or are not franchises may determined in each particular instance by similar criteria as used in previous examples.
Co-Partnerships and Joint Ventures

These are contractual arrangements involving two parties in the joint ownership of a business unit or units and joint participation in the financial outcome of the venture. Normally, an initial financial contribution is made on an approximately equal basis by both parties, with a proportionate sharing between them of operating profits (or losses).

Such arrangements were popular (and still exist) amongst some hotel companies in the U.S.A., and currently constitute a proportion of the interests of one British hotel company.

In relation to hotel ventures, apart from the financial stake, there is a continuing contribution by each party to the arrangement: the hotel company providing initial advice, training etc. on the establishment of the hotel; the other party acting as an owner-operator to manage the venture. A fee is paid to reimburse the latter, usually based on ten per cent of the gross room revenue; and a royalty payment made to the hotel company to compensate for group expenses incurred, for example, in marketing.

Such schemes closely resemble franchising, particularly such franchise arrangements in which a substantial amount of capital is provided by the franchisor. However, the distinction between these arrangements centres on the legal and financial independence of the two parties necessary in a true franchise arrangement, which does not apply to co-partnerships because of the mutual funding and mutual sharing of profits or losses. In circumstances where a franchisor contributes financially to a franchised unit, this contribution is in the form of a loan, involving repayment from operating profit, but not a sharing of such profit (42).
3.59 Management Incentive Schemes

Management incentive schemes are financial arrangements between employers and their hired managers, involving in addition to the payment of a regular basic salary, an incentive element which is normally calculated as a percentage of operating profit.

Where such arrangements are more complicated they may closely resemble franchising. Some management incentive schemes involve the manager in the contribution of working capital to the business whilst retaining the major share of profits (or bearing of losses); some allow the manager to build equity in the business which may subsequently be realized. In circumstances where the manager is offered a license to operate the business on his own behalf for a specified term, such an arrangement has close affinity with those franchising arrangements in which the franchisor leases the premises and equipment within a franchised unit to the franchisee for a specified period. The distinction between the two arrangements is thus difficult to make, and depends on the particular terms governing each incentive scheme.
3.6 CLASSIFICATION OF FRANCHISING

Franchising may be classified by a number of different methods:
1. Inter-level relationship within the distribution channel.
2. Totality of branding.
3. Product/service or trademark.
4. First or second generation.

The various merits and demerits of such classifications may
be argued at length, but it has been considered outside the
scope of this study other than to outline these classifications
and to select those particular categories which best accord
with the type of franchises being considered within this survey.

3.61 Inter-level relationship within the distribution channel

In one of the early academic treatments of modern franchising
(43) the following classifications of franchising in the USA
were suggested: (44)

1. Manufacturer - retailer.
   (a) franchise of entire retail outlet
   (b) single department
   (c) line within a department of a particular retail outlet.
2. Manufacturer - wholesaler.
4. Wholesaler - retailer.

This classification was expanded and modified to one differenti-
tiating essentially between product/service and trademark.

3.62 Product/service or trademark (45)

<table>
<thead>
<tr>
<th>Product or service franchise system</th>
<th>Trademark Licensing franchise system</th>
</tr>
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<tbody>
<tr>
<td>1. Manufacturer - retailer systems eg. car dealers, petrol stations.</td>
<td>4. Trademark Licensor - manufacturer systems eg. fabricated textiles.</td>
</tr>
<tr>
<td>2. Manufacturer - wholesaler systems eg. carbonated beverage bottlers.</td>
<td>5. Trademark licensor association - association members eg. bread, milk, mattress industries.</td>
</tr>
<tr>
<td>3. Wholesaler - retailer systems eg. Co-op and voluntary trading groups in food, drugs, hardware stores.</td>
<td>6. Trademark Licensor - retailer systems eg. food, beverage, ice-cream, hotels, car rentals, dry cleaners etc.</td>
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</table>
3.63 Totality of Concept
An even earlier publication (46) distinguishes between (A) product franchises and (B) entire business enterprises, and pointed to the main difference between the two being that product franchisees are not identified as members of a group and do not follow standardized or prescribed methods of operation.

3.64 Channel Innovation
One (then) British-based authority (47) on franchising distinguished between what he called first and second generation franchising. In circumstances where manufacturers or suppliers were already distributing goods and services via normal channels, and then resorted to franchising as an efficient, alternative method of distribution for the same products, he termed this '1st generation' franchising. Such a classification would therefore apply to the distribution of cars to dealers, of petrol to petrol stations, of soft drinks to licensed wholesale and to the distribution of beer to tied-trade tenants. (48) When franchising was used as a distinct method of distribution for the express purpose of introducing new goods and services to the market place, he termed this '2nd generation' franchising. This last classification would be applicable to the bulk of recently initiated or 'modern' franchise systems.

A French writer (49) takes this concept one stage further by suggesting that 'true franchising' occurs when a franchised unit is initiated by a franchisor, whilst 'empirical franchising' occurs when an operating unit is acquired by a franchisor and subsequently absorbed into the franchise system.

3.65 Classification as used for this study
A definition of franchising has already been proposed which includes those franchise systems in which there exists an initial and continuing contribution by both parties. Other contractual relationships have been excluded which have not been expressly formed for the purpose of distributing the particular franchised product or service and in which the initial contribution by the franchisor is no more than the sale of basic equipment or products. Thus the focus of this study is on those systems where a total product is franchised (i.e. a total business package including a basic method of doing business plus a brand image). Such a franchise is fre-
quently referred to as 'modern franchising' and distinguished from such franchises as car distributorships and beverage bottling, in which the aspect of product distribution was more significant than the concept of the total business package.

Thus this study focusses on Hall's third category of franchising: that of service sponsor - retailer, and on Thompson's sixth category: that of trademark licensor - retailer. It coincides with Lewis and Hancock's 'entire business enterprise' and Izraeli's '2nd generation franchising' or with Mendelsohn's 'pure franchise' (50).

3.7 CATEGORIES OF FRANCHISEES, FRANCHISORS AND FRANCHISES
A number of different types of franchisees, and to a lesser extent franchisors and franchises, exist, which need to be defined in order to prevent confusion.

3.71 Single franchisees
This term is usually applicable to a private individual who has entered into an agreement with a franchisor for the operation of a single unit in a location (either specified at an exact address or within a limited geographical area). Such an individual may be trading as a sole trader, partnership or limited company, but is usually the owner-operator of the franchise. He may negotiate with the franchisor from time to time for the addition of one or more units.

For the purposes of this study the term 'single franchisee' has been taken to denote a franchisee's close involvement with his franchised units, relatively small capital worth and limited status within the franchise organization. Thus an owner of from one to five units with operational involvement in or frequent supervision of such units, has been termed a single franchisee (51). Such a franchisee has relatively low bargaining strength vis a vis the franchisor. Some authorities on franchising claim that only a single franchisee is truly representative of franchising; and that multiple franchisees should be regarded in a totally separate light (52).
3.72 Area, regional, territorial franchisees
Within this category are included franchisees who are allocated a given area by the franchisor, as opposed to the rights for one unit only. This area may vary in size from a postal district of a city (suitable for two or more franchised units), to a whole town, county, region (or state in the U.S.A.), or country (53). Such an area may be centred on marketing divisions rather than on geographical or local-government boundaries (54). The number of franchised units to be developed within the area may be specified, or this may be left to the area franchisee's own commercial judgement regarding suitable density.

Payment for such rights may be by a specific area franchise fee, or may be levied in the form of an aggregate standard payment in respect of each unit (with subsequent credit if a specified rate of opening new units is maintained).

Depending upon each agreement between franchisors and area franchisees, there are two main courses of action:

1. The area franchisee may open a number of units in his area and install his own unit managers, working for him as his own employees; or

2. He may sub-franchise in his area, with varying arrangements between the franchisor and area franchisee as to what services the latter undertakes on behalf of the former, and what payments are made for such services. The area franchisee may receive a proportion of the franchise fees or royalty. Operational responsibility for the over-seeing of the franchised unit may be placed upon the franchisor, area franchisee or divided between them. Some references in franchising literature allude to area franchisees as area franchisors, because the franchisor's responsibilities have devolved upon them; and some writers maintain that area franchisees should not be included within a definition of true franchising (55).
3.73 Multiple franchisees

Although in common use this term has not been adequately defined, for the purposes of this study, 'multiple-franchisee' primarily denotes a franchisee's relative remoteness from the operation of each franchised unit, either because of the large number of such units, or because of other significant commercial interests which do not permit extensive involvement with the franchised outlets. In addition 'multiple franchisee' denotes the capital worth and relative status of the franchisee within the franchise organisation.

Thus 'multiple franchisee' may denote a franchisee with six or more franchised units (56), whether acquired through growth over a period of time, by immediate concurrent development or by acquisition from other franchisees. It may also denote a substantial franchisee (either a company or individual with extensive business interests) with only one franchised unit. In both cases, such franchisees represent a stronger bargaining position with the franchisor, than a single franchisee with up to five franchised units.

3.74 Master franchisees

This term is not in common use, but for this study is used to indicate the status of franchisees who simultaneously hold franchise rights to more than one type of franchise. This could include interests in two separate franchise systems organized by one franchisor; or agreements with two separate franchisors (eg. two separate catering franchises, or a catering franchise together with a car rental franchise) (57). Therefore, it is possible to be a master, multiple franchisee, and indeed a master, multiple, area franchisee.

3.75 Master franchisor

Comparable to the above description, master franchisor is a term applied to franchisors who simultaneously operate two or more franchise systems. It is a situation commonly encountered in the U.S.A. as the result of planned diversification of different product ranges (eg. a hamburger franchise and a pizza franchise) or of entirely different products (eg. franchised dress shops, franchised restaurants and franchised pet shops) (58). In the latter instance, master franchisors (or multiple franchisors as they are also called) often result from mergers and
takeovers of existing franchise companies (59). A number of American conglomerates include both franchised and non-franchised interests, within a variety of different franchise systems.

3.76 **Celebrity franchisor**
This term is not of significance in Britain, but because of its widespread use in the U.S.A. should be briefly mentioned. It relates to the practice of using the name of a well-known celebrity (often a figure in sport or entertainment) in conjunction with a franchise, thus inferring the celebrity's close involvement with, and approval of the franchise. By paying the celebrity for the use of his name, the franchisor obtains a possible three-fold advantage: prospective franchisees, prospective investors in the franchisor's equity, and prospective consumers of the franchised product, all of whom may equate the glamour (and possibly the financial success) of the personality with the financial success of the franchise and glamour of consuming the product. As a number of celebrity franchises proved to be ill-conceived and based on very little other than a well-known name, they caused considerable financial loss to participants (other than the celebrities). Moves were made in the Federal Court to convert the celebrity's moral obligation to a legal one (60).

3.77 **Mobile franchises**
This is a widely used term in the U.S.A. relating to those franchises which are operated from mobile vans etc. Such franchises may be issued direct to single mobile franchisees, or to area franchisees who sub-franchise to drivers.

3.78 **Joint-Managership franchises**
This denotes an arrangement in which a franchisee is given the opportunity by a franchisor to buy an interest in a franchised business for an agreed sum for an agreed period. Thereafter he has the option to acquire a 100% holding and become a fully fledged franchisee (61).
3.79 **Lease franchises**

This term is sometimes used to describe franchises in which the franchisor owns the franchised units, but leases them to franchisees for a fixed period for an agreed rental (normally based on turnover). This rental may be the franchisor's total remuneration encompassing the normal franchise royalty or premium on goods supplied, as well as the rent payable for use of the premises. Depending on the extent of the franchisor's initial and continuing contribution to the franchised business, and whether or not other payment is made to the franchisor by the franchisee, such an arrangement could be defined as a franchise or a landlord:tenant relationship.
CHAPTER 4

AN HISTORICAL SURVEY OF FRANCHISING, MANAGEMENT
CONTRACTS AND SIMILAR RELATIONSHIPS

4.1 EARLY FRANCHISING IN ITS BROADEST TERMS

4.2 BIRTH OF FRANCHISING AS A METHOD OF DISTRIBUTION
Tied trade tenancies within the brewing industry.

4.3 TWENTIETH CENTURY ADAPTATION AND GROWTH OF FRANCHISING
IN THE USA.

4.31 Early forms of franchising in the United States of America
4.311 Automobile Dealerships
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4.1 EARLY FRANCHISING IN ITS BROADEST TERMS

In its broadest sense, franchising began in the Middle Ages, when those in powerful positions (for example, royalty or local government officials) granted to others (such as noblemen or high church dignitaries) the right to collect taxes or enforce special levies, to hold markets or fairs, or to operate ferries or perform some of the activities normally carried out by the guilds. In exchange, the franchisee customarily made a single cash payment and contributed his allegiance or continuing personal services to the franchisor (1).

However, tax reform in Britain in 1562 (2) ended the use of franchising as a means of tax collection. But as a method of granting trading or monopolistic rights, franchising was employed by royalty or legislative bodies in the seventeenth, eighteenth and nineteenth centuries. Franchisees were granted rights to specific areas for a long duration, in exchange for an initial sum and continuing obligation to the franchisor (3).

4.2 BIRTH OF FRANCHISING AS A METHOD OF DISTRIBUTION.

TIED TRADE TENANCIES WITHIN THE BREWING INDUSTRY.

The extension of the franchising concept from one of allocating specific rights to that of a means of distribution originated in the British brewing industry. The business relationship between producers (the brewers) and retailers (licensees of public houses and off-licenses (4) evolved into a system known as the tied house system, in which retailers became tied trade tenants of licensed outlets owned by the producers. This system was stimulated by external political, social and financial factors.

Between the fourteenth and nineteenth centuries there was a varying degree of latitude in respect of liquor distribution channels, which ranged from one of complete freedom to close
restriction. The political and financial expediency of successive governments, the changing moral and social standards of the population, and the rise and fall of the power of the church were all elements which influenced these changes.

The first main impetus given to the tied trade system occurred after a particularly unrestricted period of liquor distribution in the eighteenth century. Excessive drinking and immorality arising from wide-spread availability of alcohol eventually gave rise to a royal and public outcry, and successive legislation was introduced to ensure the restriction and regulation of liquor outlets (5). Those premises which retained a liquor license were consequently greatly increased in value, both in distributional and financial terms. The brewers were anxious to secure retail outlets which had suddenly been rendered scarce. At the same time, the sudden rise in capital value resulted in many premises being beyond the financial resources of prospective publicans. Greater insistence was also being made by licensing magistrates on raised standards within licensed premises.

The mutual needs of brewers and licensees resulted in the creation of the tied house system. Brewers usually bought the licensed premises outright and gave considerable credit to the publican (often in return for a mortgage) (6). Help was frequently given to the supervision of the licensed premises. In exchange the tenant agreed to sell no beer other than his own brewer's, and to make a continuing payment to the brewer.

The dimension of this first wave of brewery control of the trade was indicated in two government reports of 1817 and 1818, in which it was stated that out of 48,000 licensed alehouses in the county, 14,200 in 1816 were owned by the brewers and many more were controlled by the brewers as a result of the licensees indebtedness (7). Another source suggests that the tie to brewers related to half the licensed premises in London and a greater number in the provinces (8).
Following this period of restriction on liquor outlets, there was another period of relaxation lasting until legislation in 1869 was introduced to enforce the licensing of liquor outlets. (9). From then until the end of the nineteenth century, increasing hostility on the part of the authorities became apparent towards the licensed trade, particularly influenced by the emergence of evangelical temperance movements. This gave rise to a second and even more significant scramble by brewery companies for acquisition of licensed premises in England and Wales, in order to secure captive retail outlets and to aid publicans who were affected by rising property values and by increased police action in enforcing standards. This second wave of acquisitions meant that by the turn of the century, the large majority of the 102,000 or so onlicences in England and Wales were owned by brewers and many more licencees were tied to brewers because of indebtedness (10).

In the first three-quarters of the century the brewery industry has undergone a number of changes, notably a trend towards increased concentration and a diversification by brewery companies into other roles including manufacturers, shippers and wholesalers of wines, spirits, cider and other products. By 1967, tenancies accounted for approximately 76% of all on-licensed premises owned by breweries (11), and by 1975 these had been reduced to just under 71% (12).

A number of attitudes and customs have changed within the brewer-tenant relationship and are still altering. (13) In Scotland recent legislation is likely to cause changes to the tied house estate, whilst in England and Wales even more changes would occur within the industry and within the tied house system, if suggested legislation were implemented (14).

This method of distribution has in essence remained the same since the beginning of the nineteenth century, and can be clearly seen as the forerunner of franchising.
4.3 TWENTIETH CENTURY ADAPTATION AND GROWTH OF FRANCHISING IN THE U.S.A.

4.31 Early Forms of Franchising in the United States of America

Franchising, in its broad sense, occurred early in the development of the U.S.A., when trading or operational rights were allocated by those in authority (eg. British monarchs or Parliament) to certain individuals for the monopolistic rights to certain areas. Later in the nineteenth century the issuing of franchises for the construction and operation of railway networks, for example, played an important part in the economic expansion during the American industrial revolution (15).

However, as a method of distribution involving active participation of two parties, franchising first took root around 1863 in the post-Civil war economy. The Singer Sewing Machine company was reportedly the first company to establish a nationwide network of retail outlets, using the franchising method (16) and in 1902, the Rexall Drug and Chemical Company similarly used franchising to establish a network of drug stores throughout the country (17).

The growth of franchising (in its broad sense) in the U.S.A. can be mainly attributed, in its initial stages, to four areas of economic activity; namely (a) the selling of passenger cars or 'automobile dealerships'; (b) the selling of petrol and allied supplies to passenger cars or 'gas station dealerships'; (c) the production under license of soft drinks and minerals; and (d) the formation of voluntary trading groups contributed to the growth of franchising in grocery retailing and in other business areas.
4.3.11 Automobile Dealerships

Because of its size and economic significance, the car-manufacturing industry gave franchising a major impetus in the U.S.A. Keen to establish nationwide retail outlets for the sale of their products, automobile manufacturers used franchising as a method of growth. By creating tied units within geographically restricted areas, they increased the value of such units, ensured 'loyalty' of the dealer to his manufacturer and thereby made certain a high degree of motivation. (In order to make a living the dealer had to sell vigorously the only brand of products that he was permitted to handle). Greater market sensitivity could be achieved through such committed dealers, and thus production of cars would be better geared to demand. Reduced selling and distribution costs resulted, as did a more personalized after-sales service to customers, and a logical replacement trade-in service.

For his part, the franchised dealer benefited from insulation from intra-brand competition, and had a reliable source of supply. As investment in such dealerships was substantial, it was particularly beneficial for dealers to have the backing of the reputation and business acumen of a large and well-known manufacturer (18).

The first franchised dealership for the sale and service of cars was established in 1898 by General Motors, and was in respect of steam-driven and electric cars. By 1910 or 1911, the use of franchising as a method of distribution amongst car manufacturers was firmly established (19).

4.3.12 Gas-station Dealerships

The related commercial activity of selling petrol and other supplies for passenger cars was instrumental in popularizing a method of franchised distribution in the mid 1930s. Prior
to that period most service stations were company owned and operated. Two main reasons have been suggested for the change to franchising (or a system similar to franchising). (20) New tax legislation was enacted which discriminated against company-owned outlets, including a tax on total chain turnover and on number of outlets, plus a levy on labour costs. In addition, there was pressure from trade unions for higher salary levels for unit managers. Thus petrol distributors turned to a system of franchised distribution thereby avoiding some of the taxation, containing some of the costs and enabling quicker reaction to market pressures. Petrol dealers, in their turn, benefited from modern management techniques of petrol-producing companies (21).

4.313 Soft-drink bottlers

Companies such as Coca-Cola and Pepsi-Cola developed their chains in the early 1900s by using the franchising method from the very start. One main reason for this has been given as the need to overcome a lack of capital (22).

4.314 Voluntary Trading Groups

During the 1920s and 1930s what has been termed by at least one writer on franchising (23) as the 'first franchising boom' occurred. Voluntary trading groups were formed, primarily to counteract the increasing power of vast, growing corporate chains, but also in response to the power of manufacturers. Wholesalers encouraged independently-owned retail units to affiliate with them. Some retailers formed their own voluntary groups and vertically integrated backwards with wholesalers. These voluntary trading groups included grocery, hardware, drugstore, car parts and 'variety' store businesses.
Modern franchising, or the method of franchising variously labelled as 'total business package' franchising, 'trademark licensor-retailer' franchising or 'second generation franchising' (24) was first represented in 1919 when A and W Root Beer (a very substantial national company) opened an initial franchised unit in California. In 1927 the Howard Johnson chain of restaurants (another household name in the U.S.A.) opened its first franchised restaurant (25). (Another national chain within the hotel and catering industry - Travelodge Inc. - began a system in 1948 of co-ownership. This was similar in concept to franchising).

But it was not until the 1950s, and more particularly the 1960s that what has been termed an 'Entrepreneurial Revolution' (26) or 'Franchise Boom' (27) occurred. This phenomenon involved a very extensive range of business and commercial activities, apart from those mentioned above which predate the 'modern' definition.

Dimensions of franchising in the U.S.A.

A full listing of all business activities in which franchising is used in the U.S.A. would be very extensive indeed and outside the scope of this study. However, an indication of the range of businesses (particularly services) in which franchising is prevalent is of interest and is given below:

- Restaurants, hotels, food take-away units, car rentals, car repairs, tool and equipment rentals, cleaning and laundry services, employment agencies, business and accounting services, the installation of swimming pools, fitting of hearing aids and sale of tools (28).

Though less prevalent, franchising is still widely used in the following areas:

- Travel agencies, art galleries, youth night clubs, social introductions, nursing homes, diet programs, beauty salons and shop security and surveillance systems (29).
A number of estimates have been made of the dimensions of franchising in the U.S.A., varying according to the estimator's delineation of franchising. An early estimate in 1963 suggested that some 338,000 outlets generated approximately $59,200 million per annum, which figure represented ten per cent of gross national product and twenty-five per cent of total retail sales (30). In 1967 another study which allowed a slightly broader definition of franchising, estimated that over half a million outlets were involved, with an annual sales volume of $89,200 million (31).

Figures for 1975 and estimates for 1977 provided by the U.S. Department of Commerce (32) show that the overall number of franchised outlets (33) is now slightly less than the 1967 estimate, but that sales volume will have more than doubled in the last seven years. In 1976 sales are estimated to have increased by over sixteen per cent on 1975 sales, with a further estimated 12.5 per cent increase in 1977 over 1976. 'Modern' franchising is now increasing at a faster rate and is expected to continue to do so than 'traditional' franchising. See Table 4-1.

Whilst it is interesting to note the increase in the percentage of franchise sales on all retail sales from 25 to 31%, this statistic is misleading for not all the activities included within the franchising definition are retailing activities, eg. soft drink bottlers are wholesalers (34).

4.322 Awareness of franchising

Apart from economic indicators, a measure of the significance of franchising within the U.S.A. is the extent of attention paid to the phenomenon by government, academics and practitioners, and the understanding of the concept and practicalities of franchising by the general public.
Table 4.1
Dimensions of Franchising in U.S.A.* Estimated for 1977

Total Sales

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of franchised outlets</td>
<td>463,000</td>
</tr>
<tr>
<td>Total sales volume **</td>
<td>$239,000 million</td>
</tr>
<tr>
<td>Total employed in franchising (in 1975) ***</td>
<td>3.5 million</td>
</tr>
</tbody>
</table>

Franchise sales as % of all retail sales                                   | 31 %        |
'Modern' franchising sales as % of all franchised sales                    | 21 %        |

Fast Food Franchising

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of outlets</td>
<td>53,000</td>
</tr>
<tr>
<td>Total sales volume **</td>
<td>$16,000 million</td>
</tr>
<tr>
<td>Total employed (in 1975) ***</td>
<td>0.9 million</td>
</tr>
<tr>
<td>Number of franchisors (in 1975)</td>
<td>293</td>
</tr>
</tbody>
</table>

Hotel and motel franchising

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total number of outlets</td>
<td>6,000</td>
</tr>
<tr>
<td>Total sales volume **</td>
<td>$5,300 million</td>
</tr>
<tr>
<td>Total employed (in 1975) ***</td>
<td>.33 million</td>
</tr>
<tr>
<td>Number of franchisors ***</td>
<td>34</td>
</tr>
</tbody>
</table>

* includes outlets of franchisees and those directly-owned and operated by franchisors.

** original figures in U.S. billion (= to 1,000 UK million)

*** includes employees, and franchisees working full or part-time in their outlets.

Source: Franchising in the Economy 1975 - 77, Bib. ref. (209) from page 2 and Tables 3, 6, 51 and 57.
4.3221 Government Interest

Apart from undertaking surveys of the dimensions of franchising (35), the U.S. government has given support to research on the phenomenon (36), has sponsored extensive public hearings on it (37) and has provided funds and advice for the creation of franchised businesses through the auspices of the Small Business Administration (a government-funded agency). The SBA provides substantial sums to those establishing themselves as franchisors or franchisees, and offers information and advice on franchising through a nationwide network of bureaux (38). The U.S. government has used or endeavoured to use franchising as a means of socio-economic engineering, specifically to encourage minority group participation in business (39).

4.3222 Published material and interest shown by academics

Much journalistic and substantial academic interest has been evinced in franchising, as demonstrated by the hundreds of articles and scores of books on the subject. (40) At least one academic centre has been set up entirely for the study of franchising (41) and there are a number of University professors and postgraduates who specialize in franchising or have a substantial knowledge of it (42). The American Marketing Association and the American Management Association have sponsored research and/or conferences for the further amplification and understanding of the subject (43). At least five regularly published periodicals and two annuals devote their copy to franchising (44).

4.3223 Other Indicators

Various trade associations and pressure groups have been formed, with specific interest in franchising. Chief amongst these is the International Franchise Association – an
association of franchisors, which was formed in 1959 to promote ethical standards amongst its members, to improve the general public image of franchising, and to protect franchisors from possible restrictive legislation (45). Associations representing intra- or inter-company franchisees have also been formed (46). In addition, a specific service to franchising has developed - that of franchise brokers, whose business it is to marry franchisors with franchisees.

A number of specialists from various fields have also shown interest in franchising and have written extensively on the subject from their own particular discipline. These specialists include lawyers, accountants, economists, marketing specialists, industrial psychologists, stockbrokers and business consultants. A few politicians have been particularly active and vocal on the subject of franchising, on a continuous basis over a number of years.

4.323 Main Factors Affecting Growth

Some indications have already been given as to the reasons for growth of early franchising (in its broad sense) in the U.S.A., in respect of the particular business sectors previously mentioned. It is also appropriate to isolate factors which have led to the growth and development of 'modern' franchising, and which have affected the three main parties involved in franchising: the franchisor, the franchisee and the consumer.

4.3231 Economic background (47)

A period of dynamic economic and social change occurred in the 1960s, in which the expectations of the American consumer rose rapidly after repression during the 2nd World War, together with a general increase in disposable
income. The resultant demand for a wide range of luxury goods and services, including passenger cars, needed to be satisfied. There were a number of new techniques, new materials and new equipment (spin-offs from war-time advances in technology), which were available for adaptation to the consumer market. An increased mobility of consumers also stimulated a demand for well-known, reliable products and services in widely-dispersed locations. Thus the scene was set for widespread distribution of new branded goods and services providing customer security in many new commercial activities.

In order to respond to this new market and to gain maximum marketing coverage in advance of possible competition, producers or service-sponsors needed to develop as many units as would be economically viable with as wide a geographical coverage as possible. In addition to an initial readiness to adapt, they needed five main elements: capital, suitable locations, development management resources, unit management and operating expertise. Those most ready to adapt proved to be individuals and small companies, particularly those engaged in the service sector. The personal service and close contact between the service retailer and the customer which existed in many service activities proved a peculiarly suitable medium for the franchising method of distribution - a medium in which spectacular growth occurred in franchising.

4.3232 Capital

Despite the resources of large companies and their access to funds for development, it has been claimed that no one organisation could have raised capital equivalent to that raised by a number of large, successful franchise chains. (48) The sources of capital to franchisors were usually provided by private investors (franchisees) from their personal savings, sale or mortgage of their domestic properties and by loans from their bank managers (49). Other sources of franchisee capital such as payments made
to war veterans (GIs) and redundancy money to executives have also been suggested as stimulants to the growth of franchising (50).

Once a franchisor had established an initial successful business and commercial standing, there was a synergistic effect. Banks and loan companies were more willing to lend money to private individuals as franchisees, on the basis of the franchisor's good name, such sums being considerably in excess of what would have been released to the franchisor as an independent single party.

An important component in the availability of capital for economic expansion (in franchising as in other methods of distribution) was the American tax structure and business climate. Until recently, attractive mortgages and interest rates prevailed in the U.S.A. In addition, the Internal Revenue Codes provided particularly attractive depreciation provisions, which have allowed franchisees in many instances to write off their total investment (except land) in approximately eight to nine years (51). Such depreciation allowances have been used, also, to protect franchisees' income - both earned and unearned - from sources other than the franchised unit to which the depreciation was initially applicable.

4.3233 Locations

To have identified and arranged the purchase of suitable sites on an extensive scale would have been very demanding on the human and financial resources of even large companies. By harnessing the energy and local knowledge of prospective franchisees to search for suitable locations, franchisors benefited not only from the searchers' motivations to scan the property market but also from being offered sites already in the possession of entrepreneurs,
keen to change their outlets from their current use to being a unit within the franchisor's network. Owing to a less restrictive attitude in the U.S.A. to planning applications (than current in Britain), franchisors encountered relatively few problems from zoning or advertising restrictions.

4.3234 Development Management Resources

Particularly in the earlier years of 'modern' franchising, most franchise systems grew organically from very small beginnings. Hundreds of innovative entrepreneurs perceived market gaps and employed franchising as a method of introducing their ideas despite an increasing dominance in the market place by large organizations and a general decline of small businesses. These (initially) small entrepreneur-franchisors developed their businesses through close personal involvement and, normally, from first hand experience of operating a franchised unit. By utilizing highly motivated franchisees to oversee their own units, franchisors were able to devote more time, energy and finance to development, and less to supervision and control of existing franchised units. Franchisors were thus able to grow with fewer head office and regional resources than non-franchised systems.

4.3235 Unit Management

As a wave of franchising gathered pace, and the method was proclaimed as the answer to an American's dream (of the small man 'making good' and succeeding financially in the face of big business) and as the last bastion of private enterprise, there was no lack of prospective franchisees (52). Many thousands of entrepreneurial Americans threw caution to the winds and joined a mid-twentieth century scramble equivalent to that of the 1849 gold rush. Thus the problem of attracting unit management for fast-developing
and widespread chains was resolved by an abundance of prospective owner-managers in the first instance, many of whom later recruited their own unit management for further expansion within the franchise. Franchising was seen to be the ideal vehicle for entrepreneurs (or more properly semi-entrepreneurs) to set up in business under the umbrella of a franchisor, whilst retaining a perceived independence.

4.3236 Operating Expertise

As mentioned above, franchisors normally had accrued operating experience and expertise from close involvement with their prototype units. An important factor in the growth and appeal of franchising has been the ability exhibited by franchisors to break down the component skills and information required for successful operation of their franchised units, and to offer such skills and information to those with usually minimal or no previous experience or knowledge of such a business. Hence franchising has been particularly predominant in commercial areas in which only basic skills were necessary, or in which a narrow range of specialist skills could be acquired with reasonable ease and speed. This is demonstrated by the dramatic growth of franchise systems within the fast food restaurant sector, in which the standardization of menus and of operating procedures coincided with a shortage of skilled labour, rising operating costs and consumer preference for speciality restaurants and ethnic food.

4.3237 Legal constraints

There was almost no legal restraint over franchising during the initial stages of growth. Because of this, and due to the unwise or unscrupulous activity of hundreds of franchi-
sors, together with the unwise and hasty action of thousands of franchisees, many hundreds of franchisees lost considerable sums (sometimes their life-savings) (53). Following widespread success stories of the fortunes made from franchising (54) there was wide-spread adverse publicity of the misfortunes arising from franchise involvement due to misrepresentation by franchisors and unethical practices (55).

Concern erupted at the beginning of the 1970s over the inadequate legal protection to franchisees, centering on areas of disclosure and termination. A variety of laws were passed in different States relating to these two areas (56). The laws on disclosure were primarily aimed at a requirement for franchisors to reveal their past business identity and performance and to furnish adequate information on the franchise being offered, sufficient for a franchisee to make an informed assessment of the business. The laws on termination were aimed at ensuring that franchisors could not terminate an agreement with their franchisees other than for a substantial breach of the terms of the contract. Federal laws have also been proposed on the same lines (57).

Further concern centred on anti-trust questions (equivalent to monopolistic and restrictive practices in Britain). Specific issues were the franchisor's right to allocate exclusive territories to franchisees (thereby excluding competition); the right to tie franchisees to specific sources of supply (in particular a tie to the franchisor's supply); and the right of franchisors to stipulate retail selling prices. A number of actions were brought to contest these rights (58). Decisions were contradictory and confusing, and some cases have been very long drawn out over a number of years. Franchising commentators and practitioners have claimed that judges appeared ignorant of the franchising concept, and of the potential practical effects
of their decisions. In 1976, a well-known legal expert on franchising claimed that the proposed legislation would strike at the very roots of franchising and that the future of this method of distribution was in the balance (59).

4.4 RE-IMPORTATION OF FRANCHISING TO GREAT BRITAIN

4.41 Franchise systems in the 1950s and 1960s

Mention has been made of the origins of franchising as a method of distribution within the British brewing industry. Despite the longstanding and evident success of the tied house system, with the exception of petrol service stations and car sales distributorships and of voluntary group trading within the grocery trade, no other industry or business sector appears to have made any significant attempt to emulate or adapt the system. Petrol service stations were established during the 1950s and 1960s as tenanted outlets or as solus trading outlets (60), and in many respects resemble the tied house system setup by the brewers. Whether such outlets or those of car dealers or of voluntary trading groups were influenced by the British brewing experience or by the importation of the American or European experience in each related business activity is beyond the scope of this study (61). Of more direct relevance is the introduction to Britain during the 1950s and 1960s of 'modern' franchising expressed as total business package or second generation franchising, involving a service sponsor-licensor relationship.

The first, most extensive and durable example of American-type 'modern' franchising was initially begun in 1954 in what would now be termed the fast food restaurant sector. The introduction of this franchise concept— the Wimpy Bar—by a large food production and catering company— J. Lyons and Co. Ltd.,— was not due to any considered policy regarding the potentiality of franchising (62). Rather it started because of continued pressure from the original American franchisor combined with the reluctance of the British company to invest in company-owned units, and with an interest expressed by individual prospective franchisees. Slow to start, and growing somewhat piecemeal, the Wimpy franchise
has proved a monument to the efficacy of franchising as a means of market penetration and growth, using the capital and labour of individual investors - the franchisees.

Few franchises in Britain have achieved comparable status or have shown such sustained presence. During the 1960s a number of attempts were made in Britain by British and American businessmen to set up franchise systems, particularly within the fast food sector, and within the laundry and dry cleaning business. Many of these proved to be ill-conceived, even fraudulent schemes. Many 'franchisors' were more interested in the sale of capital equipment (63), than in setting up a business of continued viability. In a number of instances the 'franchise' scheme had not been tested, and no provision was made for back-up services to sustain franchisees. In essence, such schemes were not franchises, and would be excluded from the defined terms used within this study.

Other franchise schemes initiated in the 1960s were genuine attempts to fill perceived market gaps, and included plans for a continuing mutual contribution by both franchisor and franchisee. But a number of these franchises went awry, either through misjudgement of the market demand, poor siting, bad introductory timing or lack of systematic approach. Within this category were several American fast food franchisors, whose attempt at introducing products to the British public were unsuccessful, despite their wide-spread popularity amongst American consumers (64) No analysis has been undertaken of the reasons for their failure, but it would seem to be due to an inadequate translation of American eating habits and foodstuffs to the British market, combined with an over-optimistic approach to the expected growth of such systems - and consequent withdrawal when such growth did not materialize as fast as anticipated (65)
Perhaps because of the failure or lack of success of these and other franchise systems (66) there was no marked growth in the number of such systems or in the extent of units within existing systems in the 1960s except for the steady increase of the Wimpy franchise.

4.42 Awareness of Franchising

The dynamic growth of franchising in the U.S.A. and the resultant awareness of the concept and attention paid to it by American media, had some small effect in Britain. In the late 1960s there were a few articles in the national and trade (hotel and catering) press, mostly of an explanatory nature, outlining the concept and major advantages and disadvantages of a franchising method of business (67). At least one publication, aimed at the small entrepreneur, began to include frequent and continuing references to franchising and opportunities in franchised businesses. (68) Only a very limited number of in-depth articles have been traced to this period (69) and only a very few educational centres, public libraries or professional associations have been found to contain special sections within their reference libraries on franchising per se (70).

An attempt was made to instigate enthusiasm in the franchising technique, and to promote specific franchise schemes, through a national franchise exhibition held in Brighton in 1968 (71). A franchise trade association was established in that year (72), but by 1975 when this study commenced, was no longer traceable. In 1971 a few British businessmen attended an International franchise congress in Zurich, sponsored by the European Franchise Association (73), and a few people set themselves up as consultants in franchising (74).

No further evidence of formal representation for franchising activities was apparent until November 1977, when what appears to be a successful second attempt has been made to establish a formal association of franchisors, namely the British Franchise Association (75). Unlike the previous attempt to establish such a body, the BFA has as founder members eight well-known and established franchisors including the Wimpy organisation. These and all subsequent members must abide by the code of ethics (modelled on the American International Franchise Association's code), and must pass a formal assessment of their capacity and intention to establish or continue a successful franchise system (76).
As yet, no specific government interest in franchising has been traced. No separate statistics are maintained on franchise system outlets, turnover or manpower (77). The Office of Fair Trading maintains a legal interest in franchising in the context of the Restrictive Trades Practices Acts, but as yet has not taken any action against franchisors (78).

4.43 General Extent of Franchising in the 1970s

The failure of a number of franchise schemes in the 1960s together with the mistaken coupling of franchising with pyramid selling have undoubtedly been factors affecting the growth of franchising in this country. But whilst the extent of franchising in Britain is extremely modest in comparison with its extent in the U.S.A., it is growing perceptibly in the number of units under franchise, in the number of franchise systems, and in the business areas in which it is found. Franchising now occurs in the following commercial sectors: carpet cleaning services, drain clearing services, car rentals, car repairs and accessory fitments, tools and equipment rentals, temporary staff employment agencies, educational programmes, electrical equipment sales, wedding ensemble shops, (79) Within the hotel and catering industry, franchising occurs in fast food restaurants, take-away outlets and in hotels.

A number of companies within the hotel and catering industry have announced or formulated expansion plans (80) and there is evidence of a resurgence of interest by a few notable American companies in the British market (81).

The dimensions of franchising in this country are open to speculation. Reference was made in the national press in 1971, and in a book published in 1972, to franchising being (then) worth £25 million per annum; and in another source to franchising representing .05% of total retail turnover in 1971. No substantiating evidence was included with these articles (82). More recently, it has been suggested that some two thousand franchised outlets enjoy a sales volume of around £250 million (83).
4.5 BIRTH OF CATERING CONTRACTS IN GREAT BRITAIN

4.51 Early History of Employee Feeding

Before examining the history of catering contracts it is necessary to mention briefly the backcloth against which they were set. Catering services for employees were first provided in the nineteenth century by a few factory owners, keen on social reform and of a paternalistic nature, such as Robert Owen (84). But the practice did not become widespread until the introduction of government regulations made compulsory the provision of canteens in munition factories that were established during the first world war. From an estimated 100 canteens at the beginning of the war, the numbers rose to some 1,000 within four years.

At the end of the 1st World War, many firms which had started canteens, subsequently closed them for reasons such as a lack of committed support from the factory directors and management as well as indifference on the part of the employees themselves (85). The numbers of industrial canteens remained approximately at the same level throughout the 1920s, and did not begin to increase until the late 1930s (86). By the onset of the Second World War some 6,000 units were in operation (87). Tremendous growth occurred during the Second World War due to government regulations, the introduction of night-shifts in factories and the practise of billetting workers far from home (and consequent requirement for feeding arrangements at work). In addition the increased employment of women removed the chief provider of meals from many households. By 1951 there were some 20,400 units providing catering services to employees in factories, docks and building sites (88).

4.52 Dimensions

In recent years various estimates of the size of the employee feeding sector have been made, differing in the same year, 1969, from 18,300 to 25,000 (89). More recent research indicates that in 1971 approximately 25,000 units were providing meals, snacks and beverages in separate working premises (90). Thus from 1951 to 1971 the employee feeding sector had grown by some 25%. The reasons for this growth included legislation aimed at
certain employers (91), the location of employing firms (often in areas far removed from catering facilities) and the contribution which employers felt such services made towards employee recruitment, good labour relations and employee retention.

Amongst the first large employers to hire the services of catering contractors were the Ford Motor Company and Fairey Aviation in the 1930s (92). By 1950 the few major companies, which now dominate the British scene, had been established for the express purpose of catering contracting. There were also a number of small firms which operated mainly in local areas on a restricted geographical basis. A government survey in 1969 (93) suggested that 203 contractors who operated some 4,000 units, accounted for about 22% of all employee feeding units. Two recent estimates put the contractors' market at approximately 4,500 units in 1972, and comprising about 25% of total employee catering services (94).

Apart from operating food service units for industrial and commercial employees, independent contractors have also undertaken contracts in independent schools, National Health Service hospitals, private hospitals and in colleges and other welfare establishments. In 1972, 500 such units represented 10% of the contractor's portfolio (95).

**Growth**

Penetration of the above sectors has continued since then, and new fields of operation have been created by the emergence of oil as a highly significant factor in the national and world economy. Catering contractors have recently turned their attention to the provision of catering and ancillary services to oil-rig employees, to workers involved in the construction of oil pipelines and platforms, and to areas such as the Middle East, where general development and construction projects have resulted from increased oil revenue.

In addition, some independent contractors have also diversified into other products and services, such as the sale of frozen or chilled products to client-owners, the retailing of non-food products on clients' premises, or the creation of separate divisions or subsidiaries for non-related services such as contract cleaning (96).
There are two main reasons for clients to employ the services of catering contractors within the industrial and commercial feeding sector: the increasing complexity of client's business, and the higher level of skills and knowledge required in the provision of catering services. As trading activities have become more complex, increased functional specialization has occurred within organisations. Where the size of the business has not warranted the appointment of a full-time specialist or line manager, the client has had three main options: to withdraw the catering function; to place the responsibility for it within the compass of another specialist or line manager; or to buy in the services of an independent contractor. Other activities within business which are often similarly assessed, and which frequently result in the appointment of independent contractors, include security services and cleaning operations.

A higher level of skills and knowledge within the catering function has become generally necessary, following increased consumer expectation regarding the content and presentation of food, and concerning the eating environment. In addition, increasing food and labour costs, problems of attracting suitable staff and a rising tide of legislation have all created particular problems for the client without catering expertise, being too time-consuming or beyond the capabilities of the designated executive on whom the burden has been placed. The creation and growth of independent catering contractors has been in response to this need.

### 4.6 ORIGIN OF HOTEL MANAGEMENT CONTRACTS

#### 4.6.1 Evolution by American Companies

Management contracts for hotels were first evolved in the late 1940s by American hotel companies as a means of expansion overseas, particularly in the Latin American countries (97). Hotel companies were normally unwilling to make large capital investments in such areas, owing to their potential political and financial instability. Nevertheless, they were eager to penetrate these new markets, and in some cases encouraged by airline companies to provide suitable accommodation at the end of a flight. The situation could not be resolved by the normal procedure of signing a standard lease agreement for two reasons. The first was that most owners were unwilling to enter into long lease
agreements with the (then) relatively unknown American hotel companies. The second reason was that leasing in countries where English law was not applicable proved to be a complicated process, involving obligations and guarantees, and attracting huge taxes.

An answer to the problem was a management contract, which was perceived as providing adequate returns to both parties, the owner and operator, and for which the tenure was of a duration to suit their respective needs. Intercontinental Hotels (now the wholly-owned subsidiary of Pan American World Airways) were the original protagonists of such agreements, followed closely by Hilton International (the majority of Hilton's contracts were 'operating lease agreements' which were similar but not identical to management contracts) (98).

Other U.S. chains apparently did not recognize the potential of such arrangements for two decades. During the 1950s and 1960s a 'mere handful' of management contracts were signed (99), as franchising was viewed as the major channel for expansion, and company ownership and leasing were still regarded as the acceptable means to growth.

However, in 1971 one successful company (the Hyatt Hotel Corporation) arranged, by dint of its negotiating strength, a risk-free management contract instead of a lease arrangement. This initiated what was to become a normal method of growth for the large hotel chains. Market penetration could be achieved with very little or no capital involvement (and thus virtually free of risk), using available group expertise, and spreading group overheads on a wider base.

4.62 Growth
Economic recession in 1971 following a period of substantial expansion in all property investment, including hotels, led to many hotels becoming unable to service long and short term debt. A large number of hotels reverted to institutional lenders, including the Real Estate Investment Trusts (REITs). Many lenders were disillusioned with the hotel market, and with investments that had proved unwise, and were keen to sell (100). These companies either formed their own
hotel management divisions to operate the properties, or turned to hotel management contractors to provide a short term service, and bring the hotels back to operating viability prior to sale. A side effect of this general experience was that a number of lending institutions developed a more wary attitude to financing hotel projects, and were prepared to make loans only if a well known chain were to operate the hotel. Thus the recession provided a means of growth to management contractors, whether they were independents, expressly formed to operate management contracts, or chains diversifying into a contracting role.

4.63 Dimensions
Growth in management contracts amongst the ten largest hotel chains has been spectacular. In 1970 these chains accounted for twenty two such contracts (101). By 1975 the figure had risen to one hundred and forty (a 650 per cent increase) (102), and an estimate for 1977 put the expected growth at approximately three hundred and seventy management contracts (a total increase over seven years of 1600 per cent) (103). Apart from these ten chains, one researcher mentions a further forty contracts held by another six large companies, and an additional four hundred and ninety contracts held by sixty two independent contractors. (104).

4.7 ADOPTION OF HOTEL MANAGEMENT CONTRACTS BY BRITISH COMPANIES

4.71 History
A few scattered examples of British companies operating hotels under management contract occurred in the 1950s and 1960s, but there appeared to be no particular expansionary aim behind these agreements, each one seeming to be accepted for its own particular merits, with individual arrangements tailored for each one.

The first example of an independent British contractor company being expressly set up for the operation of hotels under contract occurred in an overseas location (105).
But it was not until the early 1970s that a few hotels were built in Britain, which had been specifically planned to be run under contract (106).

Hotel companies have been slow to utilize contract management as a means of expansion and diversification. The number of hotels in Britain operated under contract is still very small, and the extent of British company involvement overseas in management contracts has only just begun to increase appreciably.

4.72 Reasons for Growth

Three main elements have affected recent growth in management contracts. As in the U.S.A., a certain stimulus was given to management contracting by a number of hotels being unable to operate viably. The early 1970s was a period of tremendous hotel expansion in certain areas of Britain. The 1969 Hotel Development Incentives scheme, through a system of grants and loans for a limited period, created precipitous activity in new building and in extensions to old buildings, some of which took place irrespective of market conditions and despite similar activity by competitors. The resultant over-capacity in some areas coincided with a period of national economic depression. The performance of most hotels was affected, but particularly those which had been built with insufficient prior assessment and/or were not operated by competent hoteliers. Some such hotels have reverted to the lenders, some have gone into receivership, some in a precarious financial state have been the subject of attention from consultants and contractors. Thus short term management contracts were gained by a few companies in respect of a few hotels.

The second main element affecting growth in contracting has been a domestic restriction on expansion. The high cost of new hotel building, limited availability of suitable sites, the high cost of borrowing and the deterrent effect of the British tax structure on capital investment in hotels have caused a considerable cutback on growth through building or acquisition. Thus some companies have turned to management contracts as a lucrative and speedy method of enlarging a chain or group.
The third and most important component stimulating growth has been the creation of new hotel markets, particularly in developing countries such as the Middle East. American, European and British companies have joined in a race to gain representation in these areas, either through company ownership or franchising, but more particularly through management contracts.

The combination of restricted opportunity in Britain and new opportunities overseas has stimulated a few large hotel companies and small independent contractors to point to their future growth as lying outside Britain, significantly or (in the case of the independents) wholly in management contracting.
CHAPTER 5 CATERING CONTRACTS

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5.2 PROFILE OF RESPONDING CATERING CONTRACTORS
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5.1 INTRODUCTION AND METHOD

The provision of catering and other ancillary services by independent catering contractors is a significant element within the industrial and welfare catering sector of the British hotel and catering industry. Recent research on the sector (1) showed that in 1972 just over two hundred independent catering contractors operated some 5,000 units in Great Britain, with a total turnover in the region of £69 million (2).

Four companies predominate in the industrial catering sector; in 1972 they accounted for over sixty per cent of all contracts, over sixty per cent of turnover and some fifty per cent of all contract catering employees (3). The remaining forty per cent of units were operated by some 200 contractors, most of whom were small, localised companies operating in limited areas throughout the country.

Research on the independent catering contractors for this thesis included interviews with representatives from the four major contractors and, in order to obtain a balanced response, from six other contractors which may be described as medium or small companies. The ten responding companies together represented 4,000 units or over eighty per cent of the universe of units under contract. Each contractor was asked to provide a copy of a standard catering contract for further examination.

In addition, as a means of checking the data provided by the contractors, and as a method of collecting additional primary information, interviews were also conducted with a small proportion of client-owners who employed the services of
the responding companies. Owing to constraints of time and funds, two clients per contractor were interviewed. In the selection of these clients, attention was paid to their size, relative importance to the contractor and geographical location, in order that as wide a range of client-types as possible could be included within the limited sample.

5.2 PROFILE OF RESPONDING CATERING CONTRACTORS

5.21 Dimensions
The ten selected companies varied widely in size, using as indicators the number of units operated, number of employees and estimated annual turnover (See Table 5.1). Using all three indicators, four contractors were classified as 'major' companies and two as 'medium-size' companies; the other four contractors were classified as 'small' companies in terms of employees and estimated turnover, but not necessarily in respect of number of units operated. The size of the contractor was not related to the size of the units operated, nor to the size of the client companies.

Table 5.2 gives an indication of the average size of unit per contractor and of the generally wide range of unit size per contractor. Only two contractors (the smallest) had a definite policy towards the size of unit which they were prepared to operate: one aimed at small units only; the other only operated units with a minimum of 1,000 potential customers.
Table 5.1
Responding Catering Contractors By Size in 1976

<table>
<thead>
<tr>
<th>No. Units</th>
<th>Frequency</th>
<th>No. Employees</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 50</td>
<td>2</td>
<td>Less than 100</td>
<td>1</td>
</tr>
<tr>
<td>51 to 100</td>
<td>1</td>
<td>101 to 1,000</td>
<td>3</td>
</tr>
<tr>
<td>101 to 250</td>
<td>2</td>
<td>1,001 to 2,500</td>
<td>2</td>
</tr>
<tr>
<td>251 to 500</td>
<td>2</td>
<td>2,501 to 5,000</td>
<td>1</td>
</tr>
<tr>
<td>501 to 1000</td>
<td>2</td>
<td>5,001 to 7,500</td>
<td>2</td>
</tr>
<tr>
<td>1001 to 1500</td>
<td>-</td>
<td>7,501 to 15,000</td>
<td>-</td>
</tr>
<tr>
<td>1501 and more</td>
<td>1</td>
<td>15,001 and more</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>10</td>
<td></td>
<td>10</td>
</tr>
</tbody>
</table>

Estimated Turnover *

<table>
<thead>
<tr>
<th>Less than £2.5m</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>£2.5m + to £5m</td>
<td>1</td>
</tr>
<tr>
<td>£5m + to £7.5m</td>
<td>1</td>
</tr>
<tr>
<td>£7.5m + to £10m</td>
<td>-</td>
</tr>
<tr>
<td>£10m + to £20m</td>
<td>1</td>
</tr>
<tr>
<td>£20m + to £30m</td>
<td>2</td>
</tr>
<tr>
<td>£30m + to £50m</td>
<td>-</td>
</tr>
<tr>
<td>£50m + and over</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>10</td>
</tr>
</tbody>
</table>

* Estimates for 1975

Source: Interviews with Contractors, Jordan Dataquest estimates
Table 5.2  Size of Units of Responding Contractors

<table>
<thead>
<tr>
<th>Average No. of Employees per Unit</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 5</td>
<td>1</td>
</tr>
<tr>
<td>More than 5 to 10</td>
<td>4</td>
</tr>
<tr>
<td>More than 10 to 15</td>
<td>3</td>
</tr>
<tr>
<td>More than 15 to 20</td>
<td>1</td>
</tr>
<tr>
<td>More than 20 to 30</td>
<td>1</td>
</tr>
</tbody>
</table>

Approximate Size of Contractors' Units by Potential Customers/Actual Meals Served *

<table>
<thead>
<tr>
<th>Range</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>25 - 300 meals/24 hours</td>
<td>1</td>
</tr>
<tr>
<td>15 - 1,800 potential customers</td>
<td>1</td>
</tr>
<tr>
<td>100 - 2,000 potential customers</td>
<td>1</td>
</tr>
<tr>
<td>4 - 2,100 meals/24 hours</td>
<td>1</td>
</tr>
<tr>
<td>25 - 4,500 meals/24 hours</td>
<td>1</td>
</tr>
<tr>
<td>less than</td>
<td></td>
</tr>
<tr>
<td>100 - 5,000 meals/24 hours</td>
<td>1</td>
</tr>
<tr>
<td>200 - 5,000 potential customers</td>
<td>1</td>
</tr>
<tr>
<td>1,000 - 11,000 potential customer</td>
<td>1</td>
</tr>
<tr>
<td>30 - 18,000 meals/24 hours</td>
<td>1</td>
</tr>
<tr>
<td>No response</td>
<td>1</td>
</tr>
</tbody>
</table>

* Variation of indicators due to differences in available statistics of respondents

Source: Interviews with Contractors
5.22 History
The ten contractor companies varied in age range over forty years. Two were formed in the 1930s, five in the 1940s, two in the 1960s and one in the 1970s. All began as small private companies (4), five of the older contractors having been taken over by large groups in recent years, and a sixth (more recently formed company) having been taken over after this survey was conducted. (5). In 1976, four of the contractors were owned by large British companies (two by the same company), two by large American companies, and four remained small, privately-owned and British.

5.23 Location
Two contractors had stayed quite localised in their operations. One operated within a twenty mile radius of a particular town in the Midlands; the other within Greater London and the Home Counties. The remaining eight contractors had a policy of operating nationally, although the resources of the smaller companies placed some restrictions on location. For instance, one company did not operate in Scotland, Wales or Northern Ireland; another company was not represented in the South West of England or North of Scotland. One company enjoyed a substantial turnover from units situated overseas or separate from the mainland of Britain (6).

5.24 Policy
As far as could be ascertained, all the contractor companies had been specifically established to undertake catering contracting, in order to take advantage of a perceived requirement for on-site catering services at factories and commercial establishments (7). The arrangement, which involved little capital expenditure, was regarded by almost all contractors as a profitable method of doing business. However, in one case, contract catering was seen not to be profitable, but had been introduced in order to retain existing clients or attract new ones to the parallel major profitable element of the business.
All but one contractor either were part of a larger company with considerable other interests, or had other interests within the contractor company, such interests including a number of activities within the hotel and catering industry, retailing of vending machines and supplies, equipment brokerage, a contract cleaning business, and a security business. One company was considering setting up a catering staff employment agency.

Over ninety per cent of the contracts of all ten contractors were within the industrial and commercial sectors (the relative proportions of which varied between contractors, but were approximately half and half). Clients within the industrial sector were reported as including foundries, breweries, heavy and light engineering companies. Clients within the commercial sector included banks, insurance companies and building societies, corporate head offices, public corporations, broadcasting and television stations, newspaper publishers and retailers. There was a trend towards increasing the percentage of units in other sectoral activities including hospitals, schools and leisure complexes.

Mention has already been made of geographical restrictions on some contractors, of policies defining the size range of unit to be operated, and of business sectors in which contractors customarily had contracts. Overall, however, the main criterion of whether or not a unit should be accepted within the contractor's portfolio was one of profitability. If a prospective unit was assessed as being a viable proposition, contractors normally accepted it, irrespective of size or market segment. Apart from profitability, other elements which sometimes took priority included the prestige and advertising value of a contract; whether the owner was already a client and therefore the contract would be accepted as a 'favour'; or whether the contract could be regarded as a 'loss leader' for future lucrative agreements of a multiple owner.
Most of the contractors had a number of multiple clients (8) ranging from those with 'one or two' clients, to one with a few hundred multiples, involving approximately one-third of that contractor's units. In another instance, one contractor had forty four per cent of total units under contract to only two multiple clients.

5.3 PROFILE OF CONTRACTORS' CLIENTS PARTICIPATING IN SURVEY

5.31 Type
The eighteen clients (9) included in the survey represented a wide range of activities. Table 5.3 reveals the split between industrial, commercial and educational sectors. Such units of the clients as were operated by the specified responding contractors were located in the following areas; six in Central London, four in peripheral London, three in the Home Counties, four in the Midlands, and one with units distributed nationwide. Ownership of the clients' businesses was predominantly in the hands of public companies, but a local government authority was included, a private company, and one which had been taken under public ownership.

5.32 Size in terms of potential customers
Table 5.4 indicates the size of the client in terms of potential customers at units operated by the contractors. Ten of the eighteen clients had agreements with the specified contractor for one unit only, thus being classified as 'single' clients. The remaining eight were 'multiples': six of these had two or three units being operated by the specified contractor; two had ten or more such units. A normal commercial practise of a number of clients was to retain the services of more than one contractor at different units. Whereas the client company might be classified as 'single' for the purposes of this survey, the company might well be a 'single' or 'multiple' client of other contractors. Of the eighteen clients within this survey, there were seven which concurrently employed more than one contractor, and two of which retained the services of five or more different contractors. Nine clients operated under their own direct management separate units or separate outlets within the same building as the contractor.
TABLE 5.3

Business Activities of Contractors' Clients

Industrial:
- 2 vehicle manufacturers
- 2 machine engineering manufacturers
- 1 silver-plate manufacturer
- 2 chemical manufacturers with related interests
- 1 manufacturers of non-moving plant

Commercial:
- 3 corporate offices: a car distributor
  - a consumer association
  - a pharmaceutical company
- 2 insurance companies
- 2 computer companies (systems divisions)
- 1 broadcasting company
- 1 departmental store

Educational:
- 1 college

Source: Interviews with clients.

TABLE 5.4

Client-owners: Size by Potential Customers per Contract

<table>
<thead>
<tr>
<th>No. Potential Customers</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>up to 250</td>
<td>4</td>
</tr>
<tr>
<td>251 - 500</td>
<td>4</td>
</tr>
<tr>
<td>501 - 750</td>
<td>1</td>
</tr>
<tr>
<td>751 - 1000</td>
<td>1</td>
</tr>
<tr>
<td>1001 - 2000</td>
<td>3</td>
</tr>
<tr>
<td>over 2000</td>
<td>5</td>
</tr>
</tbody>
</table>

Range: minimum at one site = 200; maximum = 4,300

Source: Interviews with clients.
5.33 Policy Towards the Provision of On-Site Catering

As the options open to clients in determining whether or not to employ the services of a particular contractor included the possibility of engaging another contractor, or directly-operating the catering function under the client's management, or not offering any catering function on site, the reasons for the on-site provision of such a facility are briefly examined.

Responding clients indicated a number of factors that influenced their decision to offer catering services, chief amongst which was the non-availability of alternative adequate feeding facilities near the site in question. Restrictions on time available for meals was an important factor, as was the perceived need to provide 'perks' to employees (particularly in the current period of wage restraint).

There was a general feeling amongst respondents that the provision of such facilities was a necessary aid to the recruitment and retention of staff (particularly where competitors offered these services). Where companies had historically provided on-site catering, there was an expectation on the part of employees, trades unions, and of the employers themselves, that the status quo would continue.

The need to maintain parity within a firm was mentioned by some respondents, where pressure had been brought to induce the firm to offer all employees comparable fringe benefits (including catering facilities) whether or not suitable facilities were available near the various units belonging to the firm.

Lastly, the availability of on-site catering was cited as an advantage in entertaining visitors, in terms of prestige as well as in the reduction in time and cost.
5.34 Policy Towards the Employment of Catering Contractors (10)
The most frequent response from clients was that by employing the services of a contractor, the firm would be released from the time-consuming activity of monitoring the catering function, so that it could concentrate on its mainstream activity. Allied to this, and equally stressed, was the freedom, engendered by the contractor's presence, from the necessity to recruit, interview and manage catering personnel (who were regarded as a particularly problematical category of staff). Apart from this awareness of the need for particular personnel skills, respondents indicated a need for specialist knowledge in matters such as purchasing, menu planning, budgeting, financial and stock control, and in the introduction of new policies, methods and products.

Such professional skills could have been imported by directly employing a caterer, but respondents also pointed to the benefits of permanent availability of relief staff (as and when necessary), and to the advantages of employing a catering contractor where units were geographically dispersed over considerable distances. A number of clients also thought that by using a contractor, a more standardized catering service and product could be maintained on a nationwide basis (11).

Another reason for the employment of a contractor was given as the reduction in demand on the company's specialist departments, including accounts, wages and personnel departments. The extent of saving in time and expenditure obviously varied in each situation. The most dramatic economy instanced was the reduction in the number of catering invoices which were handled by one company's accounts office from 1000 to thirteen.

By using a contractor's expertise in purchasing, and the increased buying leverage, clients hoped for benefits resulting from better products at more competitive prices. Advantages were also perceived by some clients in the provision of interest-free working capital by contractors (in the form of food stocks, payment of catering staff wages and credit from suppliers).
A number of clients suggested that an important reason (in one instance, the only reason) for using the services of a contractor, was the separation of the catering workforce from the employees engaged in the company's main activity. Reasons for requiring a separation varied. Some companies which employed highly-trained, skilled staff who commanded high salaries and extensive fringe benefits wished to avoid granting similar payments and particularly benefits to catering employees (12). In companies where the main work force was semi-skilled, but whose wages were higher than those paid to catering employees, recruitment and retention of catering staff was made easier by the agency of a third party - the catering contractor.

Mention was also made of the benefits accruing from the catering contractor acting as a 'buffer' between the client as an employer and his mainstream workforce, or between the client and the catering employees, particularly where there was significant trades union activity. Contractors were also seen to be, in some circumstances, a useful 'buffer' between over-demanding and competing line managers, insisting on a particular share of the catering services 'cake', or keen to force their own solutions on catering problems. One contractor summed up this particular role somewhat cynically by terming it the 'kick the caterer' attitude.

In some instances the decision to employ contractors was influenced by external factors, sometimes quite beyond the control of the client. In one example, according to the respondent, despite the lack of any operational or direct financial advantage accruing from a change-over from direct company catering to the employment of a contractor, such a move was initiated because of a corporate policy decision (taken in another country) to improve the company's accounts by changing fixed costs to so-called variable costs.
Schedule 5.1

Main perceived advantages resulting from the employment of contractors: per client respondents

1. Overall professional expertise in:
   - operational management
   - staff management and selection
   - budgeting and financial control
   - purchasing

2. Financial advantages from:
   - utilization of contractors' specialist skills instead of clients' group services
   - reduction in staff costs and fringe benefits
   - provision of working capital by contractors
   - purchasing economies

3. Other factors:
   - year round availability of staff
   - 'buffer' role of contractor
   - regional/national coverage

Source: interviews with clients.
The reasons for (and perceived benefits from) employing catering contractors were thus many and varied, with the predominant reason being the resultant ability of the client company to concentrate on the main activity for which it was in business. Schedule 5.1 summarizes individual responses given by clients.

5.35 Policy towards recouping or subsidising catering costs
As mentioned above, clients had various motives for providing on-site catering facilities. Allied to these various motives were differing policies in connection with recouping or subsidizing such costs. These ranged from an aim of providing free food and drink to all employees (or students, residents etc.) at a unit during normal meal and break periods, to providing only a partial subsidy on some costs. Most commonly, clients aimed either at recovering food costs but subsidizing all other related expenses, or recovering food costs plus a (varying) contribution towards labour costs and the contractor's management fee (see table 5.5).

5.4 CONTRACTUAL AND FINANCIAL TERMS OF THE AGREEMENTS
5.41 Duration of Contracts
All contracts were on an indefinite basis but usually with specified minimum initial periods. Six contractors laid down an initial six months' period, and two an initial twelve months' period. Contracts could be terminated thereafter, normally by three months notice on either side, unless a material breach of contract occurred, and was not rectified in which event agreements might be terminated immediately. Renegotiation of fees and budgets was normally on an annual basis.

Contractors were questioned about the length of retained contracts with their clients. Responses reflected varying degrees of success of relationships with clients, and differing length of existence of the contractor company. The shortest relationship was reported to be nine months, whilst a number of contractors claimed clients of from fifteen to thirty five years' standing. Not all contractors were able to respond to a question on the average length of contract before it was lost. Of the seven who did, one stated nine years and the other six contractors stated between three and five and a half years.
Catering Policy of Responding Clients

Policy                                      Frequency
- to provide completely subsidized meal      2
- to provide up to twenty per cent subsidy on food costs and to fully subsidize all other costs 3
- to recover food costs and fully subsidize all other costs 6
- to recover food costs with a 12 - 40% G.P. towards labour and management fee 6
- to subsidize costs (not specified) 1
                                            18

Source: Interviews with clients.

Table 5.5
RetentionPolicy of Responding Clients

<table>
<thead>
<tr>
<th>No. Years</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1½ - 3</td>
<td>6</td>
</tr>
<tr>
<td>3½ - 5</td>
<td>4</td>
</tr>
<tr>
<td>5½ - 7</td>
<td>3</td>
</tr>
<tr>
<td>7½ - 9</td>
<td>1</td>
</tr>
<tr>
<td>9+</td>
<td>2</td>
</tr>
<tr>
<td>no response</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: interviews with clients.

Table 5.6
Retention of Contracts in Relation to Existing Agreements

<table>
<thead>
<tr>
<th>No. Years</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1½ - 3</td>
<td>6</td>
</tr>
<tr>
<td>3½ - 5</td>
<td>4</td>
</tr>
<tr>
<td>5½ - 7</td>
<td>3</td>
</tr>
<tr>
<td>7½ - 9</td>
<td>1</td>
</tr>
<tr>
<td>9+</td>
<td>2</td>
</tr>
<tr>
<td>no response</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: interviews with clients.
Table 5.6 shows the responses by clients with regard to the duration of existing agreements with contractors. The median average fell between three and a quarter and five years, thus approximating to the response of the above six contractors when questioned. Clients were in substantial agreement with contractors in respect of the current initial and termination periods written into their agreements.

5.42 Remuneration of Contractor

5.421 Methods of Remuneration

There were two main methods by which contractors were remunerated: an 'overall fixed fee' system and a 'cost plus' system (13). Of the ten contractors within the survey, nine operated on a 'cost plus' basis and one on an 'overall fixed fee' basis. Those on 'cost plus' terms were reimbursed for costs, and in addition were paid a management fee which was calculated by one of the following methods: a fixed management fee only; a fixed management fee plus a percentage of unit gross revenue; a fixed management fee plus a percentage of unit food costs; a percentage of gross revenue. Table 5.7 analyses the terms of remuneration current amongst responding contractors (some of whom used more than one system) and, where available, states the number of units to which such terms were applicable. Table 5.8 shows the methods of payment to contractors by responding clients.

5.422 Amount of Management Fees or Main Remuneration of Contractors

Table 5.9 gives an indication of the management fees paid by responding clients. In the case of the clients of the one contractor using a fixed fee system only, no separate information was given of the actual profit retained by the contractor. Whilst this table serves as a guide to the range of fees paid by each client, it does not necessarily refer to the amount of fees per unit. In general, the higher fees were payable in respect of more than two or three units operated by one contractor for a particular client. Contractors were not able or willing to disclose information relating to their overall management fees (14).
Table 5.7
Method of Remuneration of Contractors

<table>
<thead>
<tr>
<th>Contractor</th>
<th>Fixed Cost:</th>
<th>Cost +:</th>
<th>Cost +:</th>
<th>Cost +:</th>
<th>Cost +:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Overall</td>
<td>Fixed man-</td>
<td>Fixed fee</td>
<td>% turnover</td>
<td>fixed fee +</td>
</tr>
<tr>
<td></td>
<td>Fixed Fee</td>
<td>agement fee</td>
<td>+% turnover</td>
<td>only</td>
<td>% food costs</td>
</tr>
<tr>
<td>A</td>
<td>150 units</td>
<td>150 units</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>B</td>
<td>104 units</td>
<td>416 units</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>C</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>D</td>
<td>'most' of 1800 units</td>
<td>'some' of 1800 units</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>E</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>F</td>
<td>25 units</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>G</td>
<td>5 units</td>
<td>46 units</td>
<td>24 units</td>
<td></td>
<td></td>
</tr>
<tr>
<td>H</td>
<td></td>
<td>*</td>
<td>*</td>
<td>*</td>
<td></td>
</tr>
<tr>
<td>I</td>
<td>'most' of 120 units</td>
<td>'some' of 120 units</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>J</td>
<td>4 units</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

117 units

* relates to total 732 units. Proportions not specified
Source: interview with contractors

Table 5.8
Method of Payment by Clients

<table>
<thead>
<tr>
<th>Method</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fixed fee basis</td>
<td>2</td>
</tr>
<tr>
<td>Cost plus basis:</td>
<td></td>
</tr>
<tr>
<td>+ fixed management fee only</td>
<td>10</td>
</tr>
<tr>
<td>+ fixed management fee + % turnover</td>
<td>3 *</td>
</tr>
<tr>
<td>+ fixed management fee + % food costs</td>
<td>2 **</td>
</tr>
<tr>
<td>+ % turnover only</td>
<td>1</td>
</tr>
</tbody>
</table>

18

* of which 2 at 5% turnover; 1 at 3% turnover
** of which 2 at 8% food costs

Source: interviews with clients.
**Table 5.9**

Management Fee paid to Contractors by Responding Clients in 1976*

<table>
<thead>
<tr>
<th>£ per annum</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than £1,000</td>
<td>2 **</td>
</tr>
<tr>
<td>1,001 - 2,000</td>
<td>4 ***</td>
</tr>
<tr>
<td>2,001 - 3,000</td>
<td>2</td>
</tr>
<tr>
<td>3,001 - 4,000</td>
<td>2</td>
</tr>
<tr>
<td>4,001 - 5,000</td>
<td>1</td>
</tr>
<tr>
<td>5,001 +</td>
<td>3</td>
</tr>
<tr>
<td>overall fixed fee</td>
<td>2</td>
</tr>
<tr>
<td>no response</td>
<td>2</td>
</tr>
</tbody>
</table>

* i.e. total paid by clients, not necessarily in respect of only one unit.

** 1 with discount deducted

*** 2 with discount deducted

**** impossible to separate management fee from expenses

***** unwilling to disclose information

Source: interviews with clients.
Apart from management fees a wide-spread practice amongst contractors for obtaining additional remuneration was the retention of discounts allowed by suppliers, such a practice being justified by some contractors as compensating a very low level of management fee charged to clients which would otherwise have to be increased. Three main types of discounts were discerned: a discount on regular bulk orders; a discount on additional orders placed; and a discount on prompt payment. A bulk order discount on substantial and regular orders was commonly received by contractors from suppliers, and it was to this discount that contractors normally referred when claiming to reduce costs through buying leverage and passing on such benefits to the client. The second discount which was sometimes received by contractors was given for an increase in orders over and above those for which the first discount was allowed. Thus if a contractor ordered additional supplies resulting from the gain of one or more new contracts, or from increased business within existing units, he might receive a second discount. The third type of discount - for prompt settlement of an account - was often allowed by suppliers to improve their cash flow position.

Information on the amounts obtained by contractors through the retention of discounts proved difficult to obtain. Apart from the problems involved in establishing which of the three possible discounts was received by the contractor (one of which might be argued to be an internal accounting matter, unrelated to the amount of remuneration received directly or indirectly from clients), there was an understandable reluctance on the part of contractors to reveal the sums involved, and some doubt on the part of the researcher as to the accuracy of such answers as were obtained. A further complication was the difficulty of defining 'discount'. Some contractors maintained that suppliers raised their 'list' prices before offering a 'discount', thus rendering the term meaningless, or involving a lesser discount than was apparently offered by the supplier.

Information on this aspect was equally sparse amongst clients, a few of whom were unaware that any discounts were given to
their contractors by suppliers, were ignorant of whether or not such discounts were retained by contractors or passed on to the clients, and could not give any reliable indication of the amounts involved.

Such responses as were made by contractors related not to overall amounts received or retained, but to specific discounts on specific commodities. Thus without comprehensive knowledge of the weighting of supplies, an assessment can only be very approximate, and dependent to some extent on the second-hand opinions of responding contractors in respect of their competitors. (15).

Estimated discounts varied widely in relation to different products from $2\frac{1}{2}\%$ on frozen food to $20\%$ on certain consumables and equipment. Overall estimates suggested by contractors ranged from 5 to 15%; an average of 7 to $8\frac{1}{2}\%$ seems likely and probably relates only to the first type of discount mentioned.

5.424 Discounts Credited to Clients

As mentioned above, little information was available from clients about whether or not they were credited with discounts allowed by suppliers. In three instances, however, clients provided information on the amount of such credits, which they deducted from the management fee paid to their contractor.

5.43 Obligations of Contractors

Catering contracts tended to be fairly brief documents which did not significantly differ from one to another. They defined the legal obligations of both parties, but only broadly outlined the operational obligations of contractors. In addition to what was contained in these contracts and in the published promotional material of a few contractors, there was an expectation on the part of both contractors and clients that a number of services would be performed which were normally offered by contractors.
The primary obligation of all contractors was to operate the designated unit or units in compliance with the terms set out in the contract, or more frequently set out in separate schedules or letters. Although details were included in respect of the number and location of units, hours to be operated and, in some instances, the selling prices to be charged, there was normally no precise detail of the type of service, method of cooking, presentation, menu size, menu cycle, speed of service or numbers of staff to be employed; such matters were usually left to the discretion of the contractor (usually after consultation with the client).

The provision of adequately trained unit management was implied and in some contracts there was an obligation upon contractors to obtain approval from clients prior to the appointment of unit managers. The constant availability of relief management was an expected service, though one that was not written into a number of agreements.

The recruitment, selection and training of staff adequate to the operation of the unit was an essential obligation in most contracts, though again this was not formally stated in all agreements. In most instances, catering and ancillary staff were employed by contractors (as principals, not as agents for the clients), though a few examples were given where such staff remained in the employ of clients (16). Normally the responsibility devolved upon contractors to ensure compliance with all appropriate aspects of employment law. A recent move by a few contractors was to distinguish carefully those obligations relating to the employment of catering staff which devolved upon them (the contractors) from those which were the responsibility of the clients; such a move being in response to new employment legislation.
The obligations of contractors encompassed not only the control of the catering and ancillary staff, but also to a varying degree control over the working environment, and over the food, liquor and sundry stocks and cash takings.

Whilst staff were normally in the direct employ of contractors, the provision and maintenance of the premises and equipment comprising the working environment was primarily the responsibility of the client. Whilst in a number of agreements there was no formal allocation of legal or operational responsibility between client and contractor, detailed specifications were found in four contracts, which allocated duties precisely to each party (17). Where such provisions were not formally made, the obligations of contractors normally included day-to-day cleaning and maintenance of the kitchen and ancillary areas, and the provision of light operating equipment; and responsibility was normally placed upon the contractor to notify the client of any faults or deficiencies in equipment or working conditions.

Control of food, beverage and ancillary stocks, together with control of cash receipts, was a normal obligation placed upon contractors, some of whom had special insurance policies to cover this responsibility. Although contractors often supplied initial food and beverage stocks, there was an increasing tendency to require payment (either directly or in the form of a deposit) from clients, and thus to transfer ownership of such inventory, whilst retaining control over it. Depending upon the system of operation and methods of payment between clients and contractors, the cash receipts (where such were taken) were normally retained by contractors as part of their fee and used as working capital to pay catering staff wages and other payments.
5.433 Financial and Budgetary Control

Implied, but not always stated, was an obligation upon contractors to exercise financial and budgetary control over the designated unit(s). Normal practice was to provide annual budgets and trading accounts, and most contractors offered to produce weekly budgets. Usually clients were sent a monthly (or 4 weekly) trading return, together with a variance report (if necessary) to explain discrepancies between actual and budgeted figures. At the same time contractors normally submitted invoices for reimbursement of costs plus a proportion of management fee (in cost plus catering).

Included in half the standard agreements were detailed headings of categories of costs that contractors were obliged to record on behalf of the client, whilst other contracts were less specific.

5.434 General Advice and Supervision by Group Management/Advisors

An obligation to control the activities of each unit manager and to offer advice on problems with the units was implied within the contractual relationship, and all contractors offered at least a second tier of management (though in the case of the smallest contractor this was, on some occasions, in the person of a director). The major contractors had extensive field staff consisting of district, area and regional managers (18), reporting to regional directors. The larger contractors also had a number of specialists within their organisations to offer advice on such matters as design, hygiene, purchase of equipment etc.
Purchasing Advice and Services

The provision of purchasing advice and the responsibility of arranging the delivery of food, beverage and ancillary supplies was an implied, if not a stated, obligation in almost all instances. Expected of contractors was an expertise in selection of suitable products, at competitive prices in relation to their quality, and being of a consistent standard, with a reliable delivery.

Assistance in selecting suitable fixed and operating equipment was also normally expected from contractors, though not formally offered within contractual agreements.

Implied by statements made by contractors, or through promotional literature, was an obligation upon contractors to provide supplies to clients at overall more competitive prices than through normal channels (quality, portion size etc. being equal).

Marketing, research and development

Contractors had a two-fold obligation in respect of marketing (i.e. of providing a suitable product at the required price and in the required conditions). Their first obligation was to their client in the context of meeting a need for suitable on-site catering services. Their second obligation was to the client's employees, in the context of providing them with a required product and service (of the type, quality, quantity and in the manner desired).

This dual obligation implied initial and continual reference to the needs and desires of both the client and the client's employees. Formal reference was made to this marketing function by only one contractor, although most contractors expected to undertake some initial exploration of at least the client-owner's needs, if not of his employees.
5.437 Technical Assistance

Contractors customarily carried out initial feasibility studies on the units for which they were tendering, but this was more in the context of a right (to protect themselves by eg. assessing potential sales and estimating fees chargeable) than as an obligation to the client.

Where considerable further assistance or advice was required, there was a tendency for contractors no longer to regard the provision of such services as an automatic obligation within the contract, but as an extra benefit for which the client or prospective client should pay (19). This was particularly so in circumstances where detailed plans and specifications for a new or modified unit were requested by purported prospective clients. A number of contractors mentioned that such 'clients' had obtained, through considerable effort by the prospective contractor, blue-prints for the design and operation of a unit; these plans thereafter being used to establish an operation directly-managed by the erstwhile prospective 'client'.

5.44 Rights of Contractors

In comparison with the extensive formal or implied obligations of contractors, their rights were considerably fewer.

5.441 Access and Sole Catering Rights

Most contracts contained reference to the rights of contractors to gain access to the designated units at all reasonable times. The majority of contracts also contained the proviso that no other caterer should be allowed to operate concurrently at the designated site.

5.442 Adequate Premises and Equipment etc.

Implied but not stated in all the agreements examined was the contractors right to operate in adequately constructed, equipped and maintained premises, with proper supplies of services
(eg. lighting, heating, water, telephone). As mentioned previously, there was a considerable variation in the emphasis placed in contracts on the respective rights and obligations of each party in relation to the care of, and responsibility for the premises and equipment.

5.443 Payment by Clients

The right to prompt payment of invoices rendered to clients was stated in most agreements, with specified terms of payment noted. Normally contractors sent out invoices on a monthly or four weekly basis, three weeks after the end of the trading period. Payment terms ranged from two weeks to two months.

5.444 Branding

A few contractors placed more emphasis on maintaining a readily identifiable brand image, than did the others, although in most cases this was subject to the wishes of their individual clients. Where branding was desired by the contractor, and agreed to by the client, this was normally restricted to wall plaques bearing the contractor's name and/or logo, uniforms, menus and sometimes to table napkins.

5.445 'Non-poaching' of Employees

A mutual right for (or obligation upon) both parties that was frequently found in agreements, related to the 'non-poaching' of employees who were working for the other party. It was introduced by contractors into their agreements as a protective measure against the practice (displayed by some clients) of offering the unit manager at their particular site a higher salary than he was paid by the contractor, to join their employ, prior to cancelling the arrangement with the contractor, thereby saving expenditure on the contractor's fee. Because of its more usual context as a right of the contractor, this provision has been included in this section. Normally the period of restriction upon such employment was for six months from the current contract.
In two instances, contractors retained the right to terminate the contractual agreement with immediate effect if the client company were liquidated or a Receiver were appointed, or if a material breach of the agreement were not rectified after due notice had been given.

5.45 Obligations of Clients
The obligations of clients may be summarized as the mirror image of the rights of contractors. In brief, they were to allow access to contractors to the designated site; to provide adequate facilities and services for the provision of catering and ancillary products; to pay within the agreed period such fees and reimbursements as were justifiably requested by contractors; not to employ the contractor's employees within a specified period and to comply with mutual obligations as defined.

5.46 Rights of Clients
Similarly the rights of clients have been extensively outlined as obligations of contractors. In addition to the right to the many services and benefits that have been discussed above, clients in almost all cases retained the right to monitor the contractor's performance through personal visits, access to books and records at each unit, and access to the relevant records at the contractor's head office (in fewer instances) as well as through receiving comments on the contractor's performance from employee-customers.

5.47 Mutual Obligations
Depending upon the precise wording of each agreement, and upon the customary division of responsibilities between client and contractor, there were various areas in which either or both parties had obligations. In matters of insurance, particularly in respect of employer's liability and public liability there were differing arrangements regarding whether the policy was held by one party or the other, who paid the premium and who was liable if a claim was made. Similarly, insurance for food stocks or covering the loss of cash takings, or the obligation to make good any loss, varied according to each circumstance.
Table 5.10 - Summary of Generally Obtaining Responsibilities and Rights of Catering Contractor and Client.

**Contractor:**

**OPERATIONAL Responsibilities**
- To manage and control the unit in accordance with agreed policies.
- To provide advice and help in technical and operational aspects such as choosing inventory, staff selection, training, cost control etc.
- To provide an adequate and continuing supply of manpower.
- To evaluate and select sources of supply of goods and to ensure a regular and reliable supply of same.
- To control goods, services and finances as agent for the client and to be accountable for these.

**FINANCIAL Responsibilities**
- To comply with agreed budgets (where applicable).
- To provide best possible financial performance (ie. to require lowest possible subsidy) within agreed policy.
- (Where applicable) to collect revenue from customers, i.e. client-employees and to keep account of such transactions.
- To keep proper account of all expenditures on behalf of client (except in overall fixed cost catering).

**LEGAL Responsibilities**
- To comply with all or a defined part of legal obligations in respect of working environment, equipment and (usually) of employment regulations.
- To comply with contractual provisions of catering contract.
- Not to employ client's directly-employed staff within a specified period.

**Rights**
- To sole catering rights at unit and to unfettered access.
- To compliance by client with obligations to provide adequate premises, defined equipment and a continuous supply of public services such as lighting and heating.

**Client:**

**OPERATIONAL Responsibilities**
- To provide environment and facilities for operation of catering (and ancillary services, where applicable) in accordance with agreement.
- To provide potential customers for product.

**FINANCIAL Responsibilities**
- To reimburse contractor's expenses and/or to receipt of agreed fees, at intervals as stated in agreement.
- To expect complete disclosure by contractor of receipts on behalf of clients, and expenditure.

**LEGAL Responsibilities**
- To indemnity (as agreed in contract) from employee and public liability.
- To performance by client of agreed contractual obligations.
- To prohibit client from employing contractor's staff within specified period.

**Rights**
- To agree with contractor on initial and subsequent policies and procedures.
- To use own functional executives to advise and/or implement certain functional activities (eg. architect's plans, purchasing equipment).
- To expect best possible performance from contractor in accordance with agreed policies.
- To access to unit at all reasonable times, and in most instances, to access to unit records and relevant records at contractor's head office.
Summary of Obligations and Rights of Two Parties

Mention has been made in some detail of the respective obligations and rights of catering contractor and client. Table 5.10 gives a summary of the generally prevailing operational, financial and legal responsibilities and rights of the two parties.

Performance of Terms by Two Parties

Performance by Contractors

Provision of Manpower

No formal qualitative assessment was made of the manpower provided by contractors to clients, such an exercise being beyond the scope of this survey. However, clients expressed reasonable satisfaction with the numbers and capabilities of employees supplied by contractors; although only four of eighteen clients stated that formal training of employees was undertaken by their contractors. Unit management was regarded as satisfactory by most clients, and in the few cases where in the past dissatisfaction had been expressed, contractors had replaced them with alternative managers. Relief management (one of the main perceived advantages of employing a contractor) was provided where necessary, according to respondents (20). In the larger units, however, there appeared to be adequate coverage by existing supervisory and management staff for holidays and normal rates of illness.

Operation of Unit(s)

Considerable flexibility of type and method of operation was found to exist amongst all contractors, both in terms of the numbers to be catered for, and of the quality of product and service required (extending from a snack meal to an extensive, costly, silver-service dinner) and of the method of distribution (from tea trolleys to self-service cafeteria to waitress service in private dining rooms). Clients reported the contractors' willingness to undertake additional, occasional demands of a special nature, and their capability of carrying out such functions.
Few clients made any formal attempt to assess accurately their contractor's quality of performance in the operation of their unit(s), and no such assessment was possible by this researcher within the time available. Any accurate assessment would have been dependent upon much more precisely defined standards of product and methods than were prevalent in the situations that were examined.

In general there were two methods of assessment used by clients to determine whether contractors were fulfilling their expected role: a passive method and an historical method. The former depended upon the client perceiving a marked degree of customer rejection of the catering services; the latter was through a delayed comparison of the actual with budgeted overall financial results.

In circumstances where the client organisation employed a qualified catering co-ordinator, it was customary for detailed criteria to be set in respect of products, service methods and financial and budgetary controls, and thus enabled a much more accurate assessment of the contractor's performance.

5.513 Provision of Group Services

In general, contractors provided technical assistance to clients as and when required, though no assessment was made of the quality of such assistance. Where contractors were part of a larger organization they were able to point to the availability of substantial group resources in research and development of new types of equipment, processes and food products.

Half the responding clients indicated that they had made significant use of technical advisory services of contractors in respect of fundamental re-organisation or renovation of their catering premises; and two-thirds of the clients had been advised by their contractors on equipment for catering or ancillary purposes. In some circumstances, though advice on building or design, for example, was available through a contractor's group services, larger clients (who had their own
similar group services) preferred to undertake this function themselves.

The acceptance of responsibility for a continuous marketing role (i.e. for attempting to provide suitable catering services in accordance with the detailed requirements of primarily the client, and secondarily the client-employees) was not general amongst contractors. Although most undertook an initial assessment of the client's individual requirements (in order to establish the extent and costs of services desired), this was usually in general terms only and tended to be based upon the existing situation rather than a fundamental assessment of particular needs. A general appraisal was usually repeated at annual intervals, but was most often made in the context of establishing overall budgets and contractors' fees, than of a total appraisal of the catering services. Whether, for example it was more appropriate to provide self-service or waitress-service, an elaborate or functional environment, composite meals, individual items or snacks, was rarely assessed.

Indicative of the attention paid by contractors to their indirect responsibility for meeting the needs of client-employees was the importance which they attached to channels of informational feed back. Very few instances were recorded of contractors carrying out a survey on employees' requirements for catering services. The extent of use of variously termed 'canteen committees' as media for obtaining marketing information was most frequently influenced by client-employees than by the contractor or client. Where trades-unions were active amongst employees, there tended to be much greater use of such committees and more importance attached to their deliberations,
The majority of contractors viewed such tripartite meetings of client-employee and client company representatives as 'a waste of time', being merely vehicles for 'petty moans and groans'. But a few contractors underlined the importance which they attached to such sessions, (particularly in prestigious contracts in large organisations) both as an opportunity to explain their own viewpoint to the other two parties, and as a chance to receive suggestions for the improvement or alteration of the catering services.

Considerable variations in the degree and sophistication of financial control and reporting were evident amongst contractors, but in general clients stated that they found the service adequate to their wants. Thus clients who required frequent and detailed analysis of costs and receipts and comparative figures from previous periods, employed contractors who could provide such a service. Those who were content with a monthly invoice giving a few sub-totals of expenditure and receipts, tended to employ contractors offering a more simple service.

Most contractors did not provide clients with any comparative data to indicate the range of, or average expenses, subsidies, receipts, percentage uptake of facilities etc. In some instances clients obtained indications of normally accepted ratios and amounts from their peers in other organisations. Those clients with centrally-controlled catering functions usually provided their own data.

5.5.1.4 Purchasing

Mention has previously been made of the problems inherent in determining in either qualitative or quantitative terms the claims made by contractors that a better service accrued to
clients through the contractors' centrally-organised purchasing arrangements. Without a strict comparison of product (in terms of portion sizes, taste and appearance) and of price (in terms of the amount debited to clients and the credit period allowed) and of other less tangible factors such as reliability of delivery and flexibility of the supplier to accede to variation in demand, no accurate assessment could be made of this purported benefit.

Most clients were unaware of particular purchasing arrangements of their contractors (eg. whether commodities were purchased centrally or locally or whether supplies were tied to the contractor or to nominated suppliers or could be freely purchased). Similarly most clients were unaware of generally prevailing commodity prices. None of the clients was able to provide other than a vague estimate of the discount which they thought their contractors were allowed by their suppliers, (some were unaware that discounts were awarded), and over half the clients were ignorant of whether a discount was credited to them or not.

Even clients with experienced catering co-ordinators had not undertaken an assessment of their contractor's purchasing performance except in relation to a few specific commodities, and though able to provide a more informed estimate of discounts awarded to or retained by their contractor, could give no precise figures.

Two contractors claimed that discounts on food and beverage products were passed on in full to all clients, and three stated that respectively 2%, 5% and 5% were credited to all clients (being part of the discount allowed by their suppliers). The other four contractors had various policies depending upon individual arrangements with clients. Thus in some cases no discounts were passed on; in some a proportion was credited;
and in others the total amount was attributed to the client. Discounts that were obtained on the purchase of equipment were commonly retained by contractors to offset handling and, sometimes, installation or advisory costs.

5.5.15 Availability of Field Staff

A precise assessment of such an intangible element as the quality of managerial assistance was impossible within this survey, but indicative of the availability of second tier management to unit managers and clients was the span of control. Eight of the ten contractors stated that the average span was between ten and twelve units per field supervisor (or whatever name was applied to second tier management). The size, complexity and distribution density of units varied (thus varying the spans of control within each organisation) as also did the number of tiers of management and degree of support from contractor-company advisors. Higher level management were reported as having spans of control which ranged from 35 to 80 units.

Another indicator that was used to assess the level of support from field staff was the frequency of visit to each unit. The majority of contractors stated that their aim was to ensure at least one visit per week to each unit; a few aimed to visit once every three weeks. Factors which influenced the frequency of such visits included the size and complexity of units, the capability of the unit manager, the expectations and status of clients, the amount of telephone contact between unit manager and contractor, and the existence of particular problems or events arising at each unit.

Over half the clients stated that a representative of the contractor visited their unit at least once a week, whilst one sixth of clients said a visit was made once a month or less frequently.
5.52 Performance by Clients

5.52.1 Attitude towards the Provision of Catering Services

Although clients gave a number of reasons for the provision of on-site catering services, there was a discernible variation in commitment. In a number of instances such provision was seen to be a token gesture only. Examples were given by clients of situations where either the catering environment and facilities were inadequate (in quality or extent) or the level of subsidy from the client was too low to permit the contractor to provide services that client-employees desired (e.g. wider choice of menu, larger portions, better quality products). Unwillingness by the client to increase capital investment in, or annual subsidy of catering services often prevented contractors from adjusting to evident market demands of client-employees or from increasing their sales revenue (and thus remuneration if this was linked to turnover and food costs). Thus the contractor's performance was often curtailed by client policies that were not overtly acknowledged.

5.52.2 Non-adherence to Contractual Terms

Most contractors stated that a significant proportion of their clients were dilatory in settling their accounts, and thus contravening the terms of their contractual agreements. One major contractor quoted five months as being a normal period of credit enjoyed by a substantial number of clients. Responses from clients indicated an average credit period taken of seven to eight weeks, though agreed terms differed amongst contractors from two to eight weeks. The more widespread consciousness amongst contractors of the need to monitor cashflow had caused some to introduce measures to accelerate payment of accounts, and others to consider doing so.

Some clients were reported by contractors to be unwilling to comply with their contractual responsibilities for renewing or maintaining premises or equipment; such responsibilities
being accentuated by more stringent legislation on hygiene, fire precautions and working conditions. In such cases contractors tended to rely on third-party enforcement (in the form of hygiene or fire precaution inspectors) or on the effect of proposed termination.

A number of contracts contained clauses which conceded to the contractor the sole catering right at a designated unit. Although no evidence was found of contravention of this proviso, there was a practice by a number of clients of directly operating outlets within the same complex as the contractor. As such outlets were usually those involving more prestigious or potentially more lucrative catering (such as directors' dining rooms), this was a source of considerable annoyance to contractors.
CHAPTER 6. HOTEL MANAGEMENT CONTRACTS

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6.52 Actual Performance by Clients
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INTRODUCTION AND METHOD

The task of identifying which companies and which hotels were involved in management contracts proved a daunting one. Hotels which were operated under such agreements and which were identified by a corporate name and image normally had no external features by which they could be distinguished from wholly-owned and operated, franchised or leased hotels; and if operated without external evidence of the contractor's identity were not distinguishable from privately owned and operated hotels (1). Only three companies held themselves out as being exclusively concerned with management contracts — thus enabling ready identification of the companies though not necessarily of the hotels under their management, some of which were operated without public reference to the contractor's name. The other companies which were identified as being involved in management contracts were simultaneously involved in varying combinations of leasing, franchising and in the operation of their wholly-owned hotels.

Parameters of Survey

The definition for this study of a management contract has been given elsewhere (2). Excluded therefore are wholly-owned and operated hotels and those which are franchised or are the subject of straight-lease agreements (3). Hotels which are the subject of operating-lease agreements are included, as they were found to be more closely analogous to a management agreement than to a straight-lease arrangement (4).

Distinction had to be made also between management contracts and agreements which related to pre-operational periods. A number of hotel contractors were identified as having negotiated or being in the process of negotiating contracts for the provision of pre-opening expertise to clients. Such expertise related to feasibility studies, construction plans,
furnishing and design schemes, development schedules and suggested organisational and operational requirements and procedures. In most instances, contractors anticipated or hoped that the pre-opening agreement - or technical services agreement as it was customarily called - would lead to a subsequent management agreement. Casual reference by contractors to 'management agreements' included in some instances technical services agreements, feasibility studies and consultancy projects as well as sales referrals or marketing arrangements. Unless otherwise stated only management agreements proper are included within this survey.

Further distinction is made between management agreements for hotels in operation (i.e. currently operating under such agreements at 31.12.1976), those for which a contract had been signed for management at a later date, and those which were pending or being negotiated. Various contractors were in the process of negotiations for management contracts with clients, parts of which contracts had been signed but whose validity was subject to the execution of other arrangements, e.g. the provision of suitable finance, or the mutual agreement on the exact location of the hotel. Such agreements are excluded from this survey.

Three categories of management contractors are included within this sector: British companies operating hotels under management contract in Britain; British companies operating hotels under management contract in other countries; and contractors originating from outside Britain which were operating hotels under management contract in Britain. Excluded from this survey are the overseas' interests of the last-mentioned category and foreign contractors with no current management contracts in Britain.
6.12 Methodology

Enquiries were made to establish the identity and number of companies involved in management contracts. Relevant bodies and individuals within the hotel and catering industry, business consultants, property agents and lending institutions were consulted, if they were thought likely to have been engaged as principals or agents in such arrangements or to have knowledge of those who were. The published accounts and reports of companies together with financial data on leading firms were examined.

A total of fourteen companies were found to be involved within the parameters of this survey, and one other company had signed a contract for the future management of a hotel that was under construction. Twelve hotel management contractors were interviewed in respect of fifty-five of the known fifty-eight hotels currently being managed under contract, and of eighteen of the known nineteen hotels for which future management contracts had been signed (5).

Whenever possible, reference was made to particular management agreements relating to specific hotels; where such information and documents were not available, reference was made to the standard management contracts and normal contractual terms of the contractor in question.

Some difficulty was encountered in obtaining an adequate response from clients, both in overall terms and in respect of achieving a balanced reply from both parties to a specific agreement. Although it was intended that two clients per contractor should be included in the survey, this was not possible. Half the current and all the identified signed future contracts were for hotels overseas which, as far as could be ascertained, were owned by clients based outside Britain. Constraints of time and funds prevented such interviews being held and the desire of certain other clients to maintain a low profile or remain virtually anonymous behind a company name resulted in their unwillingness to participate in the survey (6). An additional factor was that seven contractors each had current management agreements with only one client (7). Thus only eight current clients were available for interview. In addi-
tion two former clients of contractors were questioned in order that additional perspective could be obtained as to reasons for initiating and terminating the arrangement.

In making an assessment of normal contractual and financial terms between contractor and client, standard management contracts of an additional five well-established, international contractors were examined and included within the analysis. Thus a total of twelve contracts were examined (seven from twelve of the responding contractors and five as mentioned above).

6.2 PROFILE OF HOTEL MANAGEMENT CONTRACTORS

6.21 Background and Dimensions

Various criteria may be used for classifying the twelve contractors who took part in the survey. Their dimensions as companies, interests in hotels, current status and aims as management contractors were very disparate.

Classified according to size, they ranged from one company with more than 750 hotels under direct ownership, lease, franchise or management, to the smallest company with only one hotel currently in operation. This wide variation in size and current significance was further emphasized by the extensive interests in other sectors of hotel and catering and related fields that were held by two of the larger contractors. As a general order of magnitude, Table 6.1 indicates the approximate size of the twelve respondents.

Whether or not the responding companies had or were implementing policies for a long-term role as management contractors, or whether such a method of operation was a short term activity of no particular significance in the company's overall policy was another means of classification. Three companies were seen to come within the latter 'ad hoc' category, whilst nine were assessed as placing considerable emphasis on management contracts as a means of future expansion.
Respondents were further classified according to whether their role was as a contractor per se, or whether such an activity was part of wider interests in a group or chain of hotels. Three companies were in the 'independent category', having little or no involvement in wholly owned or leased hotels; eight companies were classed as 'chain or group operators'; one was in a category mid-way between these two classes. Nine contractors were British companies, three were foreign.

Thus, nine respondents (six of whom were British and three foreign) were perceived to view their role as management contractors within a long-term and significant context. Three such contractors were 'independents', six had group or chain interests.

There was also a variation in the length of time that contractors had been operating hotels under management contract. Whilst two companies had operated one or more contracts for ten years, eight had commenced such activities between 1970 and 1973 and two had begun in 1975.

Apart from their role as management contractors or operators of their wholly-owned units, several respondents were cast in other roles. Three were franchisors of a considerable size; one was a multiple franchisee; one was the organiser of a management incentive scheme with considerable similarities to franchising, and one was also a client of another contractor.

6.22 Extent of companies' Interests in Management Contracts

The small extent of involvement in current management contracts in Britain or overseas by British companies is shown in Table 6.2, together with definite future contracts that were revealed to the researcher. The extent of managed hotels per contractor varied from one hotel to fourteen. Six contractors had current managed interests in two to six hotels, and six contractors had future contracts for seven or more hotels.
Table 6.1 Dimensions of Hotel Contractors including all hotel interests *

<table>
<thead>
<tr>
<th>Size (in broad terms) **</th>
<th>No. of contractors</th>
</tr>
</thead>
<tbody>
<tr>
<td>'very large'</td>
<td>3</td>
</tr>
<tr>
<td>'large'</td>
<td>2</td>
</tr>
<tr>
<td>'medium'</td>
<td>4</td>
</tr>
<tr>
<td>'small'</td>
<td>3 ** 12</td>
</tr>
</tbody>
</table>

* i.e. including wholly-owned, leased, franchised or managed hotels

** based on indicators of estimated turnover applicable to hotel interests and/or number of units

'very large' = turnover in excess of £100m and/or more than 100 hotels

'large' = turnover between £10m and £100m and/or 20 to 99 hotels

'medium' = turnover between £m and £10m and/or 10 to 19 hotels

'small' = turnover less than £m and/or 1 to 8 hotels

*** 1 being a subsidiary company of a large group.

Source: interviews with contractors, company accounts and reports; brochures.

Table 6.2 Distribution of Hotels under Management Contract

<table>
<thead>
<tr>
<th>No. Hotels</th>
<th>No. contractors (current)</th>
<th>No. contractors * (signed future)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 hotel only</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>2 - 6 hotels</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>7 and more</td>
<td>3</td>
<td>6</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td>12</td>
</tr>
</tbody>
</table>

* only includes those disclosed to researcher.

Source: interviews with contractors.
The total involvement in managed hotels in Britain or by British companies overseas was a very small proportion of total hotels. Table 6.3 shows that within the survey those in Britain totalled 28 (and a further three were known to exist). Thus managed hotels accounted for less than 0.1 per cent of all hotels within Britain, and a much smaller percentage was applicable to British interests in managed hotels on a worldwide basis.

The size of hotels under current or definite future contract is indicated in Table 6.4. Less than one-quarter of currently managed hotels had under fifty bedrooms, and only about one-third had under one hundred bedrooms. No new contracts were known to exist for hotels of under one hundred bedrooms.

6.23 Management Fees
The variation in fee structures of contractors is discussed in a later section, with an analysis of current terms relating to some thirty agreements. Without recourse to the individual financial accounts of each hotel it was impossible to make an assessment of the sums involved, and in most instances responding contractors or clients were unable or unwilling to give detailed information.

6.24 Policy Towards Acceptance of Hotels
Contractors' policy towards accepting hotels under management contract varied but was normally subject to the usual commercial safeguards. Companies which enjoyed a high degree of branding and standardization required the prospective hotel to meet similar standards (in some cases stipulated in considerable detail) and to accord closely with the chain image. Companies which owned or operated hotels of a less standardized nature were concerned not only with the potential viability of a hotel but also whether it filled a particular marketing gap within the existing pattern of location and range of services available.
### Table 6.3 Distribution of Managed Hotels by Location

<table>
<thead>
<tr>
<th>Location</th>
<th>Current No.</th>
<th>Signed future no. *</th>
</tr>
</thead>
<tbody>
<tr>
<td>GB</td>
<td>28</td>
<td>-</td>
</tr>
<tr>
<td>Europe</td>
<td>6</td>
<td>2</td>
</tr>
<tr>
<td>N. America</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Middle East</td>
<td>-</td>
<td>9</td>
</tr>
<tr>
<td>Africa</td>
<td>17</td>
<td>4</td>
</tr>
<tr>
<td>Other</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
<td>55</td>
<td>18</td>
</tr>
</tbody>
</table>

* only includes those disclosed

**Note:** Disregards current agreements for technical services, consultancy, construction and operation of camp sites, and contracts for which partial agreement has been reached (see para 6.11).

**Source:** interview with contractors

### Table 6.4 Distribution of Managed Hotels by Size

<table>
<thead>
<tr>
<th>No. Bedrooms</th>
<th>In operation</th>
<th>Signed for Future Management *</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 50</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>50 - 99</td>
<td>7</td>
<td></td>
</tr>
<tr>
<td>100 - 199</td>
<td>17</td>
<td>2</td>
</tr>
<tr>
<td>200 - 299</td>
<td>6</td>
<td>8</td>
</tr>
<tr>
<td>300 - 399</td>
<td>7</td>
<td>5</td>
</tr>
<tr>
<td>400 - 499</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>500 - 599</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Over 600</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>55</td>
<td>18</td>
</tr>
</tbody>
</table>

* includes all those disclosed to researcher. No estimate can be made of the total number that have been signed to date.

**Source:** interviews with contractors.
The three companies which were formed primarily to operate hotels under management contracts were willing to undertake agreements on a world-wide basis. The smallest of the twelve contractors operated on a restricted regional basis only. The range in size of hotels under contract to any one contractor is demonstrated by two examples: One contractor operated hotels of a size varying from fourteen to 410 rooms; another had current or signed future contracts for hotels with from thirty two to 1270 rooms.

Table 6.3 gives details of the location of hotels currently under contract within the survey parameters, and of such future contracts that had been signed and notified to the researcher. Half those currently under operation were within Britain; no future contracts were announced in respect of this country. Two-thirds of overseas hotels under current management contract were in Africa; almost three-quarters of announced expansion was in the Middle East and Africa.

6.25 Reasons for Accepting Management Contracts

According to contractors a predominant reason for undertaking management contracts was the overall profitability of such an arrangement. Usually very little or no capital was involved, with a resultant minimal risk to the contractor (except in respect of his reputation), and a high return in relation to the contractor's investment. The profitability of such an arrangement to the contractor was usually further enhanced by the lack of direct involvement in any operating loss - the client normally being responsible for bearing all or most risks.

A second reason (closely linked to the first) was the lack of capital available for hotel expansion, or the unattractive financial returns from such investment which in the prevailing economic circumstances of high land and construction costs, and of high interest rates, made contractors reluctant to build or purchase hotels, unless the circumstances were peculiarly propitious. With possible expansion blocked in this direction, respondents suggested that the use of management contracts or franchising (and therefore other sources of capital than their own) was a possible solution.
Companies also perceived significant marketing benefits from wider exposure to potential custom, an increased number of outlets to accommodate brand-loyal guests and a broader revenue base for marketing and sales promotion, all of which could be derived through selectively accepted outlets, chosen to complement market requirements, with very little or no capital involvement.

The larger contractors contended that such additional units could be serviced by group management and specialists at proportionately little or no extra cost, at the same time as offering wider opportunities and career structure to various levels of management. Thus increased productivity could be achieved at group service level, to considerable advantage in profitability.

There was also an element of pure competitiveness, and 'showing the flag'. Certain British contractors felt that British hotel operators could achieve as good results, as management contractors, as could foreign companies. Although slow entrants into this particular field (13), they were confident that their expertise in wholly-owned and operated hotels and their resultant reputation as hoteliers, together with various national prejudices of clients (against contractors of certain national or international background) would result in their significant penetration of this market.

6.3 PROFILE OF HOTEL CONTRACTORS' CLIENTS

6.31 Business Interests and Reasons for Client Status

As only eight current and two past clients were interviewed, a detailed breakdown of their size, location, business interests etc. would have involved disclosure and would not have been meaningful in such a small sample. However, clients were broadly classified into two types: those who had initiated the building of an hotel and whose express policy from the commencement of the project had been to employ an hotel management contractor on a long term basis; and those who entered such an arrangement on an ad hoc basis, and whose intentions varied as to the duration of the relationship.
Clients within the first category numbered three. In each case the contractual agreement between the client and hotel management contractor was formed (in intention if not in law) prior to the planning and construction of the hotel or hotels. Two of these clients were companies which subsequently became hotel operators in their own right, but at the initiation of the management contract lacked expertise and human resources to undertake themselves the operation of the designated hotels. The other client was a syndicate of financial interests, with no internal expertise in hotel management, whose interest in the project was primarily a financial one, though other considerations had obtained.

The 'ad hoc' category encompassed seven clients with various reasons for hotel acquisition. Two clients were themselves hotel operators, but owing to a varying combination of factors including their geographical location, head office policy, financial rationalization and inadequate experience, a decision was made by both to employ the services of a management contractor on a short-term bridging basis in order to obtain operational and marketing benefits. In respect of two other clients, hotel acquisition was not part of their corporate policy but occurred, in one case, through a package purchase of interests, and in the other case, through the activities of a subsidiary company. The retention of ownership of these hotel interests (and of the 'contractors' services) was in each case mainly based on the ability of such an investment to provide an adequate return, though in the former instance consideration was taken of some slight mutual benefit that was perceived to result from the conjunction of the hotel with the client's main business interests. Two other clients purchased or constructed hotels as temporary adjuncts to their main business activity, and required the short term services of hotel contractors. The tenth client had signed a management contract in a tripartite arrangement which included the hotel's first mortgagee. This arrangement was a protective measure to retain the hotel's facilities and amenity value for certain sections of the public for whom the client had responsibility.
Each of the last five 'ad hoc' clients signified a desire to retain flexibility of action should disposal of the hotel or hotels be deemed necessary, and to avoid the commitment in time, effort and money necessary if direct management were to be implemented (14).

6.4 CONTRACTUAL AND FINANCIAL TERMS OF THE AGREEMENTS

An assessment of the terms governing the relationship between contractors and clients was based on interviews with both parties, together with an examination of promotional literature produced by contractors, and of the twelve management contracts, (15). In addition information was obtained from five separate 'technical services' agreements in relation to the terms governing pre-opening services offered by contractors.

Though varying in length and detail (from nine to fifty pages) all the management contracts examined were considerably more comprehensive than were the contracts of catering contractors. Not only was much attention devoted to financial aspects but in the longer agreements, there were many clauses relating to possible eventualities, and actions or remedies to be taken in each case. In general, there was a lack of definition of operational obligations on the part of contractors, which perhaps reflected the legal rather than operational background of those who drafted the agreement, as well as being an indication of the inherent difficulty of adequately defining criteria to establish standards and methods of an activity which includes many diverse elements of service.

The contracts of the foreign hotel companies who operated internationally tended to be very similar both in phraseology and layout, and to a lesser extent in the terms offered. Such similarity may reflect less secretive treatment of management contract documents amongst such companies, enabling the creation of 'normal' terms and general expectations in relation to such arrangements.
6.41 Definitions
Most contracts included a number of definitions (the maximum in one document being twenty six) in order to prevent possible misunderstandings and future disagreements between the two parties. The predominance given to defining financial terms and periods of time reflected the method of joint participation in financial results, whereby the inclusion or exclusion of certain revenues or expenses, or an alteration in the date of the opening of the hotel or of the timing of certain payments could materially affect the rewards of either party (16).

6.42 Duration of Contract, Renewals, Notice of Termination
An initial term was included in all contracts, the length varying between five and thirty years, with renewal periods ranging from one to fourteen years. The three 'independent' contractors offered shorter terms than contractors with group or chain interests. Thus five year initial terms with one to five year renewal periods were offered by the independents, whilst ten to thirty year initial terms, normally with ten year extensions, were offered by the chains or groups.

Parity in termination clauses was normally given to both parties, although one British contractor's agreement was weighted against the client (17). Half the contracts stipulated a minimum six months notice on either side; half required one year's notice. A number of contracts included involved provisions relating to different stages at which notice of termination or renewal had to be given by either party. Substantial penalty clauses against clients were included in some agreements, should the contract be terminated earlier than agreed for reasons other than breach by the contractor, force majeure etc.
Remuneration and Financial Responsibilities of Both Parties.

In order to preserve confidentiality regarding standard conditions and amounts of payment, or to allow for negotiations, some standard contracts did not contain information on the amount of remuneration payable to the contractor, or the timing or methods of such payment. A general indication of current rates and methods of remuneration has been drawn from the responding twelve contractors and eight clients plus information from standard contracts (where available). This section therefore represents standard or particular practices of seventeen contractors and thirty-one separate contractual arrangements.

Main Method of Remuneration

Two main methods were distinguished for the remuneration of contractors and rewarding of clients. One involved paying the contractor a management fee in consideration of the managerial and operational services rendered. In these circumstances, the contractor collected as agent for the client all revenues from the hotel and ancillary operations and paid all related expenses. The contractor's permitted remuneration was either withdrawn from the hotel account at agreed intervals, or retained from cash flow, the balance of which was payable to the hotel account or direct to the client.

The other main method - an operating lease agreement - was a combination of a lease and management contract. Payment for the lease was usually calculated as a percentage of the hotel's gross operating profit; any balance over such a percentage being retained by the contractor. Safeguards to protect the owner's 'rent' were normally included.
Whereas some contractors used only one of these systems and employed only one type of fee structure, others had arrangements involving either management fees or operating-leases, and utilized a variety of fee structures. Factors affecting the amount of fees chargeable included not only characteristics such as the size of hotel, capital investment, complexity of operation and its location (both in terms of particular locality and specific region of the world), but also the relative negotiating strengths of the two parties (based on their status, potentiality of future business, prestige of contract etc.) and national and political influences (18).

6.432 Fee Structure

Table 6.5 provides a classification of management fee structures that were encountered within the survey, including either those terms that were specific to separate agreements or the range of terms that one contractor had with a number of clients. Thirty-one separate responses were obtained. The percentages or amounts of fees are indicated, where available, together with the frequency with which each type of structure was encountered.

The most usual method of remuneration was found to be a combined basic fee plus incentive fee: the former being calculated normally as a percentage of gross revenue, and the latter most frequently as a percentage of gross operating profit, though alternatively as a percentage of net profit. Other methods of remuneration are summarized in Table 6.5 and specific examples of basic plus incentive fee structures are given in Appendix L.

Without detailed information on the financial performance of each hotel, no assessment could be made of the total sum involved in each case, nor could a comparison be made between structures or combination of terms (19).
## Table 6.5  Management Fee Structures

<table>
<thead>
<tr>
<th>Type of Fee</th>
<th>Frequency In Sample</th>
<th>Examples in Survey</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Basic Fee Only</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Percentage of gross revenue</td>
<td>1</td>
<td>4%</td>
</tr>
<tr>
<td>(b) Fixed £ amount</td>
<td>1</td>
<td>amount not stated</td>
</tr>
<tr>
<td>2. Incentive Fee Only</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Percentage of gross operating profit plus other incentive (formula not specified)</td>
<td>1</td>
<td>= to approx. 15% gross revenue.</td>
</tr>
<tr>
<td>(b) Percentage of net profit only</td>
<td>1</td>
<td>not specified</td>
</tr>
<tr>
<td>3. Basic Fee plus Incentive Fee</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Percentage of gross revenue plus percentage of gross operating profit * **</td>
<td>14</td>
<td>2 to 5% gross revenue + 5 to 20% GOP</td>
</tr>
<tr>
<td>(b) Fixed £ amount plus percentage of gross operating profit ***</td>
<td>4</td>
<td>£2,500 - £200,000 + 7½ to 25% GOP</td>
</tr>
<tr>
<td>(c) Percentage of gross revenue plus percentage of net profit</td>
<td>6</td>
<td>2 to 5% gross revenue + 10 to 20% NP</td>
</tr>
<tr>
<td>(d) Percentage of gross revenue plus percentage of 'super profit' ****</td>
<td>1</td>
<td>2½% gross revenue + 25% super profit</td>
</tr>
<tr>
<td>(e) Percentage of gross revenue plus percentage of gross operating profit plus percentage of net profit</td>
<td>1</td>
<td>2% gross revenue + 5% GOP + 10% NP</td>
</tr>
<tr>
<td>4. Basic Fee OR Incentive Fee</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(a) Fixed £ Amount (Minimum) or percentage of net profit.</td>
<td>1</td>
<td>£33,000 OR 30% NP</td>
</tr>
</tbody>
</table>

TOTAL 31
Table 6.5 (continued ..)

Key

Gross Revenue: normally defined as including all receivables from the operation of the hotel.

Gross Operating: normally defined as the excess of gross revenue over and above operating expenses, prior to deduction of rent, rates, property insurance, interest, depreciation, amortisation and tax.

* includes three examples in which the percentage of gross operating profit is calculated after a specified return on owner's capital or in which a specified proportion of the percentage is subordinated to debt service.

** includes 1 example of 'improved' gross operating profit where ten per cent paid to contractor on the improvement of GOP over the previous year's performance.

*** includes 1 example where percentage of gross operating profit is subordinated to 5% return on owner's capital.

**** 'super profit' refers to profit calculated after ten per cent return on owner's capital.

Table 6.6 Operating Lease: Normal terms of remuneration to owner

% Gross operating profit: varied from 66.66 to 75%

Payable: monthly or quarterly or half-yearly

Provisos: (1) minimum amount of £/$ to be retained by contractor.

(2) after which a minimum payment to be made to the owner (either of a return on capital, variously from 7½ - 9%, or a minimum fixed £/$ amount).

(3) if (2) is greater than agreed % GOP to owner, the balance is refundable in subsequent years if % GOP then greater than (2).

Definitions: Capital normally stated to be cost of building and equipment, excluding cost of land.

Gross Operating Profit (see definition in Table 6.5).

Source: interviews with contractors and clients, standard management contracts.
Calculated as a percentage of gross revenue, the range of basic fees varied from two to ten per cent, with three per cent being the most frequent amount. Where combined basic and incentive terms were in force, the incentive fee varied from 9½ to 25% of gross operating profit and from 10 to 25% of net profit, some terms including special provisions to protect to some degree, the client's financial interest.

The few examples that were recorded of operating-lease agreements are given in Table 6.6, and reveal the safeguards built into such arrangements.

6.433 Marketing or Advertising Fees or Expenses

Such costs were variously termed marketing or advertising and were treated either as direct expenses or fees paid to the contractors. In circumstances where a royalty was paid to the contractor's head office on a regular basis, it was normally calculated as an agreed percentage of total revenue (though other methods included a fixed sum per available bedroom per night or per annum, or as a percentage of room revenue only). Where based on total revenue, examples in the survey ranged from half to three per cent, the percentage varying not only between different contractors but also according to different agreements of the same contractor. In the case of two contractors, marketing fees were only levied on resort hotels or those aiming at a tourist market.

Some contractors identified their centrally incurred marketing and advertising expenses and either charged them out to hotels according to their directly attributable expenditure, or proportionately according to the size of the hotel in relation to the total group or chain (eg. ratio of bedrooms to the total). Others charged out central group service expenses en bloc (including marketing, sales promotion and reservation costs, and expenses of staff training and technical assistance
etc.), and allocated these either as directly incurred or as a stated percentage of turnover; examples of this latter method being from one to three per cent turnover.

A few contractors made no separate charge for marketing and included this within their management fee.

6.434 Other Fees or Expenses

Depending on the services provided by contractors a number of other fees or allocated expenses were charged. Reservation and sales fees were payable to contractors with very extensive world-wide reservation systems and sales offices, and examples of such levies were either based on a fixed sum per available bedroom or a fixed percentage of room revenue. In one example within the survey, three separate charges were made for advertising, for sales offices and for computer services.

Pre-opening or technical services fees were levied when substantial advice and supervision was required by the client (normally when a new hotel was being constructed), and were usually stated within a separate technical services agreement. Larger contractors within the survey required fees of from one to one and a half per cent of the capital cost of the project (20), and the smaller contractors levied fees of two and a half to five per cent. In one case a contractor offered a choice of alternative pre-opening services to clients, with fees scaled according to the level of contractor's involvement required (eg. 'advice only', 'advice plus supervision of construction', or a 'turnkey operation'). Normal terms for payment of pre-opening fees were for an initial payment of from twenty to twenty five per cent to be made upon signing the technical services contract, with periodic payments thereafter until completion.
Other fees that were sometimes levied included a royalty charged for staff training facilities at the contractor's head office, and a fixed sum payable for the use of the contractor's trademark or (physical) advertising sign.

Provisions were included in most of the contracts for a specified allocation of funds (ranging from 3½ to 10% of hotel revenue) to be put aside towards replacement of equipment, furnishings and operating supplies, or alternatively for an agreed level of depreciation to be charged on the original cost of various items.

6.435 General Terms of Payment and Financial Participation

All contractors contained reference to required timing of payment of the basic and incentive fees. (See Table 6.7). Marketing fees were normally charged some six to twelve months prior to the hotel opening for business.

Other matters that were commonly referred to in contracts related to the timing of, and payment for auditing services; whether or not interest would be charged by either party on payments undertaken on behalf of the other party; specifications relating to the establishment of a bank account for the hotel and required signatures; details of timing for transference of bank account funds; provisos stipulating that the contractor would not participate in any trading loss; that no losses would be carried forward from one year to the next (i.e. in respect of the calculation of profit sharing between the parties); or that the incentive fee to the contractor would have first call on gross operating profit.

Where contractors were seasoned international operators their agreements usually contained clauses relating to exchange control permission for exporting to specified countries or in specified currencies, all or part of management fees or reimbursements. Some contracts contained the proviso that if such fees were not exportable the agreement would be terminated.
Table 6.7

Distribution of Timing of Payment
Required by Contractors for Their Management Fees

<table>
<thead>
<tr>
<th></th>
<th>Basic Fees</th>
<th>Incentive Fees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quarterly in Advance</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>Monthly in Arrears</td>
<td>7</td>
<td>3</td>
</tr>
<tr>
<td>Quarterly in Arrears</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Half-yearly in Arrears</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>Annually in Arrears</td>
<td>12</td>
<td>12</td>
</tr>
</tbody>
</table>
Reference was made in all the standard management contracts that were examined to the provision by the client of the hotel building, fixtures, fittings, furnishings, furniture and equipment. No mention was made in such documents of any financial participation in capital expenditure by the contractor. However, responses from both parties revealed that in practice there were varying extents of financial involvement by contractors. Four of the contractors within the survey were financially involved with a total of seven current hotels (and substantial involvement had been agreed in respect of one future hotel for which a contract had been signed). This interest ranged from 12½ to 50 per cent of the equity in the eight given instances.

The policy of two of the contractors with an equity involvement, and of the other eight respondents without equity participation, was not to become financially involved in hotels for which contracts were obtained. When such involvement did occur it resulted from the bargaining strength of the client, competitive forces or anticipated future benefits deriving from a particular contract. A more positive policy towards financial participation was held by the other two contractors, who viewed such involvement as presenting an opportunity for leverage for the retention of the contract and a means of greater participation in taking policy-decisions.

Working capital was provided by clients in all the instances examined except where there was an operating lease agreement, when it was provided by contractors.
6.44 Obligations of Contractors
6.441 Operation of Hotel and provision of Manpower

The primary obligation of a contractor was the overall and continual operation of the designated hotel in compliance with agreed terms, through the agency of a sufficient number of adequately trained employees including suitably qualified line managers, functional specialists and a general manager. Overall guidelines relating to operating methods, procedures and standards were included in most agreements, and separate schedules stating the services to be provided were usually attached. However, these were in general terms only, with no precise criteria in respect of, for example, the number of staff to be employed in each department, or the range of dishes to be offered on the menu, or the speed with which room service should be effected, or the attitude required of staff to guests. Such criteria as were usually included in contracts were of an ill-defined nature, such as 'the hotel to be operated in accordance with internationally accepted standards' or 'as a first class hotel'. Thus the precise obligations in this respect were primarily decided by the contractor.

The selection, recruitment and training of appropriate hotel employees was a service that was expected normally through the medium of the appointed general manager of the hotel or of training advisors and training personnel provided by the contractor's head office. In some contracts a power of veto over the appointment of a general manager was retained by clients. Normal practice was for employees to be seconded from the contractor's other hotels or recruited specifically to the hotel, and for their salaries and fringe benefits to be a cost on the hotel's trading revenue. Whether or not such employees were employed in the name of the contractor or client varied, but the responsibility for hiring or discharging employees and of their direction and supervision remained in all cases with the contractor.
6.442 Operational Control of Hotel

Operational control over all aspects of the hotel was a normal obligation though ancillary facilities were, in some cases, undertaken by third parties (for example for the operation of a night club, extensive sporting facilities, beauty salon or boutique in the hotel's foyer). Thus responsibility for the preparation, cooking and service of food, service of drink and for the provision of accommodation services was a fundamental obligation, together with the responsibility for the control of food, liquor and other stocks, including cash receipts. The authority for such operational control was vested in the appointed general manager who, if the hotel was situated overseas, for example, and not readily accessible to the contractor's head office, had considerable responsibility placed upon him.

6.443 Financial and budgetary Control

This was an area where more precise criteria were provided for contractors, so that the client's expectations were more easily identified and the contractor's performance could be more accurately measured. Some contracts contained specific reference to prices that were to be charged (normally in relation to accommodation and not to other services) and/or to financial ratios that were to be achieved. Almost all contracts included detailed provisions requiring contractors to produce annual and monthly budgets and trading returns. The production of weekly returns including occupancy percentages, revenue figures, cost of sales percentages and other information required by clients was offered by most of the large contractors, with varying financial sophistication.

The installation of the necessary systems and procedures for the adequate financial and budgetary control of the hotel was similarly expected of contractors.
It was usual practice for contractors to deal completely with the receipt and banking of all monies, to control credit transactions, and to act as the client's agent in all normal payments necessary for the operation of the hotel. In some contracts considerable detail was included as to the precise limits of the contractor's discretion in such matters, as well as clauses prohibiting capital expenditure on behalf of the client or the disposal of fixed assets by the contractor without prior approval.

6.444 General Advice and Supervision

General advice and supervision by a second tier of management was expected of contractors, but unlike the system of field supervisors or area management that was normal in the catering contract situation, supervision by hotel management contractors was less frequent. This was mainly due to the difference in calibre of unit management, in this case being hotel general managers (some of whose responsibilities have already been indicated) and whose capabilities were expected to meet the normal demands of their position, without the need of frequent recourse to regional or head office advice.

Some contracts contained clauses requiring a specified number of visits per annum by area management or directors of the contractor company; in the case of overseas hotels this was usually for two or three visits per annum. One contractor specifically held out the company's ability to provide within twelve hours a senior executive at the site of any hotel (wherever located overseas) to deal with any significant problems.

Advice and assistance on a wide range of aspects was expected from the contractor company, both prior to the initial operation of the hotel and thereafter.
6.445 Technical Assistance or Pre-Opening Services (21)

Mention has already been made of this (usually separate) obligation on the part of contractors to provide pre-opening assistance in such matters as construction, design, furnishing and equipping an hotel. Where an extensive commitment was required of contractors a separate agreement was entered into, which (in the case of the five such contracts examined) gave considerable detail of the exact services to be provided, including the supervision of, consultation with and advice to third parties such as architects, builders, electrical and mechanical engineers, equipment installers, designers and landscapers.

When such agreements related to hotels located overseas contractors normally offered to install project managers on site during construction of the building, for periods varying from twelve to six months before completion was anticipated (22).

6.446 Purchasing Advice and Services

Although contractors were expected to arrange all necessary food, beverage and ancillary supplies necessary for the smooth operation of the hotel, this was an area in which there were normally no detailed obligations. Contractors usually provided advice on the initial hotel inventory, including capital items such as furniture, furnishings and equipment, and revenue items such as linen, china, glass, cutlery and uniforms. Whether or not the contractor supplied such items from his own subsidiary companies, or acted as purchasing agent depended upon the contractor's capacity and the client's requirements. The ordering and receipt of consumables was an area in which clients appeared to be uninformed and eager to leave to the contractor's presumed expertise.
The provision of marketing, advertising and sales promotion advice and services was an obligation that was sometimes explicitly and sometimes implicitly included in the arrangement. Some contracts contained detailed references to the various activities that would be undertaken by the contractor within this function, whilst others alluded in general and non-specified terms to the exercise of one or more of such activities on behalf of the client. No quantifiable obligation was included in contracts of the extent to which these functions would be undertaken, but mention of some or all of the following such as a head office marketing division, world-wide sales offices or referral systems, a central reservation facility, regularly placed advertisements in named magazines and specified promotional activities, were indicative of the marketing activity that could be expected of the contractor.

Rights of Contractors

Most contracts included reference to the contractor's rights to uninterrupted and quiet enjoyment of the management of the hotel. Several of the larger contractors also required sovereignty (subject to overall agreed policies) over a number of operating policies such as employment policies (for example, rates of pay, fringe benefits and dealings with trade unions); freedom to establish price structures (including room rates, discounts allowed, service charge, meal prices); and discretion over normal expenditure. In some agreements, contractors stated their right to the retention at the managed hotel of key management personnel including the general manager, food and beverage manager, accountant and resident manager, without whose continued presence, the contractor claimed the right to terminate the agreement.
6.452 Adequate Premises and Equipment

Particularly in the agreements of those contractors who operated an international chain of hotels (whose image was thus a matter of considerable concern) clauses were included to ensure that the hotel premises, equipment etc. should be provided by the client in accordance with agreed standards and that adequate capital expenditure should be undertaken as agreed. Some agreements referred to the contractor's right to implement any necessary changes (24) and to be reimbursed thereafter by the client.

6.453 Protection of Brand Image

In instances where hotels were identifiably operated by contractors (i.e. were externally branded with the contractor's name and image), much care was taken to ensure adequate protection of the trade mark, external signs etc. Penalty clauses were sometimes included to enable contractors to receive considerable recompense if brand identification were not immediately removed from the client's hotel upon termination of the arrangement.

6.454 Termination

All contracts contained detailed reference to the contractor's right to terminate the contract should certain enumerated eventualities take place. These related, for example, to the client's financial failure or his loss of title to the property, and to external factors which prevented the client from complying with his obligations to provide suitable premises (such as civil war, riot, destruction of the hotel building etc.). Some agreements listed particular intervals at which contractors could terminate the relationship from choice, without the need to prove the client's material breach of the agreement.
Obligations of Clients

The primary obligation of clients was the provision of capital, either for an existing building and contents, or for the construction of an hotel and purchase of contents. In the latter case, the extent of the client's investment depended mainly on the proposed size of the building, and on the type and quality of construction materials and finishes to be used. Whilst the size was readily definable, the standards were less easily so. To prevent disagreement, normal practice was for contractors to provide detailed specifications for the building, contents and utilities, and for a budget to be agreed as a guide to the extent of the client's total financial obligation.

Apart from an obligation to supply initial adequate capital, provisions in most contracts further stipulated that clients should fund required structural alterations, major refurbishing schemes, items of capital equipment and all expenses not normally included in standard accounting practice as items attributable to revenue. In some contracts, particular mention was made of the responsibility upon the client to provide funds for such alterations or improvements or purchase of new equipment as resulted from new legislation or local regulations (such as expenditure required to implement fire safety precautions).

The second main obligation upon clients was to bear operating losses (if any) and, usually, to subordinate their receipt of revenue to the whole or part payment of the contractor's fee. As mentioned previously, the prevalence of detailed definitions of accounting terms and periods generally avoided disagreement between the parties as to the precise obligations of the client.

Other obligations of clients centred on their responsibility to ensure that proper title was held to the hotel property, and that all taxes and legal obligations relating to the property were complied with.
In some contracts, provisions were included that obliged clients to ensure that an hotel would be completed and fully operational by an agreed date, and which stipulated penalty payments in the case of non-performance and/or the loss of revenue to the contractor.

Where hotels were located overseas, there was often an obligation for clients to pay travelling expenses and provide accommodation and transport to the contractor's head office personnel as well as to seconded employees and managers.

6.47 Rights of Clients
The many rights of clients have been discussed at length as obligations of contractors. In addition all agreements mentioned the right of access by the client to the hotel (within constraints of normal convenience), and in most agreements clients had the right of access to the relevant accounts and records within the hotel or at the contractor's head office.

Clients retained the right to terminate the management agreement if the contractor became bankrupt or suffered similar financial failure, or if he failed to perform his contractual obligations, or in the case of force majeure, where the contractor was unable to continue to operate the hotel.

6.48 Mutual Rights and Obligations
There were certain clauses that were normally included in agreements which related to rights of assignment or sale of interest in the property (these being mutual in some but not in all cases), and to the right of, and methods of arbitration.

In addition, most contracts dealt at considerable length and in great detail, with the various obligations of both or either party to procure and maintain insurance cover in respect
of, for example, the hotel building and equipment, public liability, employer's liability and loss of profits; and with the rights of both or either party to indemnity from direct or cross-liability. Clauses also related to the legal obligations and necessary actions that each party should take in response to an action by a third party (such as a guest, employee, supplier of goods or services or a competitor).

Agreements usually included a statement relating to the legal standing of both parties in terms of their separate legal entity, lack of collective liability and to their relationship not being a partnership or joint venture.

6.49 Summary of Obligations and Rights of Two Parties
Table 6.8 provides a summary of the generally obtaining responsibilities and rights of the two parties, separated into operational, financial and legal classifications.

6.5 PERFORMANCE OF TERMS BY TWO PARTIES
6.51 Performance by Contractors

The general absence of an accurate definition of operating standards (due to the complexity of defining intangibles inherent in the provision of services), or of precise services to be supplied by the contractor resulted in considerable discretion allowed to contractors, and a lack of yardsticks by which to judge their performance.

Both clients and contractors acknowledged that the most common method used by clients for evaluation was measurement of financial indicators, together with occasional, brief visits by clients to gain a subjective impression of operating standards.

Clients who were themselves hotel operators, or who had previous experience as clients of other contractors were in a much stronger position to assess their contractor's performance. Clients with no knowledge of hotel operation were
<table>
<thead>
<tr>
<th>OPERATIONAL</th>
<th>FINANCIAL</th>
<th>LEGAL</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Responsibilities</strong></td>
<td><strong>Responsibilities</strong></td>
<td><strong>Responsibilities</strong></td>
</tr>
<tr>
<td>To provide goods and services in the hotel to best possible standards in accordance with agreed policies and terms and to manage and control the operation on a continuous basis during the agreement.</td>
<td>To obtain best possible overall financial results from hotel in accordance with stated policies.</td>
<td>To operate hotel in accordance with national laws and local regulations.</td>
</tr>
<tr>
<td>To provide an adequate and continual supply of manpower.</td>
<td>To control receipts and expenditure as agent for client, the latter in accordance with agreed budgets.</td>
<td>To meet third party obligations (e.g., towards guests and employees) as agent for client or in own right as defined in agreement.</td>
</tr>
<tr>
<td>To hold out advice and assistance in technical and operational matters, usually including the planning and design of hotel inventory selection, staff selection, training, sources of supply etc.</td>
<td>To arrange a continual advertising and promotional service and to undertake a total marketing function, to stimulate demand for hotel services.</td>
<td>To comply with agreed terms of contract.</td>
</tr>
<tr>
<td>To control goods, services and finances as agent for the client and to be accountable for them.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Rights</strong></td>
<td><strong>Rights</strong></td>
<td><strong>Rights</strong></td>
</tr>
<tr>
<td>To enjoy uninterrupted managerial authority over hotel within prescribed limits, during the currency of the contract.</td>
<td>To receive agreed fixed sum or % as a management fee.</td>
<td>According to contract, to indemnity from third party liability.</td>
</tr>
<tr>
<td>To expect compliance by client with obligations to provide a suitable site, building and equipment in accordance with agreed plans and specifications.</td>
<td>To expect the provision by client of adequate initial and continuing funds for construction, equipment and operation of unit, to standards agreed by two parties.</td>
<td>In some cases, to prohibit client from employing contractor’s stuff within a specified period.</td>
</tr>
<tr>
<td>In many cases, to operate the hotel in the contractor’s name and under his brand image.</td>
<td>To be reimbursed for expenses undertaken on behalf of client, as agreed.</td>
<td>To terminate by client with contractual terms of agreement.</td>
</tr>
</tbody>
</table>

**Client:Contractor**

<table>
<thead>
<tr>
<th>OPERATIONAL</th>
<th>FINANCIAL</th>
<th>LEGAL</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Responsibilities</strong></td>
<td><strong>Responsibilities</strong></td>
<td><strong>Responsibilities</strong></td>
</tr>
<tr>
<td>To provide an adequate site, building and contents as agreed for the operation of the hotel.</td>
<td>To provide adequate initial and subsequent funds for the establishment and continuing operation of the hotel including initial investment, working capital and funds for re-investment as agreed.</td>
<td>In some cases, direct responsibility to comply, as named employer of staff with relevant employment legislation.</td>
</tr>
<tr>
<td>To allow, within defined limits, freedom of management to contractor.</td>
<td></td>
<td>Indirect responsibility, through the provision of adequate funds for the provision’s maintenance of equipment and environment, for the safety and well-being of guests and employees.</td>
</tr>
<tr>
<td>To decide in consultation with contractor on initial and subsequent policies for hotel.</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Rights</strong></td>
<td><strong>Rights</strong></td>
<td><strong>Rights</strong></td>
</tr>
<tr>
<td>To access to the hotel at all reasonable times to monitor performance, and in some instances, access to hotel records and relevant records at contractor’s head office.</td>
<td>To consider return on capital or to payment of debt service subordinate contractor’s fee.</td>
<td>To expect contractor’s compliance with agreed terms of contract.</td>
</tr>
<tr>
<td>To determine initial and subsequent policies for hotel operation.</td>
<td>To receipt of net operating profit less remuneration to contractor, transmitted at agreed intervals.</td>
<td>To terminate upon financial insolvency of client or enforced closure of hotel.</td>
</tr>
<tr>
<td>To expect best possible performance by contractor within agreed policies.</td>
<td>To information through written reports and financial statements on hotel’s performance at agreed intervals.</td>
<td></td>
</tr>
</tbody>
</table>
forced to rely on their contractor's interpretation of operating results, and on the evidence of the hotel's ability to provide required returns. Some clients in order to compensate for their own inability to analyse meaningfully the weekly or monthly trading returns provided by the contractor, and unwilling to wait for historical results to reflect possible operating deficiencies, resorted to using their personal contacts with other hotel operators as a means of evaluating their contractor's performance.

6.511 Financial Performance

No assessment was possible within this survey of the claimed financial benefits resulting from the employment of contractors, due to two main factors. The first was that the recent economic instability affecting hotels made invalid any comparison with operating results from a previous period. The second obstacle to such an assessment was that most hotels within the survey had either only been operated under management contract, or had been operated under contract for so short a time as to preclude a comparison of their initial results in the first few years of operation with those achieved during a longer, settled situation (25).

6.512 Provision of Services

As mentioned above, an evaluation of each contractor's performance posed problems for the client as well as for the contractor and for this researcher. No instances were recorded by respondents of a substantial lack of performance of contractual obligations, but such obligations were in the most ill-defined and dependent to a great extent upon the contractor's own interpretation. An impression was gained from discussions with clients and contractors of a wide divergence in the extent and capacity of contractors to provide comprehensive management services. This was not necessarily a function of size, as some smaller contractors appeared to provide
prompt personal attention to problems and (if certain skills or other resources were not available within the organisation) could suggest suitable external specialists, as against the wider human and other resources of their larger competitors (which were not necessarily immediately available to clients for reasons of geographical location or pre-occupation with wholly-owned interests).

The small number of responding clients, the unquantifiable nature of many of the services rendered by contractors, and the lack of time available for such research made impossible an assessment of each contractor's capacity to discharge existing obligations whilst undertaking additional management contracts. However, contractors were questioned on their policy regarding the rate of expansion through management contracts and their capability to provide adequate management services to clients. Those contractors with small head office resources and/or few or no hotels of their own from which to draw managers and employees, or in which to train staff, claimed that they were able to recruit in the market place the necessary functional and line management for expanded head office services and for each hotel that was to be operated, and suggested that adequate training in company procedures would be undertaken in situ. Contractors with extensive head office resources and wide hotel interests from which managers and staff could be drawn, or in which they could be trained, claimed sufficient present over-capacity and forward planning of resources to enable steady expansion of managed interests.

The greatest disparity between contractors was in their respective abilities to provide continuous marketing services, particularly in the areas of advertising, sales promotion and central reservation systems. Two of the twelve contractors merely produced brochures and promotional literature; one contractor owned a few travel agency outlets; two contractors had arrangements with travel agencies in Britain and overseas. One medium-sized contractor was in the process of establishing
a proportionately substantial sales force based in the company's hotels in a number of countries. Two medium-sized contractors received extensive marketing aid from their own or associated companies, including effective sales forces, reservation networks (one contractor having right of access to world-wide computer terminals for reservations) and extensive advertising budgets. Four large contractors had their own corporate or associated world-wide reservations and referrals networks, backed by very considerable advertising and promotional resources of funds and manpower. Such disparity in these services did not necessarily reflect a lack of promised performance by contractors, for in some arrangements the contractors did not hold out any extensive marketing services. Indicative of the potential availability of such services, and thus a yardstick by which the contractor's performance could be judged, was whether a specific marketing or advertising fee was charged to clients. Five of the twelve contractors normally charged such a fee.

Even the availability and continuous operation of such marketing resources were not in themselves indicative of the particular benefits accruing from them to particular clients. Without a full-scale survey of hotel guests (which would have involved considerable time, expenditure and guest co-operation), neither clients nor contractors were able to quantify the results. (26)

A tangible indicator used by clients to assess the extent of contractor support and control of the managed hotel was the frequency of visit by contractor corporate staff. Depending to some extent on geographical location such visits were usually infrequent, but were generally undertaken by a director or high-ranking executive and tended to be of considerable significance, lasting sometimes for one or two days (27).

6.52 Actual Performance by Clients
More precise definitions were available as to the role and obligations of clients than were in the case of contractors. This enabled a more accurate assessment by both client and
contractor of whether the client was undertaking his contractual obligations. Such definition was in part attributable to the tangible, financial (and thus measurable) nature of the contribution by clients to the arrangement, and in part to the fact that the contractual agreements (including provisions relating to client obligations) were drawn up by contractors whose experience of such arrangements enabled them to pinpoint the role and obligations of clients and to include provisions to forestall potential client evasion of such responsibilities.

6.521 Financial Performance

Although certain disagreements sometimes occurred between the two parties as to the precise obligation of clients in respect of the reimbursement of contractor expenses, or over the accounting treatment of certain items (thus affecting the revenue attributable to each party or the extent of loss-bearing required of the client), such disputes were not normally of fundamental significance to the arrangement. In a few cases, however, the client was reported to be in substantial breach of his financial obligations in such matters, and although (28) the contractor had the legal right to terminate under such circumstances, this was not necessarily an action that the contractor felt to be in his overall best interest.

No detailed assessment was made in this survey of the actual financial contribution made by clients, but in general terms contractors expressed no fundamental problems in obtaining performance by clients in respect of the initial capital investment in the purchase and/or construction and equipping of hotels. The contractor's sanction of not commencing management of the hotel until such time as adequate funds had been made available by the client to enable the building to be completed to the contractor's satisfaction, was presumably a potent weapon. However, problems were encountered in some cases, in obtaining performance by clients of what contractors took to be their (the clients) continuing obligation to
provide funds for alterations, renewals etc. The vague nature of certain terms governing this responsibility (such as 'the provision of necessary funds to maintain standards of an international hotel'), left room for disagreement over such concepts as 'necessary' and 'standards of an international hotel', and made extremely difficult the determination of what such obligations were. Whilst some clients suggested that pressure from their contractor for re-investment was primarily to enhance the contractor's image and not that of the particular hotel, some contractors pointed to the reluctance of their clients to re-invest in a hotel because of the client's (undeclared) essentially short-term interest in revenue, rather than in the long-term potential of the hotel.

Evidence suggested that where capital expenditure was directly linked to legal responsibility (such as in respect of fire safety precautions, or in the provision of a required working environment for employees), the client was more willing to perform his perceived financial obligations, and the contractor more insistant upon such performance, than where such expenditure hinged upon up-grading standards for commercial reasons alone.

6.522 Compliance with Stated Policy

Owing to the nature of hotel economics in which the establishment of an hotel as a viable concern takes a period of several years, the duration of any management agreement was of fundamental importance in the establishment of each particular fee structure negotiated between contractors and clients.

Thus the fee structures negotiated for a short-term agreement differed from those required for a medium to long-term agreement, in the former case being higher to compensate for the brief duration, and in the latter instance being low initially with significant later rewards expected (29).
To prevent circumstances in which clients initially declared long-term intentions and contractors negotiated an appropriate fee structure, with subsequent termination by the client after a brief period of operation and disproportionate financial disadvantage, several contracts included penalty clauses against early termination by clients without reasonable cause. Although such penalties weighed against such a declared change of policy, there was little sanction against an undeclared policy of maximizing current revenue, instead of long-term benefits.
CHAPTER 7  THE TIED HOUSE SYSTEM

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7.514  Marketing Services

7.52  Performance by Tenants
7.521  Compliance with Law
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7.524  Compliance with Financial Obligations.
CHAPTER 7  
THE TIED HOUSE SYSTEM

7.1 INTRODUCTION AND METHOD

The on-licensed retail outlets (1) of brewers which in the main are public houses, comprise a major sector of the hotel and catering industry. They are predominantly owned by the brewery companies themselves and are either under the direct management of the brewery companies, or operated by tenants for agreed periods in accordance with agreed terms with the brewers. This separation of ownership and management is of interest not only because it relates to a significant sector of the hotel and catering industry, but also because it was the fore-runner of the franchising method of distribution.

Twelve brewery companies were selected for interviews for this study, from the eighty-two breweries which currently operate in this country and which together own nearly 56,000 full on-licensed and off-licensed premises (2). Five major companies were found to dominate the scene, owning almost three quarters of outlets under brewery ownership and over one quarter of all licensed outlets (3). The five predominant breweries were included in the survey together with five medium sized and two small companies, the latter two categories being selected for reasons of size, geographical location and willingness to participate in the research project (4). Directors or senior executives within the twelve companies were asked to provide information on their companies, on their tenants (in general terms) and on their relationship with such tenants. Interviews were conducted with appointed representatives, and each brewery's standard tenancy agreement was examined. Where available, company reports and accounts were also perused.

As elsewhere in the research, difficulty was encountered in identifying tied trade tenants from other licensees of public houses, i.e. public house managers employed by the breweries. No distinguishing features or signs were externally evident at licensed premises to permit identification of the licensee's status, such status being determinable only through prior
knowledge or by questioning the licensee. It was deemed inappropriate to approach publicans without prior warning and a preliminary introduction, if a full and credible response to questions were to be achieved. Therefore, each brewery company was asked to suggest the names of two tied trade tenants who might be approachable and could be approached.

Although the sample of tenant respondents may have been biased by brewery executives suggesting those whom they preferred to be interviewed (i.e. those who were likely to view the brewer in a favourable light), there were certain balancing factors to restrict the brewers' undue partiality. In order to achieve as widespread a geographical and market sector coverage as possible, and to rationalize time and cost incurred in the field work, brewery companies were asked to suggest names of tenants within certain regions or localities. Considerations of size of public house (i.e. 'small' and 'large' turnover), the standing of the tenant (i.e. long-established relationship or relative newcomer), and the extent of the tenant's public house interests (i.e. single or multiple holding) were also taken into account. Rather than a bias towards especially amenable tenants there may have been a slight bias towards outstanding (and therefore memorable) tenants, such as those with more than average entrepreneurial skills, or those who were more than usually vocal about problems in the tied trade relationship (for such tenants were also suggested by a few brewery executives).

7.2 PROFILE OF BREWERY COMPANIES RESPONDING IN SURVEY

7.21 Size of Brewery Companies
There was very wide variation in the size of breweries, by all five indicators of number of public houses owned, number of employees, extent of capital investment, annual gross revenue and pre-tax profit figures. Tables 7.1, 7.2 and 7.3 give the actual (and in some instances estimated) figures, which provide broad indications of the magnitude of each of the twelve responding companies, though the following provisos should be taken into account.
All companies were involved to a greater or lesser extent in production, distribution and sale of a wide range of products. No separate figures were made available in relation to the breweries' ownership of, or specific trading with tenanted public houses. Thus the number of employees within the brewery group, the capital involved, gross turnover and profit all related to the total interests of the brewery. In distinguishing between the size of companies, predominant attention has been paid to the number of company-owned on-licensed premises; other indicators have been treated as secondary considerations.

Ownership of public houses ranged amongst the twelve breweries from 200 houses to 9,000, with a median average of 1850 and arithmetic mean of 3600 units. Table 7.1 indicates the distribution of on-licensed premises amongst brewery companies. Five were classified as large (with over 5000 units); five as medium sized (500 to 5000 units) and two as small (less than 500 units).

By number of employees within the brewery company, there was some polarization, with five companies employing less than 7,500 people and half with more than 22,500 (Table 7.2). These figures, of course, did not include either tenants or tenants' employees, neither of whom were employed by the breweries.

Table 7.3 reveals a variation in financial statistics not only between the small, medium and large companies, but also within each category. Such a variation reflects both differing degrees of commercial success and different portfolios of interests in production, distribution and wholesale and retail sales of various liquor products, on a regional, national and (to some extent) international basis.
Table 7.1  
Number of Public Houses Owned by Responding Brewery Companies

<table>
<thead>
<tr>
<th>No. of Units *</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 500</td>
<td>2</td>
</tr>
<tr>
<td>more than 500 and less than 5000</td>
<td>5</td>
</tr>
<tr>
<td>more than 5000</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>12</td>
</tr>
</tbody>
</table>

* to nearest 100 units

Source: Interviews with Brewery Representatives

Table 7.2  
Number of Employees Per Responding Brewery Companies *

<table>
<thead>
<tr>
<th>No. of Employees</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 7,500</td>
<td>5</td>
</tr>
<tr>
<td>More than 7,500 to less than 22,500</td>
<td>-</td>
</tr>
<tr>
<td>More than 22,500 to less than 37,500</td>
<td>3</td>
</tr>
<tr>
<td>More than 37,500 to less than 52,500</td>
<td>1</td>
</tr>
<tr>
<td>More than 52,000</td>
<td>2 **</td>
</tr>
<tr>
<td></td>
<td>11 **</td>
</tr>
</tbody>
</table>

* Full and part time, averaged over year

** No separate figures were available for two companies owned by one group

Source: Stock Exchange Year Book, Extel Cards, Company Reports and Accounts. Estimates where no such information was available.
<table>
<thead>
<tr>
<th>£m</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 10</td>
<td>2</td>
</tr>
<tr>
<td>10 - 99</td>
<td>4</td>
</tr>
<tr>
<td>100 - 249</td>
<td>3</td>
</tr>
<tr>
<td>250 and over</td>
<td>3</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>£m p.a.</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 50</td>
<td>4</td>
</tr>
<tr>
<td>50 - 99</td>
<td>1</td>
</tr>
<tr>
<td>100 - 249</td>
<td>2</td>
</tr>
<tr>
<td>250 - 399</td>
<td>3</td>
</tr>
<tr>
<td>400 and over</td>
<td>2</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>£m p.a.</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 10</td>
<td>5</td>
</tr>
<tr>
<td>10 - 19</td>
<td>1</td>
</tr>
<tr>
<td>20 - 29</td>
<td>4</td>
</tr>
<tr>
<td>30 and over</td>
<td>2</td>
</tr>
</tbody>
</table>

* Based on 1975 figures to nearest million £ where available; estimates made in respect of two companies (one with no separate figures available, one giving no response)

** Where available, based on 1975 figures to nearest £ million. Estimates made where figures unavailable, based on 1974 figures in two instances.

*** Based on 1975 figures where available to nearest £ million. Estimates made where no separate data available. Profit before extraordinary items.

Source: Stock Exchange Year Book, Extel cards, company reports and accounts.
7.22 Location of Brewery Companies
Almost all the breweries were an amalgamation of interests, the reason for such amalgamations being in some cases to effect a wider geographical coverage within the British Isles. Table 7.4 shows that only one company had strictly local interests with localised production, distribution network and retail outlets. Six companies were essentially regional in nature, though the extent of such regions varied; and five were classified as 'national' though none were represented throughout Britain, and there was a variation in their national spread of production facilities and retail outlets.

7.23 Background of Brewery Ownership
A detailed analysis of the history of the twelve breweries is beyond the scope of this study, bearing in mind the succession of amalgamations common to most of the responding companies (and to breweries in general). The consequent composition of most of these companies included amalgamated breweries, distilleries, bottling plants and depots, wine and spirit shipping and distributing companies, mineral and fruit juice manufacturers, cider producers, hotel and restaurant companies, and other subsidiary interests such as property and investment companies. The oldest brewery (i.e. being essentially in the same state as when founded and not having undergone a series of mergers etc.) was established in the middle of the eighteenth century. Those representing the middle of the chronological spectrum were three companies which had been formed in the 1920s and 1930s (and had not significantly altered since then); and at the other extreme were five companies all of which had been registered (as merged interests) in the 1960s or had been taken over by another larger company in the 1970s.
Three companies though publicly quoted, considered themselves to be essentially family-owned and operated businesses. The other nine companies ranged from those which were just moving away from dynastic ownership to those which were part of a large conglomerate. In two separate instances amongst the responding breweries two were linked. In one case two breweries were jointly owned by another company (but retained operating autonomy with regard to retailing, though merged for production purposes); and in another case, two breweries had merged, with one predominating in policy matters, though still allowing the other company regional autonomy (5).

7.24 Brewery Interests in Tied Trade Tenancies

7.241 Numbers and Ratios to Total Estate

The number of tenanted houses owned by a brewery varied from 172 in one instance to 6,100 in another instance, with a median average of 1175 and arithmetic mean of 2,480 (see Table 7.5). Tenanted houses were also calculated as a percentage of the brewer's total on-licensed estate. With one exception, where tenanted properties accounted for 18% of the brewer's public houses, the difference between each brewery, ranged between 62% and 87%.

7.242 Financial Remuneration

As mentioned above, no breweries produced specific figures relating to their internal trading with their public houses, and respondents were unable or unwilling to disclose the total net payment from tenants, which was normally obtained by a dual method: a fixed rental sum plus a premium on supplies(6).
### Table 7.4

<table>
<thead>
<tr>
<th>Type</th>
<th>No. of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>National *</td>
<td>5</td>
</tr>
<tr>
<td>Regional</td>
<td>6</td>
</tr>
<tr>
<td>Local</td>
<td>12</td>
</tr>
</tbody>
</table>

* with some international subsidiary companies, responsible for production and sales in other countries.

Source: Stock Exchange Year Book, Extel cards, company reports. Interviews with brewery representatives.

### Table 7.5

<table>
<thead>
<tr>
<th>No. Tenanted Houses</th>
<th>No. of Companies</th>
<th>On-licensed as % of total pub. houses</th>
<th>No. of Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 250</td>
<td>1</td>
<td>less than 20</td>
<td>1</td>
</tr>
<tr>
<td>250 - 499</td>
<td>3</td>
<td>20 - 29</td>
<td>-</td>
</tr>
<tr>
<td>500 - 749</td>
<td>1</td>
<td>30 - 39</td>
<td>-</td>
</tr>
<tr>
<td>750 - 999</td>
<td>-</td>
<td>40 - 49</td>
<td>-</td>
</tr>
<tr>
<td>1000 - 1999</td>
<td>2</td>
<td>50 - 59</td>
<td>-</td>
</tr>
<tr>
<td>2000 - 2999</td>
<td>-</td>
<td>60 - 69</td>
<td>3</td>
</tr>
<tr>
<td>3000 - 3999</td>
<td>1</td>
<td>70 - 79</td>
<td>4</td>
</tr>
<tr>
<td>4000 - 4999</td>
<td>1</td>
<td>80 - 89</td>
<td>4</td>
</tr>
<tr>
<td>5000 and over</td>
<td>3</td>
<td>90+</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td></td>
<td>12</td>
</tr>
</tbody>
</table>

Source: interviews with brewery representatives.
Respondents were questioned on their brewery's past, present and future policy towards the tied house estate. The inherited situation, resulting from historical actions which had been of mutual benefit to both brewer and licensee (7) was a predominant factor in determining the ratio of directly managed to tenanted houses. In the more recent past, almost all respondents acknowledged that they had indulged in a move towards decreasing tenanted outlets in favour of directly managed public houses. They suggested that the main reason for such a move was the relatively less beneficial return on tenanted houses (being the wholesale margins on supplies plus rent payments which were pegged to a very low level by legislation) (8), compared to the wholesale plus retail margins on managed houses.

Brewery executives also pointed to the need for building larger public houses than had previously been customary, in order to provide the public with more extensive catering and entertainment facilities; and to ensure a more economic system of distribution (i.e. fewer but larger 'drops', that is separate deliveries of supplies). These large public houses required considerable capital investment which, the brewers maintained, could only be serviced by a combination of wholesale and retail margins, an economic rental for such premises being beyond the capability of any tenant.

But in the last two or three years, a slight change in policy has occurred, according to respondents. Managed houses were no longer providing such a good return, as a result of increased salaries to public house managers, continued governmental restrictions on selling prices, and the general rise in cost of supplies and fixed expenses.
Head office and regional administration costs borne by brewery companies had also considerably increased, with a resultant rise in supervisory costs per managed house. Thus most breweries stated their current policy to be one of selectively discarding those managed houses which were making a loss or only marginally profitable, or which were widely dispersed (and thus involving a disproportionately high element of administration time and cost). These houses were either sold on the open market or offered as tenancies, in which latter state the breweries maintained that they could be operated profitably by the licensee.

According to respondents this trend towards a greater number of tenanted houses was partly balanced by the continued loss of tenanted houses, due to compulsory purchase orders, or to the brewer selling such properties. Where other public houses were bought and substantially renovated, or newly built either to replace such losses or to enter a new market (such as new towns or redeveloped areas), these houses were put to management. Thus a slight overall trend to tenanted houses was reported by five of the breweries, including two major companies. Of the three breweries which had a policy of increasing the percentage of managed houses, two were amongst those with the highest current ratio of tenanted: managed houses, and the third reported a lack of suitable tenants applying(9).

Two of the large companies and one medium-sized company stated that they had embarked on a policy of issuing tenants with long leases of up to 21 years, at an agreed rent and on agreed conditions. These conditions included the tenant accepting total financial and operational responsibility for the upkeep of the premises (10), but agreed the supply of liquor at better rates than to normal tied-trade tenants. Such arrangements were stimulated by two main factors. The escalating costs of renovations and redecorations were making both brewer and tenant less ready to undergo capital investment, the former because of difficulty in recouping such costs through rent increases (11), and the latter because of insecurity of tenure. The solution, which appeared to be mutually satisfactory to both parties, was to offer to tenants a long lease (and thus security
of tenure) whilst shifting responsibility for capital investment onto the licensee.

In addition to various changes in type of tenancy, and in ratios of tenanted houses to the total estate, there was a general policy amongst all breweries of raising rents payable by tenants to a more realistic level.

7.3 PROFILE OF TIED-TRADE TENANTS RESPONDING IN SURVEY
Although the population of the tenant sample was relatively small, sufficient information was obtained to provide a broad indication of tenant demographic features, financial performance and relationship with the brewer.

7.31 Location of Tenanted Houses
As mentioned earlier the breweries and their tenants were selected for interviews on as wide a geographical coverage as possible. In addition, attention was paid to achieving within the sample a balanced spread of public houses, sited in particular local environments, thus affecting their market potential. Table 7.6 gives a breakdown of the geographical regions in which the tenanted houses were situated and of their particular localities.

7.32 Personal Background of Tenants
7.321 Educational attainments

Very few tenants had any educational or professional qualifications. Twenty of the twenty four respondents had not passed any examinations, three had passed a few O'levels or similar examinations, and one had been awarded a degree. Only three had received a professional qualification (none being of direct relevance to their jobs as licensees).
Table 7.7 reveals the predominant past occupation of tenants (not necessarily immediately prior to their present tenancy but prior to tenant status in the brewing industry). Their backgrounds were varied, and almost all had been employees rather than entrepreneurs in their own right. Four of the twenty-four respondents had backgrounds within the public house sector, either as brewery-employed or tenant-employed manager or as a working member of a family with tenanted interests. A further two tenants had previously enjoyed close connections with the licensed trade as representatives for companies selling liquor. Three-quarters of the sample had no previous working experience within the licensed trade though one-third of respondents stated that their parents or grandparents had been licensees.

Most tenants had not undergone any previous formal training in any field (the few exceptions being engineering courses or training in H.M. services, this being of no direct relevance to their occupation as licensees). Table 7.8 reveals the extent of formal or informal training and experience in public house management that had been experienced by tenants prior to taking up a tenancy. Two in five tenants had no prior experience or training in the operation of licensed premises (though in three instances their wives had supervisory experience in the hotel and catering field). Of the remainder, four tenants had extensive experience as managers, six had worked in public houses in various capacities, and four had undergone formal training in public house operation and management lasting between three days and two weeks.

7.323 Age

There was a wide range of age of tenants from 29 to 62 years, the median and modal average falling between 40 and 49 years. (see table 7.9).
Table 7.6
LOCATION OF PUBLIC HOUSES OF TENANTS INTERVIEWED

<table>
<thead>
<tr>
<th>Region</th>
<th>Frequency</th>
<th>Environment</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greater London</td>
<td>4</td>
<td>Town/city</td>
<td>11</td>
</tr>
<tr>
<td>Home Counties</td>
<td>7</td>
<td>Industrial area</td>
<td>2</td>
</tr>
<tr>
<td>Eastern Counties</td>
<td>1</td>
<td>Suburban/semi rural</td>
<td>5</td>
</tr>
<tr>
<td>Midlands</td>
<td>2</td>
<td>Rural</td>
<td>6</td>
</tr>
<tr>
<td>North</td>
<td>6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>North East</td>
<td>4</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: interviews with tenants.

Table 7.7
BACKGROUND OF TIED TRADE TENANTS:

PREDOMINANT PAST OCCUPATION * **

<table>
<thead>
<tr>
<th>Description of occupation</th>
<th>No. of Tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commercial travellers/representative</td>
<td>5 ***</td>
</tr>
<tr>
<td>Public House manager or working member of tenants family</td>
<td>4</td>
</tr>
<tr>
<td>Engineers: mechanical and electrical</td>
<td>4</td>
</tr>
<tr>
<td>H. M. Services: army, navy, prison officer</td>
<td>3</td>
</tr>
<tr>
<td>Retail and office employees</td>
<td>3</td>
</tr>
<tr>
<td>Business managerial capacity</td>
<td>2</td>
</tr>
<tr>
<td>Independent businessmen/entrepreneur</td>
<td>2</td>
</tr>
<tr>
<td>Technical specialist</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>24</td>
</tr>
</tbody>
</table>

* prior to becoming a tenant (not necessarily tenant of current brewer).

** Two tenants were substantially involved in the entertainment sector in addition to their full time jobs.

*** Includes two representatives for liquor sales.

Source: interviews with tenants.
FORMAL AND INFORMAL TRAINING AND EXPERIENCE OF TENANTS
IN LICENSED TRADE PRIOR TO COMMENCING TENANCY

<table>
<thead>
<tr>
<th>Type of exposure</th>
<th>No. of Tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Extensive experience as manager for brewery or other tenant</td>
<td>4</td>
</tr>
<tr>
<td>Considerable experience of public house operation through family upbringing or regular part-time work</td>
<td>6</td>
</tr>
<tr>
<td>Formal course in licensed house management* of duration from 3 to 14 days</td>
<td>4</td>
</tr>
<tr>
<td>No training or experience **</td>
<td>10</td>
</tr>
</tbody>
</table>

* Offered by own brewery before taking up the tenancy or organised by Brewers Society at two training centres in Britain.

** To tenant. In three instances the tenants wife had catering or hotel supervisory experience.

Source: interviews with tenants

---

TABLE 7.9

<table>
<thead>
<tr>
<th>AGE OF TENANTS</th>
<th>No. of Tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Years</td>
<td></td>
</tr>
<tr>
<td>Less than 30</td>
<td>1</td>
</tr>
<tr>
<td>30 - 39</td>
<td>5</td>
</tr>
<tr>
<td>40 - 49</td>
<td>9</td>
</tr>
<tr>
<td>50 - 59</td>
<td>6</td>
</tr>
<tr>
<td>More than 60</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: interviews with tenants
7.324 Affiliation with Locality

Tenants were questioned regarding their recent connections with the locality in which their public house was sited. Half the respondents had no previous affiliation with or knowledge of the area; half had lived or worked in the locality for a significant period, with one third of these having very strong connections (such as having spent all their lives in that particular vicinity).

7.33 Tenant Stability
7.331 Loyalty to One Brewery and Duration of Relationship

Table 7.10 reveals that there was almost no movement by tenants from one brewer to the next (12). The duration of relationship between the two parties varied widely from two and a half years to twenty two years (see Table 7.11). There was some correlation between the age of the tenant and the duration of the relationship but in each age grouping there was a variation in tenancy duration of at least ten years. Thus below the age of 39 there was a span from four to fourteen years duration; from 40 to 49 a span of two and a half years to fourteen years; and over 50 years span of four to twenty two years. A number of young to middle-aged tenants had enjoyed long tenancies with their brewers, whilst a few of the older tenants had relatively short relationships with their brewers.

7.332 Stability of Holding of Licensed Premises

Also indicated in Table 7.10 is the number of licensed premises for which the tenant had had a tenancy. Two in five tenants had remained in the same public house, whilst the balance of respondents had undertaken agreements for up to four successive tenancies. When tenants moved it was normally a process of up-grading from a house with a small turnover to a larger turnover, or with better facilities or aiming at a more prosperous market.
### Table 7.10

**STABILITY OF TENANTED HOLDING**

<table>
<thead>
<tr>
<th>Successive relationships with Breweries</th>
<th>Successive Tenancies to Tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>No. of Brewers</strong></td>
<td><strong>Frequency of Tenants</strong></td>
</tr>
<tr>
<td>1 only</td>
<td>22*</td>
</tr>
<tr>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>24</td>
<td></td>
</tr>
<tr>
<td><strong>No. of Tenanted Houses</strong></td>
<td><strong>Frequency of Tenants</strong></td>
</tr>
<tr>
<td>1 only</td>
<td>10</td>
</tr>
<tr>
<td>2 successive</td>
<td>5 **</td>
</tr>
<tr>
<td>3 successive</td>
<td>6</td>
</tr>
<tr>
<td>4 successive</td>
<td>3 ***</td>
</tr>
<tr>
<td></td>
<td>24</td>
</tr>
</tbody>
</table>

* In two instances a tenant's brewery company had been taken over by another brewery, with whom the tenant maintained a tenancy.

** of which in one instance, two houses now held concurrently.

*** of which in one instance four houses now held concurrently.

Source: interviews with tenants.

### Table 7.11

**LENGTH OF TENANTED RELATIONSHIP WITH BREWERY***

<table>
<thead>
<tr>
<th>Duration in Years</th>
<th>No. of tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 5</td>
<td>6</td>
</tr>
<tr>
<td>6 - 10</td>
<td>9</td>
</tr>
<tr>
<td>11 - 15</td>
<td>7</td>
</tr>
<tr>
<td>more than 16</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>24</td>
</tr>
</tbody>
</table>

* relationship of tenant with current brewer as a tenant (excluding as manager). This may refer to more than one consecutive holding with the same brewer.

Source: interviews with tenants.
7.34 Extent of Involvement

7.341 Single or Multiple Holding

Four-fifths of the tenants had agreements with their brewers for a single unit tenancy, whilst one-fifth had a multiple holding of between two and four public houses. A further one-fifth claimed to be actively negotiating with their brewers for a second, concurrent public house.

7.342 Operational Involvement of Tenant's Family

In all instances the tenant's wife took an active role in the operation of the licensed premises, although such role varied from being a joint licensee (with total joint responsibility) to merely contributing a few hours labour per week. Some three-fifths of wives regularly worked full time, whilst some two-fifths normally worked in a part-time capacity. Wives were predominantly charged with responsibility for catering, but this varied from a minimal involvement of producing sandwiches on request, to a full-scale and extensive meal operation. In addition to the support of their wives one quarter of the tenants also received the regular full-time help of one or more other relatives (13) Such family commitment did not necessarily occur where there was a multiple holding. In one example, four members of one family were engaged full-time in the operation of one public house; and in another instance one tenant with only part-time assistance from his wife and no operational contribution from other relatives, had the tenancy of four public houses.

7.35 Policy of Tenants

7.351 Reasons for becoming a Tenant

There were a variety of personal reasons given by tenants as to why they left their previous employment preferring to become licensees, but most centred on their requirement to be 'their own boss' and to be free to manage their day-to-day work pattern as they themselves wished. The large majority of respondents gave three main reasons for their taking up tenancies. These were their insufficiency of capital to purchase a free house, the perceived freedom of being a tenant, and the
relatively low financial rewards payable to public house managers. In addition, a few tenants cited their inexperience of the licensed trade and consequent wish to learn their trade at their brewers expense, without risk of their own capital.

7.352 Reasons for Selection of Specific Brewery

Why tenants chose to enter into agreement with their particular brewer was due to a greater variety of reasons. In some instances, it was because the tenant desired to operate in a specific area, which happened to be predominantly the domain of that brewer. In other instances, the tenant liked one particular public house. A number of tenants approached several brewery companies, and entered into an agreement with whichever company first responded or first offered a suitable establishment. Other reasons included past family connections with the brewery company, or contact with an appropriate executive within the company.

7.353 Future aims

Tenants were questioned about their future ambitions, but whether the responses were indicative of carefully planned business objectives or mere 'pipe-dreams' could not be assessed within the time available. Just over a half of the respondents had expansionary plans either for increasing their holding or 'trading-up' to a more profitable or 'better class' public house, and five of these aimed to become independent owners of free-houses. Just under a half were content with the status quo or planned to retire.

7.36 Financial Investment and Performance of Tenants

7.361 Capital Investment

Tables 7.12 and 7.13 reveal the wide variation in initial and cumulative capital investment by tenants ranging from £500 to almost £20,000 in the first instance, and up to nearly £30,000 as cumulative outlay. The median average for initial investment of £3,050 and £4,125 for cumulative investment shows a relatively small capital contribution by tenants. Variations in extent of outlay were due to a number of factors including the size,
Table 7.12  
INITIAL CAPITAL OUTLAY OF TENANTS OR "INGOINGS"
Including sums payable for fixtures, fittings, equipment, security deposit.

<table>
<thead>
<tr>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 1,000</td>
<td>3</td>
</tr>
<tr>
<td>1,050 - 5,000</td>
<td>14</td>
</tr>
<tr>
<td>5,050 - 10,000</td>
<td>6</td>
</tr>
<tr>
<td>10,050 - 15,000</td>
<td>-</td>
</tr>
<tr>
<td>more than 15,050</td>
<td>1</td>
</tr>
</tbody>
</table>

Source: Interviews with tenants.

Table 7.13  
CUMULATIVE CAPITAL OUTLAY OF TENANTS
Including "ingoings" plus expenditure incurred in premises, equipment, fixtures and fittings.

<table>
<thead>
<tr>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 5,000</td>
<td>13</td>
</tr>
<tr>
<td>5,050 - 10,000</td>
<td>5</td>
</tr>
<tr>
<td>10,050 - 15,000</td>
<td>2</td>
</tr>
<tr>
<td>15,050 - 20,000</td>
<td>1</td>
</tr>
<tr>
<td>20,050 - 25,000</td>
<td>2</td>
</tr>
<tr>
<td>more than 25,050</td>
<td>1</td>
</tr>
</tbody>
</table>

Source: interviews with tenants.
location, and market potential of the licensed premises, the state of decor and maintenance, and the amount and value of the equipment, furniture and stocks of liquor and other supplies. Also the amount of deposit required by different breweries of different tenants (often varying within the same brewery) ranged from £25 to £1,500 reflecting changing policies and inflationary trends.

7.362 Revenue

An estimate of the gross annual revenue of tenants is provided in Table 7.14, based on the responses from tenants. No validated accounts were shown to the researcher, and thus the figures should be treated with caution. Over one-third of the respondents stated or signified that these figures differed from those given for income-tax assessment or to the brewery company (being in several instances significantly in excess of the amount declared). Gross revenue per tenant (and family where applicable) ranged from £30,000 to £160,000 in 1976, with a median average of nearly £81,000.

7.363 Payments to Brewery

Mention is made elsewhere (14) of the system of payments by tenants to their brewers normally involving a fixed 'dry' plus a varying 'wet' rent, and of the difficulty of quantifying the latter payments (15). Table 7.15 provides a breakdown of tenants' responses concerning the amount of 'dry' rent paid. Such payments ranged from £570 per annum to £5,200 in respect of any one public house, or nearly £14,000 per annum paid by one tenant with a long lease. The median average per house
Table 7.14

<table>
<thead>
<tr>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>26,000 - 50,000</td>
<td>5</td>
</tr>
<tr>
<td>51,000 - 75,000</td>
<td>5</td>
</tr>
<tr>
<td>76,000 - 100,000</td>
<td>5</td>
</tr>
<tr>
<td>101,000 - 125,000</td>
<td>5</td>
</tr>
<tr>
<td>126,000 - 150,000</td>
<td>1</td>
</tr>
<tr>
<td>more than 151,000</td>
<td>2</td>
</tr>
<tr>
<td>no response</td>
<td>1</td>
</tr>
</tbody>
</table>

* Estimated to nearest £1,000 by tenants, reflecting actual revenue (not necessarily disclosed) in 1976. Where tenants operated more than one public house the response includes the total revenue from licensed premises.
Source: interviews with tenants.

Table 7.15

'DRY' RENTS PAYABLE BY TENANTS TO BREWERIES **

<table>
<thead>
<tr>
<th>£ p.a. *</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 1,000</td>
<td>4</td>
</tr>
<tr>
<td>1,050 - 2,000</td>
<td>8</td>
</tr>
<tr>
<td>2,050 - 3,000</td>
<td>4</td>
</tr>
<tr>
<td>3,050 - 4,000</td>
<td>4 ***</td>
</tr>
<tr>
<td>4,050 - 5,000</td>
<td>1</td>
</tr>
<tr>
<td>5,050 and over</td>
<td>2 ***</td>
</tr>
<tr>
<td>no response</td>
<td>1</td>
</tr>
</tbody>
</table>

* to nearest £50
** an adjustment was made if figure was for rent and rates combined. Figures refer to 1976.
*** In the case of two tenants with multiple holdings, rents were included for all properties.

Note: two tenants with multiple holdings only responded with regard to their 'main' public house.
Source: interviews with tenants.
was approximately £1,800. Table 7.16 reveals the 'dry' rent as a percentage of estimated turnover and demonstrates the relatively low payments by tenants. These varied from 0.8% to 8.5% of turnover with a median average of 2.8%.

7.364 Pre-tax Profit

The caveats concerning revenue figures given by tenants are also applicable to pre-tax profit figures, and in addition a comparison of 'profit' per tenant is complicated by the different accounting treatment and practices of respondents. Variations were found in whether or not sums were set aside for depreciation, renovations and renewals prior to arriving at a pre-tax profit. Some tenants paid themselves and/or their relatives a nominal sum, whilst others drew a realistic wage as a manager or fees as a director before arriving at a profit figure. In addition, the practice of a substantial number of respondents of withdrawing 'extra pocket money' from the till was a further complication. Thus Table 7.17 can provide only a rough guide to tenant profitability. According to tenants their pre-tax profits ranged from £1,850 to £22,250 per annum (16), with a median average of £9,000. Table 7.18 shows that estimated pre-tax profits as a percentage of estimated turnover ranged from 3.5% to 17.7%, with a median average of 11%.
Table 7.16

'DRY' RENTS TO BREWERIES AS % OF ESTIMATED TURNOVER p.a. *

<table>
<thead>
<tr>
<th>% of turnover</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.1 - 1</td>
<td>1</td>
</tr>
<tr>
<td>1.1 - 2</td>
<td>4</td>
</tr>
<tr>
<td>2.1 - 3</td>
<td>8</td>
</tr>
<tr>
<td>3.1 - 4</td>
<td>5</td>
</tr>
<tr>
<td>4.1 - 5</td>
<td></td>
</tr>
<tr>
<td>5.1 - 6</td>
<td>2</td>
</tr>
<tr>
<td>6.1 and over</td>
<td>2</td>
</tr>
<tr>
<td>no response</td>
<td>2</td>
</tr>
</tbody>
</table>

* refer to notes for Table 7.14

Source: interviews with tenants.

Table 7.17

ESTIMATED ANNUAL PRE-TAX PROFIT OF TENANTS * **

<table>
<thead>
<tr>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than 2,000</td>
<td>1</td>
</tr>
<tr>
<td>2,000 - 5,000</td>
<td>4</td>
</tr>
<tr>
<td>6,000 - 10,000</td>
<td>8</td>
</tr>
<tr>
<td>11,000 - 15,000</td>
<td>4</td>
</tr>
<tr>
<td>16,000 - 20,000</td>
<td>2</td>
</tr>
<tr>
<td>more than 21,000</td>
<td>2</td>
</tr>
<tr>
<td>not stated</td>
<td>3</td>
</tr>
</tbody>
</table>

*Normally tenants withdraw a salary or 'living expenses' from the takings for themselves and/or the working members of the family. Pre-tax profit is after such drawings, but depreciation is not usually provided for.

**Estimated to nearest £1,000 by tenants, reflecting actual pre-tax profits (not necessarily declared) in 1976. Where tenants operated more than one public house the response includes the total pre-tax profit from licensed premises.

Source: Interviews with tenants.
Table 7.18

<table>
<thead>
<tr>
<th>ESTIMATED PRE-TAX PROFIT OF TENANTS AS % OF ESTIMATED GROSS REVENUE *</th>
</tr>
</thead>
<tbody>
<tr>
<td>%</td>
</tr>
<tr>
<td>Less than 4</td>
</tr>
<tr>
<td>4.5 - 8</td>
</tr>
<tr>
<td>8.5 - 12</td>
</tr>
<tr>
<td>12.5 - 16</td>
</tr>
<tr>
<td>16.5 and over</td>
</tr>
<tr>
<td>no response</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

* Based on estimates of tenants, refer to previous notes to Tables 7.14 and 7.15.

Source: Interviews with tenants.

Table 7.19

<table>
<thead>
<tr>
<th>LENGTH OF TENURE AND NOTICE OF TERMINATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>Length of Normal Tenure</td>
</tr>
<tr>
<td>------------------------</td>
</tr>
<tr>
<td>year to year</td>
</tr>
<tr>
<td>three years</td>
</tr>
<tr>
<td>long lease</td>
</tr>
<tr>
<td>indefinite</td>
</tr>
<tr>
<td></td>
</tr>
</tbody>
</table>

* by either side

** 1 brewery offered an optional 3 year, 1½ or 1 year contract.

*** some breweries offered long leases to selected tenants.

Source: standard tenancy agreements, interviews with brewery representatives and tenants.
7.4 CONTRACTUAL AND FINANCIAL TERMS OF THE AGREEMENT

Each of the twelve brewery companies had a standard tenancy agreement which governed the terms of the arrangement with tenants. Though varying in some aspects these contracts were basically similar in content and presentation and appeared to have been modelled on the specimen form of tenancy agreement suggested by the Brewers Society (17). All were primarily concerned with protection of the brewer's interests and centred on the tenant's duties and obligations and the brewer's rights. Scant reference was made to the tenant's rights and brewer's obligations. Indicative of this imbalance was the number of clauses relating to the obligations of each party: up to forty per contract regarding tenants' obligations and a maximum of four in any one agreement relating to brewers' obligations. In one agreement there was no mention of a single duty or obligation on the part of the brewer.

In addition to this inequitable allocation of obligations and rights, all agreements were phrased in legal terminology (thus rendering difficult the easy comprehension of terms), and were not constructed in a manner which made readily apparent the respective commitments of each party.

Provisions within contracts were normally grouped under such sub-headings as: Terms of letting; Terms of Trading; Conduct of Business; Compliance with the Law and Public Interest; Termination; Arbitration and Definitions. However, a different classification is adopted here to provide a clearer picture of the various responsibilities and areas covered by the agreement.

7.41 Duration of Tenancy, Notice of Termination

Table 7.19 shows that the majority of tenants interviewed had a three year period of tenure, whilst half the brewers responded that it was their practice to allocate tenancies for one year only. This discrepancy may indicate a sample bias in that the tenants interviewed (who were likely to have been more amenable or more vocal in their requirements) enjoyed better terms than those generally applying. Two thirds of the tenants and two thirds of the brewers stated that a twelve month
period for notice of termination was the normal current contractual arrangement. Although this was in theory applicable to both sides, in practice a tenant was often allowed to give less notice, it being against the brewery's interest to enforce an unwilling tenant to remain, thus affecting sales and customer relations. A few contracts referred to extension periods allowed to tenants.

7.42 Payments to Brewery
All tenants were fully cognizant of the traditionally accepted practice of a dual method of payment made to breweries in the form of a fixed rental sum, termed a 'dry' rent, and of a sum calculated as a premium on supplies, termed the 'wet' rent, which varied with the size of orders placed. However, no specific mention of the latter form of payment was found in any of the tenancy agreements examined. Wording relating to prices of supplies tended to be such as 'prices equivalent to those charged to other tenants in the area'.

7.421 'Dry' Rent

The amount of dry rental payments were usually (but not always) included within the contract (18), as were terms concerning timing of such payments (varying from 1 month in advance to quarterly in arrears). Tenants were unaware of the specific basis upon which rental calculations were made and brewery executives were not keen to impart this information either to tenants or to the researcher. Different brewers appeared to have different criteria, though how formalized these were was discovered in only one instance (19). Indications were that one or more of the following criteria were normally used:
(a) required return on capital value of property
(b) repayment for cost of maintenance and repairs
(c) reasonable rental for tenant's quarters
(d) rental linked to rateable value of premises
(e) standard % on estimated gross turnover
(f) standard % on estimated pre-tax profit (before rent)

Even where a formula was specified at least one imprecise factor (such as the capital employed (20), or estimated revenue, or pre-tax profit), usually permitted latitude of decision and thus allowed some negotiating scope on the part of the tenants. Examples were given by tenants of substantial rent reductions which they had negotiated, either through submitting evidence or through misleading their brewery representative as to actual or potential financial hardship.

Several brewery executives acknowledged that they took into account the fact that tenants often understated their gross revenue and pre-tax profits, or overstated their costs, and made their calculations accordingly, using their managed houses as indicators of current levels of trading. Brewers agreed that the calculation of a dry rent payment needed very fine judgement in order to ensure a reasonable return to the tenant for his labour without reducing his motivation to sell the product, or, as one representative put it, 'to keep the tenant smiling but still on his toes'. In practice, according to the brewers, the more viable tenanted houses often subsidised those with a weaker financial performance.

7.422 'Wet' Rent

Whether or not 'wet' rent was paid by tenants on liquor supplies was an issue that was difficult to determine. Most tenants suggested that a 'wet' rent was retained in all but name, and thus thought they were charged a premium over and above free trade prices.
Ten of the twelve brewery executives claimed that no premiums were charged to tenants on wines and spirits; seven stated that beer was sold to tenants at free trade prices. As it was common practice to allow extra discounts to free trade outlets (eg. for immediate cash payment or extra large orders which minimized handling costs), no assessment was possible as to whether prices to tenants were truly comparable to free trade prices. The discrepancy in answers from brewers and tenants is shown in Table 7.20 and indicated either a widely differing policy of each brewer to different tenants, or (more probably) suggests a different interpretation put on 'free trade prices' by the two parties. In respect of prices charged to tenants for wines and spirits, several contracts included reference to 'local market prices' or 'prices of leading wine merchants in the area'. But the abolition of resale price maintenance (21) has made difficult any definition of 'local' or normal prices within the market place, and tenants interpreted 'free trade prices' as the lowest price at which supplies were available (for instance including a loss leader offer on a branded liquor product at a discount store or supermarket).

Three of the major breweries recently abolished price discrimination between free and tied trade outlets, the most recent move by any one of them giving an indication of the premium formerly charged (22).

 Contracts normally included provisions concerning the frequency and timing required for payments for supplies, with harsh terms against those tenants who did not comply.

7.423 Deposit

Most brewers required a deposit from tenants, usually equivalent to one or two weeks supplies of liquor. Depending upon the period when a tenant entered into an arrangement with his brewer, the sum required for deposit varied extensively (tenants of long standing not normally being asked to increase their deposit to keep pace with inflation). Interest was normally payable upon such deposits.
TABLE 7.20

Prices at which Liquor was Purported to be Sold to Tenants

<table>
<thead>
<tr>
<th></th>
<th>Response of Brewery Representative</th>
<th>Response of Tenant</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Beer at:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Free trade prices</td>
<td>7 *</td>
<td>4</td>
</tr>
<tr>
<td>Tied trade prices</td>
<td>5</td>
<td>20</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td>24</td>
</tr>
<tr>
<td><strong>Wines, spirits at:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Free trade prices</td>
<td>10 **</td>
<td>7 **</td>
</tr>
<tr>
<td>Tied trade prices</td>
<td>2</td>
<td>17</td>
</tr>
<tr>
<td></td>
<td>12</td>
<td>24</td>
</tr>
</tbody>
</table>

* Despite one brewery executive's response, the company's standard tenancy agreement stated otherwise.

** Of which three specified that discounts were available in respect of large quantities.

Source: Interviews with brewery representatives and tenants. Examination of standard tenancy agreements.
7.43 Obligation of Tenants

7.431 Compliance with Licensing and Other Law

Considerable emphasis was placed in the agreements on the duties and obligations of tenants to ensure that the Justices' License to the premises was not endangered either by contravention of the Law or by any administrative omission for re-application for, or transference of such licenses by the tenant or to a successor. Brewers stipulated their right to intervene in such matters in order to maintain the currency of such licenses. In addition clauses placed the obligation upon tenants to ensure continuance of legal title to the property and prohibited various activities within the licensed premises such as gaming or immoral activities or illegal trading practices such as dilution, adulteration or substitution of one product for another.

7.432 Tie on Supplies

All contracts contained strict provisions relating to a tie to the tenant's brewery on supplies of beer, wines and spirits and in two instances to minerals, fruit juices and cigarettes as well (23) Such a tie to the brewer or to subsidiary companies was fundamental and any breach of these terms was considered to be a material breach of the agreement and sufficient justification in most cases (unless special circumstances permitted) to terminate the contract (24).

7.433 Protection of Brewery's Image

Emphasis was placed in all agreements upon the tenant's obligations to supply drink (and usually also food), and to provide service and general amenities to the public. Clauses related to such aspects as courtesy, hygiene and general decor, and to the prohibition of amusement machines or the playing of music without prior specific approval from the brewery. Provisions were also included stipulating that the licensed
premises should remain open during the maximum permitted hours. Some agreements required tenants to take out third party insurance against public or employer's liability. Other clauses that were commonly included related to the promotion of the brewery's products and name (e.g. a continuous display of brewery products and night time illumination of the brewery sign) and to the protection of the immediate environment (e.g. no parking of caravans on the property).

7.434 Conservation of the Licensed Property

Most contracts contained provisions requiring the tenant to be responsible for internal redecorations and general maintenance of specified facilities such as drains, car park and grounds etc. Included in contracts were clauses forbidding alteration of the premises without approval from the brewer, clauses relating to the insurance of the property, and necessitating the tenant to give first option to the brewer to purchase any fixtures and fittings that he wished to sell.

7.435 Other Obligations

Most contracts contained clauses requiring tenants to sell liquor (and sometimes food) at 'reasonable' prices, and some contracts stipulated that tenants should respect such selling prices as stated from time to time by the brewery, usually but not always with reference to maximum prices in the public bar.

Agreements usually also obliged tenants to allow access by a brewery representative to the premises in order to inspect the building and to test and sample products; and to permit a prospective tenant to view the premises. Some contracts included clauses stipulating that certain books and records should be available for inspection by the brewery, and some tenants were obliged not to disclose confidential information relating to the brewery or the particular public house.
Obligations were frequently imposed upon tenants in respect of their personal circumstances, such as a stipulation to reside on the premises at all times, not to leave the premises for more than twenty four hours without permission, to retire at sixty or sixty five years, to vacate the tenancy within two weeks of widowhood (in one agreement), not to undertake any other concurrent business, and not to enter into competitive trade for a specified period subsequent to termination of the agreement.

Further obligations upon tenants included the necessity for reporting immediately to the brewery any complaints or legal actions in respect of the tenant or licensed premises. Most agreements also precluded tenants from assigning the tenancy to another party, and expressly denied the right to payment for goodwill.

7.44 Rights of Tenants
Express rights of tenants were few. Most tenancy agreements stated that tenants had the right to quiet enjoyment of the property during the period of the agreement. Allied to this was the stated or implied right to the provision by the brewer of suitable premises (including landlord's fixtures and fittings), in an adequate initial and continuing state of repair and decoration.

A specific right to the continuity of supply of liquor products was accorded to tenants in only two agreements, and was hedged with the proviso that in certain circumstances (such as an industrial dispute), the brewer could not be held responsible for a lack of such supply.

Whilst there was no reference found to a tenant's right to terminate the agreement upon a breach of conditions by the brewer, most contracts mentioned the tenant's right, upon receipt of notice from his brewer to terminate the agreement, to seek arbitration through the medium of 'the Panel' (25) at a local or national level.
Obligations of Breweries

Being the mirror image of tenants' rights, the express obligations of breweries were few. Most agreements referred to the brewer's responsibility for external repairs and redecoration of the licensed premises and for structural alterations, though such clauses were usually imprecise and, for example, excluded specific reference to the frequency of repainting.

Mention has already been made of the few instances where breweries assumed (with provisos) a contractual obligation to maintain continuity of supply of liquor products. Not expressly stated, but normal to such arrangements, was the brewer's obligation to offer a reasonable selection of the brewer's own beer, wines and spirits and other products (if these were tied), together with a reasonable choice of 'national' brands (i.e. products that enjoyed wide-spread national popularity) as well as the brands of other brewers with whom reciprocal arrangements had been made.

Traditionally expected of brewers by tenants, but not a contractual obligation, was the availability of advice and assistance of a general and specialized nature. This was expected primarily through the medium of intermediate management such as district managers and, to a lesser extent, through formal training sessions and material published by the breweries.

There was an expectation on the part of both brewers and tenants (but not a contractual obligation) that each brewery would maintain the marketability of its branded liquor products and of its total brand image (i.e. the overall image of its public houses) through market research, advertising and promotion and through the development of new products and facilities. Also expected was the provision of promotional aids to tenants such as branded beer mats, ash trays etc.
Rights of Breweries

An outline of brewers' rights has already been made in the context of tenants' obligations. Thus tenancy agreements accorded brewers the right to control the supply of all or most liquor products, in some cases to control the selling price of such products, to control the operating hours of the tenanted house and to lay down certain conditions relating to the tenants' personal and business behaviour. In addition brewers retained the right of access to tenanted property including the admission of their representative to inspect the premises and to sample the products, and to advise on or stipulate compliance with specifications for the external and internal environment of the public houses.

In the contracts of two breweries, the brewers maintained the right to insist on tenants completing an initial training course prior to commencing the tenancy.

Most agreements included the brewer's right to give three month's notice to terminate a contract, should a tenant commit a material breach of his agreement.

Summary of Obligations and Rights of Two Parties

A summary of the respective responsibilities and rights of brewers and tenants is provided in Table 7.21, analysed according to their operational, financial or legal nature.

Performance by Breweries

Difficulty was encountered in measuring the brewers' performance towards tenants, for several reasons. In contractual terms, few obligations upon brewers were included in most tenancy agreements and those that were stated tended to be in broad terms only. Many of the services expected of brewers by tenants were customarily provided, but were not formal obligations and thus were without definition. The intangible nature of some of the services rendered, made difficult a precise qualitative or quantitative assessment. However, a broad assessment has been made, based on the responses of both tenants and brewery representatives.
Table 7.21

Summary of Generally Obtaining Responsibilities and Rights of Parties to Tenancy Agreement

**Brewer:**

**OPERATIONAL Responsibilities**
- To provide premises, and certain specified equipment (landlord’s fixtures and fittings) in a condition suitable for the public sale of alcoholic liquor and other products.
- To maintain specified parts of such building and equipment throughout the tenancy.
- To supply on a continuous basis, alcoholic and other liquor ordered by the tenant from the brewer.
- To provide advice and assistance in respect of operating problems, promotional matters etc.

**FINANCIAL Responsibilities**
- To provide all or major part of capital for licensed premises and some equipment.
- To provide funds for certain renovations etc. to premises.

**LEGAL Responsibilities**
- Towards customers, tenants and tenant’s employees in respect of the provision and maintenance of the building’s structure to required standards of safety and hygiene.
- In respect of supplies, complying with the required standard as signified by their description.

**Tenant:**

**OPERATIONAL Responsibilities**
- To provide the service on a continuous basis of liquor and other products in compliance with the terms of the tenancy agreement including the purchase of all or specified liquor products from brewer.
- To hire and train staff to provide such services.
- To provide certain equipment (tenant’s fixtures and fittings) necessary for the smooth operation of the unit (eg. drinking glasses).
- To maintain the premises and specified equipment (including cellar equipment) in good working order, and to be responsible for the redecoration etc. of specified areas.

**FINANCIAL Responsibilities**
- To provide small proportion of initial capital (for tenant’s fixtures and fittings) and to supply working capital. To pay rental on a continuous basis, as agreed in contract.
- To pay for supplies from brewery, including a premium on supplies (where applicable).

**LEGAL Responsibilities**
- To obtain, maintain current, and respect the provisions of a Justices’ License. To assume full operating responsibility including public and employer’s liability (except in respect of that enjoyed by brewers).

**Rights**
- To operate the licensed premises as a semi-independent business, having the right to determine (within brewery-imposed limits) the liquor products for sale (usually), the selling prices of such products, all food products and prices without restraints, staffing matters, operating procedures, day-to-day administration, the environment of the premises (within limits) and the particular market aimed at (within constraints of location etc.)

**Rights**
- To make a profit or bear a loss (providing that the above responsibilities have been met).

**Rights**
- To quiet enjoyment of tenancy for the duration of the agreement.
- To performance by the brewer of contractual obligations contained within tenancy agreement.
A wide variation was found in the state of repair of the licensed premises visited during the survey. This was partly attributable to the different stage each had reached in its redecoration cycle, and partly attributable to the wide discretion allowed to most brewers by the terms of their agreements with tenants in respect of the timing and extent of capital expenditure to be undertaken by breweries in each case. Without such specifications or guidelines, tenants were often unable to exact performance from their brewers in situations which they, the tenants, considered to merit attention.

Complaints from tenants about their brewery's non-performance in these matters have been separated into two kinds. The first type of complaint centred on structural defects or other problems causing major operating difficulties or hazards to customers, which had not been rectified by breweries despite a representative's attention being drawn to them. The second type of complaint from tenants revolved around the rejection or lack of action by breweries to improve the image of the premises by repainting or implementing structural alterations, so that trade could be boosted or minor operating difficulties eliminated.

Conflict was likely between the two parties if such a situation was prolonged, but particularly so in respect of the first type of complaint which not only was likely to affect the tenant's revenue (and personal profit) but also to endanger his employees and customers. Whereas some tenants rectified such situations themselves at their own expense, (rather than endure a prolonged wait for brewery action), others were precluded from doing so by the provisions of their tenancy agreement.
7.512 Supply of Liquor

No substantial instances were given of breweries not providing adequate supplies of liquor in normal circumstances. Tenants were for the most part satisfied with the quality and quantity of products delivered. However, at such times when supplies were disrupted or inadequate (such as during industrial disputes or in unusually hot weather), tenants pointed either to the total lack of contractual obligation of their brewery to supply or the 'escape' clause negating such contractual obligation in such circumstances. The lack of the brewery's responsibility to supply, combined with the continuing responsibility of the tenant to serve liquor to customers and the accompanying prohibition (in some cases) to purchase supplies from outside the brewery tie, was a situation which demonstrated the imbalance of power between the two parties. Thus some tenants had the choice of losing revenue at such times (and possible losing disappointed customers unable to purchase their preferred brand of liquor), or risking the termination of their tenancy agreement by committing a fundamental breach of terms in purchasing supplies outside the brewery tie (26).

One contract provided an acute example of a tenant's possible untenable position, by including the following three consecutive provisions: an obligation upon the tenant to buy all non-food products from the brewery; prohibition on buying any liquor outside the tie, even when the brewery was unable to supply; and a stipulation on maintaining adequate supplies at all times.

7.513 Provision of Advice and Assistance

All brewery companies within the survey employed intermediate management (who were variously termed, but more frequently called district managers). Their primary role, according to brewery representatives, was a controlling one (i.e. to ensure that licensed premises were being managed in an appropriate
manner), and secondary role was to advise and assist licencees through their own experience or by channelling queries or problems to appropriate group management and specialist advisers. Their tertiary role was as a promoter of brewery-produced or other products.

The availability of district managers to tenants was assessed by the frequency of their visits, and by the span of their control, although no assessment could be made of the quality of their performance or of the proportion of the time spent in their advising capacity as opposed to their controlling or promotional roles. Table 7.22 provides information given by responding brewery representatives and tenants in respect of the normal frequency of visit by district managers to tenants. It indicates that according to tenants, such visits occurred less frequently than was thought or planned by breweries.

Table 7.23 provides an indication of the span of control of district managers, ranging from those with responsibility for between 31 and 50 public houses to those with more than 150 on-licensed premises. The wide variation in such spans was attributable to a number of factors. In some areas of the country it was normal practise for visits by district managers to be supplemented by visits from cellar and quality control inspectors with appropriate responsibilities; in those circumstances the narrower responsibilities of district managers resulted in their being allocated a larger number of houses under their control. In some breweries, visits to tenanted premises by senior management and/or specialist advisors were fairly frequent, and thus gave additional support to the district manager in his advisory role, enabling a wider span of control to be given him. Variations in the spans of control were also a function of whether a district manager had responsibility for tenanted houses only, or for a joint portfolio of managed and tenanted houses. Where the former was the case, the district manager was allocated a larger number
Table 7.22  Visits by District Manager* to Tenant

<table>
<thead>
<tr>
<th>Frequency of Visit</th>
<th>Response from Brewery</th>
<th>Response from Tenant</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 x per week</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2 weeks</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>3 - 4 weeks</td>
<td>5</td>
<td>4</td>
</tr>
<tr>
<td>4 - 5 weeks</td>
<td>2</td>
<td>6</td>
</tr>
<tr>
<td>less frequently</td>
<td>2</td>
<td>10</td>
</tr>
<tr>
<td>no response</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td></td>
<td><strong>12</strong></td>
<td><strong>24</strong></td>
</tr>
</tbody>
</table>

* or other intermediate level brewery representative by whatever name.

Source: Interviews with brewery representatives and tenants.

Table 7.23  Span of Control of District Managers *

<table>
<thead>
<tr>
<th>No. of Licensed Premises</th>
<th>Frequency in Respect of Tenanted Pubs Only</th>
<th>Frequency in Respect of Managed and Tenanted Pubs</th>
</tr>
</thead>
<tbody>
<tr>
<td>31 - 50</td>
<td>2</td>
<td>5 **</td>
</tr>
<tr>
<td>51 - 70</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>71 - 90</td>
<td>2</td>
<td>1 ***</td>
</tr>
<tr>
<td>91 - 110</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>111 - 130</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>131 - 150</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>151 - 170</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td><strong>8</strong></td>
<td><strong>6</strong></td>
</tr>
</tbody>
</table>

* Or other intermediate level brewery representative by whatever name.

** Where both tenanted and managed public houses were together supervised by one manager, his portfolio usually included some twenty five per cent of managed houses to seventy five per cent tenanted houses.

*** In this instance managed houses accounted for some ten per cent of the portfolio.

**** In two cases, brewery executives provided examples of normal spans for district managers supervising (1) tenanted houses only and (2) having combined portfolios. Thus N = 14, not 12.

Source: Interviews with brewery representatives.
of houses. The span of control of district managers was further influenced by factors of geographical distribution of the units under their control and their size and complexity. No detailed comparison could be made without a close assessment of all these factors, but there was seen to be a marked difference in the amount of contact between certain brewers and their tenants.

Responses from tenants indicated that, in the main, very little use was made of district managers as advisors or channels through which advice and assistance might be obtained. Most regarded their district management as being younger and less experienced than themselves and subject to a considerable turnover. Visits by district managers were regarded by tenants primarily as courtesy calls (with a secondary function as promoters and distributors of brewery products and point of sale merchandise). Little or no advice was apparently sought or given in respect of catering, food purchasing or the provision of accommodation facilities, though most of the responding breweries had access to such expertise within their own group services or those of subsidiary companies. The main area in which advice was requested and given was in respect of plans and designs for alterations to the interior of licensed premises.

Formal training was provided by two of the responding breweries to all new tenants, having been implemented recently as a compulsory training programme. Such training was given in the context of the brewery's right to exercise control but simultaneously was an obligation upon the brewery to provide such services. In five other breweries such facilities had been, or were stated to be, in the process of being established, and being optional to tenants were offered in the context of a brewery service. Few of the responding tenants had received such initial training from their brewery (it being a comparatively new development) and few had attended seminars or refresher courses on aspects of public house operation. In general very little written information was provided
by breweries to their tenants. No examples of operating manuals were traced and only one brewery produced a comprehensive catering manual for the guidance of tenants. In most cases tenants reported that the only literature they had received had been leaflets about the maintenance of cellar equipment.

7.514 Marketing Services

Because the role of breweries to maintain the marketability and brand image of their liquor products and licensed outlets was not defined in contractual terms but merely expected by brewers and tenants, no precise assessment could be made of the extent to which they complied with these expectations. Neither could the effects of brewery expenditure upon market research, advertising and promotion and development of liquor products and outlets be isolated in respect of tenanted interests.

In broad terms, however, whilst all brewers were aware of the need to adapt their liquor production to market demands (primarily for the brewery's own benefit and indirectly to the advantage of tenants), some breweries evidenced a greater awareness of the need to adapt licensed premises, or a greater capacity to implement such adaptation, than did other responding companies. Likewise, there was found to be a considerable variation amongst breweries in the attitude towards, and implementation of branding of premises. Whilst some brewers stipulated that only approved 'house' colours could be used for external walls, doors etc., and that external lettering on signs and walls should meet brewery standards of type, size and colour, other brewers placed no such restrictions on tenants. Some tenants were required to display three-dimensional signs to immediately identify the owning-brewery; others were not. No evidence was found of stipulated internal branding.
Although most of the responding breweries offered no advice to tenants in respect of catering activities and did not attempt to enforce standardized menus, portions or prices, several breweries provided for display by tenants standardized signs and placards which were specifically designed to promote food sales.

Inter and intra company variation was also found in the availability to tenants of promotional items such as branded beer mats, ash trays, drip-cloths and internal signs. Where district managers had a combined responsibility for directly-managed and tenanted houses, a number of tenants suggested that such supplies (as well as the manager's time) would be allocated first to directly-managed outlets (over which the district manager held direct responsibility) and only subsequently to tenanted houses (for which the district manager was not directly accountable).

7.52 Performance by Tenants
Due to the greater precision with which tenants' obligations were laid down, an assessment of the extent to which they complied with their contractual terms was easier to make than was the case with the breweries.

7.521 Compliance with Law

No evidence was collected of contravention of the licensing law by respondents, although some tenants acknowledged substituting cheaper brands of certain products in place of well-known and more expensive brands, thus contravening the Trades Description Act.

7.522 Tie on Supplies

Though regarded by breweries as the second most serious breach (after placing the license in jeopardy), a significant proportion of tenants acknowledged or indicated that they frequently or occasionally bought liquor from sources other than their own brewery or subsidiary outlets. Despite such an action, if proven, being sufficient cause for termination of the agreement, both brewery and tenant respondents acknowledged that this was not an uncommon practice.
Three main reasons were suggested by tenants for this evasion of terms: supplies from discount and similar stores were frequently cheaper than via the brewer; unrecorded purchases and thus unrecorded sales did not attract income tax; because tenants believed 'dry' rents to be based mainly on sales turnover (calculated on the basis of supplies ordered) the resultant reduction in the volume of orders placed with breweries was perceived to produce a proportional reduction in 'dry' rent.

Whilst most responding breweries allowed tenants to select minerals and fruit juices from sources of their own choice, or to choose from nominated brands or suppliers, and whilst most tenants were permitted freedom of choice of wines and spirits from their brewer's list, there was a tendency, according to brewery and tenant respondents, to encourage the sale of house brands by offering discounts on such products. A number of tenants stated that they normally selected a high proportion of house brands and suggested that their buying loyalty to house wines, spirits and minerals etc. had been or would be rewarded by preferential treatment from their brewer.

7.523 Other Operating Conditions

Responding tenants were found to commit a number of breaches of their agreed terms relating to operating conditions. Though regarded as less serious than the above-mentioned breaches, they were still sufficient in some agreements to warrant termination. Instances of non-compliance with contractual obligations included habitually not opening the licensed premises for the maximum permitted hours, using the premises for additional business purposes, having additional concurrent business interests, being absent from the premises without permission for more than twenty-four hours, or allowing more adult dependents to reside on the premises than was permitted.
Tenants tended to view such restrictions as petty regulations which applied to areas over which the tenant should use his own discretion, and therefore in the main felt justified in contravening such terms. Brewery representatives suggested that such actions might jeopardize the license, adversely affect the image of the premises (and thus affect the brewery's reputation), and reduce the volume of trade (and thus the wholesale margins of the brewery).

7.524 Compliance with Financial Obligations

No significant instances were reported of tenants who did not comply with their initial and continuing obligations to provide a small proportion of the capital investment (i.e. tenant's fixtures and fittings), working capital (i.e. a deposit) or subsequent payments for 'dry' rent and for supplies including (where applicable) a 'wet' rent. However, some instances were found where tenants had not performed their obligations to maintain or renovate such areas of their licensed premises as were their contractually defined responsibility. The extent of compliance with the initial and continuing financial obligation was mainly due to the dominant position of the breweries, which required a tenant's financial commitment prior to or at the time of signing each tenancy agreement, and which enabled supplies of liquor to be withheld if debts to the brewery were not settled in accordance with agreed terms.
CHAPTER 8
FRANCHISING

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8.1 INTRODUCTION AND METHOD

8.11 Parameters of Survey
Within the parameters of the total survey, franchising (as defined in Chapter 3) was found to exist in two main sectors: that encompassing hotels, motels and guest houses, and that including restaurants, cafes and similar establishments supplying food for consumption on the premises. In addition, franchising was found to be used amongst outlets selling meals and snacks for consumption off the premises (i.e. 'take-away' outlets). Therefore, this part of the survey was carried out in respect of systems for the operation of hotels, restaurants and take-away units.

Research was centred on franchised units within Britain, established by both British and foreign franchisors, with additional reference made to the overseas interests of British-based franchisors. To enable future trends to be suggested, account was also taken of the extent of, and policies relating to the overseas franchised interests of those foreign franchisors currently operating in Britain or negotiating the establishment of a franchise system within this country.

Information was obtained, where available (and indicated thus in the text) from participants in former franchise systems or such systems which were planned but never came to fruition. It was used to gain additional perspective on the reasons for failure or non-initiation of such systems, and on the motivations and attitudes of parties during the life cycle of their involvement in franchising (i.e. from initial negotiating stage through growth and maturity to termination).

Although franchising has been defined at length elsewhere in this study, in practise some contractual arrangements similar to franchising required closer investigation before they could be distinguished as franchising proper, or as arrangements
involving marketing consortia, co-partnerships or management incentive schemes. Therefore, interviews were carried out with a number of participants in such schemes.

To determine whether the arrangements between individual hotel owners and consortia of independent members joining together for a number of functions (such as marketing, purchasing and exchange of technical and managerial advice) should come within the classification of franchising, an assessment was made as to whether members made exclusive use of their consortium's branding, and as to their economic interdependence and the degree of control exercised over members. None of the existing arrangements between consortia and their members were found to include exclusive branding under the consortium's name and image, together with a significant degree of interdependence and a close control over, for example, operating policies and procedures, tariffs and menus. Thus all were excluded from the main section of this survey.

The interests of one British company in hotels operated under a joint venture scheme were excluded from this study, being distinguished from franchising on the basis previously outlined, (1).

The operation by three hotel and restaurant companies of management incentive schemes or management licence schemes were closely examined. These schemes involved the granting of a licence to operate an hotel, or restaurant including the building, contents and grounds, for a specified period to (in two cases), hotel and restaurant managers formerly directly-employed within the organisation; and (in the other case) later extended to include those not previously employed by the company. Upon acceptance of such an arrangement, the incentive manager (2), provided the working capital (or was loaned part of such capital by the company) and assumed responsibility for, and total participation in, the operating profit or loss of the business. An agreed rental was paid to the company, which retained responsibility for capital investment and overall policies of operation. Such an arrangement most closely resembled the tied-house system in the financial and operational roles undertaken by the two parties, though in none of the
three examples did it involve such a significant tie on supplies. Despite differing from franchising in that the incentive manager did not contribute all or the major part of the capital required for the business, this arrangement was deemed to incorporate a sufficient number of elements essential to franchising to be included within this section of the study.

8.12 Methodology
As in a previous section of this survey, some difficulty was encountered in distinguishing between franchised and non-franchised hotels, restaurants and take-away outlets, there normally being no external means of identifying the status of each unit. Some companies held themselves out to be only, or mainly franchisors, in which case there was no problem in identifying the franchisor, though (in some instances) there still remained the difficulty of distinguishing franchised from directly-owned units, or (in the case of hotels) from those under management contract.

Eleven companies (two of which had separate operating divisions responsible for different franchise systems) were found to be operating within the parameters of this survey, and were responsible for sixteen franchise systems (3).

Interviews were conducted with representatives from twelve of the thirteen franchisor companies or operating divisions (4) who were also requested to supply copies of their standard franchise agreements and of their promotional literature aimed at prospective franchisees.

Originally, it was intended that two franchisees should be selected per franchise system, to provide a check on information given by the franchisor and to give an indication of franchisees' attitudes and demographic features. However, a departure was made from this to permit interviews with franchisees who were perceived to be of a fundamentally different type. Multiple franchisees were seen to embody different
characteristics, aspirations and bargaining strengths vis a vis the franchisor to those of single franchisees, and were thus interviewed in addition to the latter.

A total of thirty-eight franchisees were selected for interview, including both multiple and single franchisees, two of the latter category being master franchisees and each responding in respect of two separate franchise systems of which they were members. Multiple master franchisees were questioned in detail on one system only, and in more general terms about their overall franchise interests. Only their detailed replies concerning one system are included with the main statistical data of this chapter, thus making a total of forty responses for analysis.

The multiple franchisees were selected, bearing in mind factors of geographical representation, size and length of relationship with their franchisor, because of their known involvement with a particular franchisor. Single franchisees were chosen mainly on a random basis, though for reasons of restricted time and funds available, such franchisees were selected mainly within the geographical boundaries of the South East of England. Within such constraints single franchisees were chosen at random from telephone directories and from franchisor's lists of franchisees. Six franchisees were the only representatives of such a status within their particular franchise system. Some multiple franchisees were master franchisees.

Interviews were also held with former franchisors and franchisees of franchise systems, and with representatives of two companies that had actively considered becoming franchisors. Three prospective franchisors were also interviewed and literature obtained from five franchisors intending to operate in Britain.
8.2 PROFILE OF RESPONDING FRANCHISORS

8.21 Ownership and Trading Interests

Franchisors varied considerably in the overall size of their company, extent of involvement in the hotel and catering industry, in the size of a particular system in which franchising occurred, in the extent of their franchised interests, and in whether they were single or master franchisors. Table 8.1 shows the origin of franchise companies and systems and reveals the American background of three companies and of a further two franchise systems, subsequently taken over by British companies.

Nine of the eleven franchisors were wholly or mainly involved in hotel and catering activities (though not necessarily wholly or mainly involved in franchising). Of the sixteen franchise systems that were examined, four related to hotels, nine to restaurants, and four to take-away outlets, (one system incorporating both hotels and restaurants).

The two master franchisors operated a total of seven systems under their corporate umbrellas, though in each company there were two separate operating divisions concerned with one or more systems.

8.22 Dimensions of Systems Involving Franchising

Though this survey is essentially concerned with franchising within Britain or by British companies, Tables 8.2 to 8.5 encompass the overseas systems in which franchising occurs of those foreign companies within the survey, to demonstrate their extensive interests and significance in the franchising context. Thus the variation in size between the systems is shown in Table 8.2 together with an indication of the contrast between the size of systems within Britain as against their world-wide dimensions. Systems thus varied between those with less than fifteen units to those with more than four thousand. In the British context, almost half the systems encompassed less than fifteen units; the largest system including between five hundred and one thousand outlets. In a world-wide context, half the systems encompassed more than one hundred units, and a quarter included more than one thousand.
Table 8.1  Summary of Status and Trading Interests
of Franchisors Within Survey

<table>
<thead>
<tr>
<th></th>
<th>No. Companies</th>
<th>No. Systems operated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of Franchisor Companies in Survey</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>Number of Franchisor Operating Divisions in Survey</td>
<td>13 *</td>
<td></td>
</tr>
<tr>
<td>Number of Franchise Systems examined</td>
<td>16</td>
<td></td>
</tr>
<tr>
<td>National origin of Franchisor Companies:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>British</td>
<td>8</td>
<td></td>
</tr>
<tr>
<td>American</td>
<td>3</td>
<td>11</td>
</tr>
<tr>
<td>Nationality of Innovator of Franchise Systems: **</td>
<td></td>
<td></td>
</tr>
<tr>
<td>British</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>American</td>
<td>5</td>
<td>16</td>
</tr>
<tr>
<td>Status of Franchisor Companies:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Conglomerates with interests not pre-dominately in hotel and catering industry</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Conglomerates with main interests in hotel and catering industry</td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Hotel and/or catering companies with main interests in activity being franchised (though not necessarily mainly in franchising method)</td>
<td>6</td>
<td>11</td>
</tr>
<tr>
<td>Classification of Franchisor Company:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Master Franchisor</td>
<td>2</td>
<td>7</td>
</tr>
<tr>
<td>Franchisor</td>
<td>9</td>
<td>11</td>
</tr>
</tbody>
</table>

Sector to which Franchise System Relates:
- Hotels 4
- Restaurants, Cafes etc. 9
- Take-away outlets 4

* In two companies with more than one franchise system, such systems were operated by two separate divisions, thus thirteen respondents were interviewed and in some cases reference is made to thirteen franchisors.
** refers to country in which the franchise system was developed as such.
*** 1 system incorporated both hotels and restaurants within the same operating division.
Table 8.2 Dimensions of Systems in Survey in Which Franchising Occurs *

<table>
<thead>
<tr>
<th>No. Units</th>
<th>In Britain</th>
<th>World-Wide **</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 15</td>
<td>7</td>
<td>3</td>
</tr>
<tr>
<td>16 - 50</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>51 - 100</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>101 - 250</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>251 - 500</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>501 - 1000</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>1001 - 2000</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>2001 - 4000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>more than 4000</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>15 ***</td>
<td>16</td>
</tr>
</tbody>
</table>

* includes total number of units within each system, including those franchised, directly owned and operated by franchisor or under management contract.

** includes the overseas interests of British and foreign companies within the survey.

*** 1 system was not represented in Britain, though owned by a British company.

Source: Interviews with franchisors, and company reports.

Table 8.3 Distribution of System Units grouped by Franchisor Within Survey * **

<table>
<thead>
<tr>
<th>No. Units</th>
<th>Per Franchisor In Britain</th>
<th>Per Franchisor World-Wide</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 15</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>16 - 50</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>51 - 100</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>101 - 250</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>251 - 500</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>501 - 1000</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>1001 - 2000</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>2001 - 3000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>3001 - 4000</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>more than 4000</td>
<td>-</td>
<td>11 **</td>
</tr>
</tbody>
</table>

* includes all units within each system, encompassing those franchised, directly-owned and operated or under management contract

** attributable (where appropriate) to master franchisor, therefore only eleven responses.

Source: Interviews with franchisors and company reports.
Table 8.3 reveals greater polarization in the size of respondents, when account is taken of their overall interests as master franchisors in systems including franchising. Thus the predominance of three franchisors is demonstrated within Britain, where their systems involved more than one hundred units, in contrast to the total system interests of six franchisors of less than fifteen units. On a world-wide basis, five respondents organized systems involving between 250 and 5000 units in contrast with six respondents whose systems included up to fifty units.

An assessment was attempted of the capital investment within each system, including both the franchisors' and franchisees' capital. No relevant published data were available and responses obtained during interviews were either obtained from, and applicable to, one franchisee's particular unit or units, or were obtained from each franchisor as an overall estimate of investment in their franchised system or systems (i.e. of their own and their franchisees' investment). Variations within each system of the age, geographic and market location of units, as well as in the method of calculating the capital investment, result in Tables 8.4 and 8.5 being indicative of the broad order of magnitude, rather than giving a precise assessment. In Britain the systems varied from one with less than a £100,000 investment to one involving between £25 million and £50 million. In a world-wide context, the range was between systems estimated to be worth less than £1 million to one of more than £2,000 million.

8.23 Extent of Franchised Interests
The actual extent of franchised units within systems in which franchising occurs is revealed in Table 8.6. As in relation to the overall size of systems, there was found to be a polarization between respondents. In Britain eight of the systems involved up to only fifteen franchised outlets, whilst three encompassed more than one hundred such units, the largest including more than six hundred franchised outlets. Six British systems included franchised units in overseas locations, two of these involving fifteen or fewer outlets, and three involving between 250 and some 1800 units.
Table 8.4

Estimated Total Capital Investment
in Units within each Franchised System in Survey*

<table>
<thead>
<tr>
<th>£</th>
<th>Systems in Britain</th>
<th>Systems World-Wide</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than £100,000</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>£100,000 to £1m</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>£1m+ to £1.5m</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>£1.5m+ to £2m</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>£2m+ to £5m</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>£5m+ to £15m</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>£15m+ to £25m</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>£25m+ to £50m</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>£50m+ to £100m</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>£100m+ to £1,000m</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>£1,000m+ to £2,000m</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>£2,000m+</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>15 **</td>
<td>16</td>
</tr>
</tbody>
</table>

* includes franchised and company-owned and operated units, but excludes head office and other assets.

** 1 system was not represented in Britain.

Source: Estimates based on information from franchisors, franchisees, promotional literature and company reports.
Table 8.5

Estimated Total Capital Investment in Units Within Franchised System: Grouped by Organizing Franchisor * **

<table>
<thead>
<tr>
<th>£</th>
<th>Organizing Franchisor in Britain</th>
<th>Organizing Franchisor World-Wide</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than £1m</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>£1m+ to £5m</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>£5m+ to £25m</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>£25m+ to £50m</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>£50m+ to £100m</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>£100m+ to £1000m</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>£1000m+ to £2000m</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>£2000m+</td>
<td>11</td>
<td>11</td>
</tr>
</tbody>
</table>

* includes all units within systems including franchised, and those directly-owned and operated.

** includes investment by franchisor and franchisees but grouped according to organizing franchisor.

Source: Estimates based on interviews with franchisors, franchisees, promotional literature and company reports.
### Table 8.6. Extent of Franchised Units Within Systems

<table>
<thead>
<tr>
<th>No. Units</th>
<th>Frequency Within Systems in Britain</th>
<th>Frequency Within British Systems Overseas</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 5</td>
<td>6</td>
<td>2</td>
</tr>
<tr>
<td>6 - 15</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>16 - 50</td>
<td>4</td>
<td>-</td>
</tr>
<tr>
<td>51 - 100</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>101 - 250</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>251 - 500</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>501 - 750</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>751 - 1000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1001 - 2000</td>
<td>16 *</td>
<td>6</td>
</tr>
</tbody>
</table>

* 1 system was not represented in Britain though owned by a British company.

Source: interviews with franchisors.

### Table 8.7. Ratio of Franchised: Total System Units

<table>
<thead>
<tr>
<th>% Total</th>
<th>Frequency in Systems in Britain</th>
<th>Frequency in Surveyed Systems in World-Wide Context</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 - 10</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>11 - 30</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>31 - 50</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>51 - 70</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>71 - 90</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>91+</td>
<td>15 *</td>
<td>16</td>
</tr>
</tbody>
</table>

* 1 system not represented in Britain

Source: interviews with franchisors + company prospectuses.
Within the parameters of the survey there were calculated to be almost 4,000 franchised outlets, of which more than 70% were situated overseas but organized by British companies. Of the 1100 or so franchised units within Britain, 90% were organized by two franchisors. The predominant British franchisor was responsible for four systems (three of which were operated by one division of the company), (5), some three-quarters of all franchised units in Britain, and a slightly larger proportion of British franchised units overseas.

The ratio of franchised: total system units varied greatly within systems, from being 7% to almost 100%. Four systems within Britain involved less than 30% franchised outlets, whilst five involved more than 90%. Within the systems surveyed in a world-wide context (i.e. including the overseas interests of those foreign franchisors within the study), half the systems involved more than 70% franchised units (See Table 8.7).

An estimation of remuneration received on a continuing basis by franchisors proved difficult. No published data were available and few companies were able to provide (or felt inclined so to do) separate figures relating to royalty payments or to their mark-up on supplies to franchisees, or could isolate figures out of a total rental received. The various main methods of remuneration found amongst responding franchisors are given in Table 8.8. Table 8.9 provides a broad estimate (based on interviews and desk research) of the main payments made to franchisors on a-continuing basis, in respect of units in Britain and of overseas interests of British franchisors.

A total of some £7.25 million pounds was estimated to be the amount receivable from royalty payments and mark-ups. A further £1.1 million pounds was estimated to arise from rental payments (though no account has been taken of amounts attributable to rates or as a return on the franchisor's investment in such properties).
Table 8.8

Main Method of Continuing Remuneration
to Franchisors Within Survey

<table>
<thead>
<tr>
<th>Method</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mark-up on Supplies</td>
<td>3</td>
</tr>
<tr>
<td>Royalty based on food and beverage revenue:</td>
<td></td>
</tr>
<tr>
<td>2 - 2½%</td>
<td>3 *</td>
</tr>
<tr>
<td>4%</td>
<td>2</td>
</tr>
<tr>
<td>5%</td>
<td>1</td>
</tr>
<tr>
<td>7½%</td>
<td>1</td>
</tr>
<tr>
<td>Royalty based on room revenue:</td>
<td></td>
</tr>
<tr>
<td>2½%</td>
<td>1</td>
</tr>
<tr>
<td>3 %</td>
<td>1</td>
</tr>
<tr>
<td>4 %</td>
<td>1</td>
</tr>
<tr>
<td>Rental payment</td>
<td>4</td>
</tr>
</tbody>
</table>

1 franchisor had recently increased the royalty % from 2½% to 4%.
As far as could be ascertained, most franchisees were still paying 2½%.

1 franchisor had two separate systems for payment, either through a royalty or fixed rental, depending on whether the operator was a franchisee or management licensee.

Source: Interviews with franchisors and franchisees.
Table 8.9
Estimated Value of Main Continuing
Remuneration to Responding Franchisors p.a. *

<table>
<thead>
<tr>
<th>Royalty and Mark-ups</th>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 10,000</td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>11,000 - 25,000</td>
<td></td>
<td>3</td>
</tr>
<tr>
<td>26,000 - 125,000</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>126,000 - £m</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>£m+ - £m</td>
<td></td>
<td>2</td>
</tr>
<tr>
<td>£m+ - £m</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>£m+ - £m</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>more than 5 million</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>No estimate</td>
<td></td>
<td>2 **</td>
</tr>
<tr>
<td></td>
<td></td>
<td>13 ****</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Rental Payments ***</th>
<th>£</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>less than 25,000</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>26,000 - 50,000</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>51,000 - 150,000</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>151,000 - 250,000</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>251,000 - 550,000</td>
<td></td>
<td>-</td>
</tr>
<tr>
<td>551,000 - 750,000</td>
<td></td>
<td>1</td>
</tr>
<tr>
<td></td>
<td></td>
<td>4 ****</td>
</tr>
</tbody>
</table>

* 1976
** inadequate information available on mark-up of product.
*** Rental payments are recorded separately, from royalties or mark-ups on supplies, as they normally included payment for rates, and for return on capital. No separation of these amounts was possible.
**** The total of 17 reflects the two methods of payment current in one system (see Table 8.8).
Source: Interviews within franchisors and franchisees.
In addition to a royalty payment, a number of franchisors levied fees for advertising and (in the case of hotels) for reservations and associated services. As the advertising fees were in some cases retained under a separate account (and were not directly administered by the franchisor) or were claimed (as were reservation fees etc) to be a direct reimbursement of expenses, they have not been included in the above estimate.

8.24 Location of Franchise Systems
The areas in which franchise systems predominated are shown according to general region and type of locality in Table 8.10. An indication is given of the present distribution of systems, though not necessarily the area in which franchised units were sited (as opposed to company-owned and operated units). Six systems were spread nationally (though in varying density, and not always being represented in all the main regions) and six were predominantly sited in London and the South East. The majority of restaurant and 'take-away' systems were located in urban/high street areas.

8.25 Age of Franchise Systems
A range of some forty years in the age of the various hotel, restaurant and 'take-away' systems in which franchising occurs, is shown in Table 8.11, with a median average for the initiation of the systems falling between 1951 and 1960. This, however, relates to wherever the particular system was started, and not necessarily to Britain. A time span of only some twenty-five years relates to the establishment of systems in this country, one third of which were commenced after 1971, one third between 1961 and 1971 and one third between 1951 and 1961. Whilst being of interest in indicating the age of the various systems, Table 8.11 does not necessarily refer to the introduction of a franchising method of operation. Table 8.12 reveals that half the franchising activities currently in operation were commenced from 1975 onwards, and over two-thirds had been initiated since 1971. Franchising has been used for more than ten years in only two systems.
Table 8.10  Predominant Location of Units Within Systems *

<table>
<thead>
<tr>
<th>Area</th>
<th>No. of Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>London only</td>
<td>4</td>
</tr>
<tr>
<td>South East region</td>
<td>2</td>
</tr>
<tr>
<td>Midlands and East Anglia</td>
<td>1</td>
</tr>
<tr>
<td>Scotland</td>
<td>1</td>
</tr>
<tr>
<td>National **</td>
<td>6</td>
</tr>
<tr>
<td>Overseas</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>16</td>
</tr>
</tbody>
</table>

Predominant Particular Locality of Units within Systems

<table>
<thead>
<tr>
<th>Area</th>
<th>No. of Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Urban/high street</td>
<td>10</td>
</tr>
<tr>
<td>Trunk roads</td>
<td>4</td>
</tr>
<tr>
<td>Rural</td>
<td>1</td>
</tr>
<tr>
<td>Other</td>
<td>16</td>
</tr>
</tbody>
</table>

* includes franchised, directly managed and units under management contract

** not necessarily providing complete national coverage

Source: Interviews with franchisors.
Table 8.11  Age of Systems in which Franchising Method is Used *

<table>
<thead>
<tr>
<th>Year</th>
<th>Commencement of System in Britain or U.S.A.</th>
<th>SystemCommenced Operating in Britain</th>
</tr>
</thead>
<tbody>
<tr>
<td>before 1940</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>1941 - 1950</td>
<td>2</td>
<td>-</td>
</tr>
<tr>
<td>1951 - 1960</td>
<td>6</td>
<td>5</td>
</tr>
<tr>
<td>1961 - 1970</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>1971 - 1974</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>1975 -</td>
<td>16</td>
<td>15 **</td>
</tr>
</tbody>
</table>

* Note: this table reflects the age of the system and not necessarily the time at which the franchising method was introduced.

** 1 system not represented in Britain.

Source: Interviews with franchisors and franchisees.
Sawyer, Ray, Bib. ref (176).

Table 8.12  Initiation of Franchising Method Within System

<table>
<thead>
<tr>
<th>Year</th>
<th>No. Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>1951 - 1960</td>
<td>1</td>
</tr>
<tr>
<td>1960 - 1965</td>
<td>1</td>
</tr>
<tr>
<td>1966 - 1970</td>
<td>2</td>
</tr>
<tr>
<td>1971 - 1974</td>
<td>3</td>
</tr>
<tr>
<td>1975</td>
<td>4</td>
</tr>
<tr>
<td>1976</td>
<td>4</td>
</tr>
</tbody>
</table>

* 1 system not represented in Britain

Source: Interviews with franchisors and franchisees.
Whether or not the franchising method of operation was a planned, express method of development within these systems, or an ad hoc measure to overcome certain problems is indicated in Table 8.13, based on an assessment of responses during interviews with franchisors and franchisees. In eleven of the sixteen systems it appeared that planned development of franchising had occurred and in seven of these systems it was the sole or major method of distribution used.

8.26 Policy towards expansion of franchised outlets
In seven of the sixteen systems in which franchising occurred, the franchisor was assessed as having no plans for expansion through franchising within Britain, though two such British companies had plans for an increase in franchised units overseas. In six of the systems forecasts had been made for considerable expansion in Britain ranging from an increase in franchised units within one system of thirty outlets (an increase of 65% in franchised outlets) to predicted expansion of 100 to 200 units in other systems (being increases respectively of 100% and 1200% in franchised outlets). In three systems expansion through franchising was considered to be likely, but no quantified predictions were made.

8.27 Reasons for franchising
A number of reasons, or subsequently perceived benefits, were mentioned by respondents. The most frequently stated reason (and one to which most weight was given) was the advantage derived in market penetration. Not only did respondents point to a much quicker coverage of geographical area, but also to the possibility of penetrating a wider area than would be feasible using existing head office or regional managerial or advisory resources, to support wholly-owned and managed outlets. Such advantages were quoted in particular as reasons for entering into agreements with multiple franchisees who had a substantial existing regional presence or group facilities. As geographical coverage increased, there was a perceived geometric progression in overall purchasing by consumers of the products of the system, through increased exposure of products to a wider public, and greater availability of such products to brand-loyal customers travelling in different locations.
Table 8.13  Perceived Policy Amongst Surveyed Systems Towards Franchising

<table>
<thead>
<tr>
<th>Policy Towards Franchising</th>
<th>Frequency amongst Systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Expressly developed, or being developed as sole/major method of distribution</td>
<td>7</td>
</tr>
<tr>
<td>Planned and developed as one of alternative methods of distribution</td>
<td>4</td>
</tr>
<tr>
<td>Ad hoc method of management and/or distribution to solve problems</td>
<td>4</td>
</tr>
<tr>
<td>Policy uncertain</td>
<td>1</td>
</tr>
<tr>
<td>Source: Interviews with franchisors and franchisees.</td>
<td>16</td>
</tr>
</tbody>
</table>
Franchisors also stressed the benefits of franchisee-motivation which they considered would result from an individual having a direct financial interest in, and narrow span of control over, one or more franchised units. They were of the opinion that franchisees were better managers than those employed directly by the franchisor, and were more highly motivated to increase sales and to control costs of operation (such increase and costs bearing directly upon the franchisee's financial return), and in particular thought them more likely to control and not to participate themselves in irregular business practices. Franchisees were also thought likely to provide a better, personal service to consumers, such service having a long-term effect on their own profitability and contributing beneficially to the image of the entire system.

The reduction on the part of the franchisor for the need for capital through using the franchising method of expansion was mentioned by most franchisors, though with varying emphasis. Where the number of franchised units was small, and the amount of capital involved was not extensive (as for 'take-away' outlets or small restaurants), this was a relatively minor reason, or not even considered as a reason for franchising according to respondents. Where franchised chains were extensive and/or the capital requirement was great (as in hotels or large restaurants), this was an important aspect to franchisors. In such cases, not only did franchising provide a means for franchisors to make a relatively minor capital contribution, but was also a method of raising large amounts of capital that would not have been possible for a single company to achieve on its own, according to one respondent with extensive franchised hotel interests.

Linked to the minimal requirement for franchisor investment in units together with the transference to franchisees of operating costs, the consequent reduction in financial risk to the franchisor was an advantage mentioned by several respondents.
A few franchisors claimed that a major reason for their use of franchising was to benefit from the resultant availability of sites for expansion. It was suggested that individuals or companies with an existing site would be more willing to offer that site for development if they were able to participate in its operation and financial performance. Alternatively, it was claimed that the energies of those wishing to become franchisees of a particular system, could be harnessed with advantage to locate suitable sites or premises, thus covering a far wider geographical area than could otherwise be searched by the franchisor.

One respondent claimed that units within his particular restaurant system had been franchised mainly to cater for the personal development of former managers who had requested the opportunity to become more independent. The use of the franchising method was seen to be of benefit both to the former managers and to the system.

In summary franchisors perceived the disproportionately advantageous marketing, financial and operating results that they could achieve through franchising, with a relatively low capital investment, using relatively limited managerial and advisory resources.

8.28 Assessment of Franchisors' Significance
Reference has already been made to the wide variation in size and significance amongst responding franchisors. Such a variation is manifest in the extensive or very small overall business interests of respondents, in the size of systems in which franchising occurs, and in the extent of, and estimated value of franchised units. Whilst two franchisors dominate the British scene, and a third company of British origin has significant franchised interests overseas, the potential importance of some other respondents should not be ignored. A number of the systems have very recently been established; some franchisors of international standing and significance are barely, if at all represented in this country by franchised outlets. Their likely effect on other franchisors and on franchising per se is discussed elsewhere. (6)
8.3 PROFILE OF RESPONDING FRANCHISEES

8.31 Representativeness of Sample

As mentioned earlier, franchisees of both single and multiple status were interviewed, thus increasing the potential number of franchisee respondents. In addition, a few franchisees of special status were also interviewed (including a 'sub-franchisee' of a multiple franchisee, and two ex-managers of franchisor-owned units who by the loan of capital from their employer-franchisor and consequent purchase of units had been transformed into franchisees). But whilst such additional interviews increased the number of respondents, there was a simultaneous reduction caused by there being only one franchisee within certain systems who could be interviewed, because of his solitary status or of the parameters of the study or of the lack of time and funds for travel overseas.

Thus the responses obtained from the thirty-eight franchisees (totalling forty separate responses) provide greater exposure to some systems than to others, particularly the two predominant systems, in which the multiple franchisees and those mentioned above are members.

The thirty-eight franchisees controlled a total of 212 franchised outlets, which represented almost 20% of the known franchised hotels, restaurants and take-away outlets in Britain.

8.32 Extent of Franchisees' Holding

The range of holding of franchisees within the surveyed system is shown in Table 8.14. Over three-quarters of responding franchisees operated between one and five units, and two-thirds of these operated one unit only. The few franchisees with extensive interests in any one franchised system operated between twenty-one and fifty units each.
Table 8.14  Extent of Interests of Responding Franchisees within Systems Surveyed

<table>
<thead>
<tr>
<th>No. Units</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 unit only</td>
<td>23 *</td>
</tr>
<tr>
<td>2 - 5 units</td>
<td>10</td>
</tr>
<tr>
<td>6 - 10 units</td>
<td>2</td>
</tr>
<tr>
<td>11 - 20 units</td>
<td>2</td>
</tr>
<tr>
<td>21 - 50 units</td>
<td>3</td>
</tr>
</tbody>
</table>

* 2 single master franchisees have been included each with one unit within two separate franchise systems. The interests of multiple master franchisees have been ignored except in respect of the franchise system which was the focal point of the interview.

Source: interviews with franchisees.
The overall business dimensions of franchisees proved to be information that was unobtainable within the time and resources available (7). Instead an assessment was made of their status as to whether they could be described as multiple or single franchisees (8). Twenty-seven respondents (two of whom each had an interest in two separate systems) were classified as 'singles' and eleven as 'multiples' (see Table 8.15).

A further breakdown of the involvement of respondents is given in Table 8.16, which shows that sixteen of the thirty-eight franchisees had very close involvement with their franchised units. Five franchisees had the combined role of being owner-operators as well as employers of unit managers. Seventeen franchisees were in the role of employers with a varying degree of involvement as co-ordinators, but not normally operating the unit(s) themselves.

### 8.33 Location of Franchisees' Units

Due to the constraints of the sampling, franchisees' units were predominantly sited in London and the South East (a total of twenty-seven such units were visited and/or discussed). Three franchisees had units which were distributed on a national basis (though by no means an even coverage), and ten were located in various regions. (See Table 8.17).

More than half the franchised units were sited in urban or high street locations, and almost one-quarter were located in prime, city centre sites (see Table 8.18).
Table 8.15  Perceived Status of Responding Franchisees

<table>
<thead>
<tr>
<th>Status</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Single franchisee</td>
<td>27*</td>
</tr>
<tr>
<td>Multiple franchisee</td>
<td>13^</td>
</tr>
</tbody>
</table>

* includes two master franchisees with two units each.

Source: Interviews with franchisees, desk research

---

Table 8.16  Extent of Involvement of Responding Franchisees Within their Franchised Unit(s)

<table>
<thead>
<tr>
<th>Involvement</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Franchisee (or family) as unit operator (1 unit only)</td>
<td>14</td>
</tr>
<tr>
<td>Franchisee in 1 unit, family in other(s)</td>
<td>2</td>
</tr>
<tr>
<td>Franchisee in 1 unit, manager in other(s)</td>
<td>5</td>
</tr>
<tr>
<td>Unit managers employed, franchisee not operationally involved</td>
<td>17</td>
</tr>
</tbody>
</table>

* combined response for two single franchisees with 2 separate franchises

Source: interviews with franchisees
### Table 8.17

**Predominant Location of Responding Franchisees' Units**

<table>
<thead>
<tr>
<th>Region</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Greater London</td>
<td>17</td>
</tr>
<tr>
<td>South East</td>
<td>10</td>
</tr>
<tr>
<td>South West</td>
<td>1</td>
</tr>
<tr>
<td>Midlands</td>
<td>3</td>
</tr>
<tr>
<td>East</td>
<td>3</td>
</tr>
<tr>
<td>North</td>
<td>1</td>
</tr>
<tr>
<td>Scotland</td>
<td>2</td>
</tr>
<tr>
<td>National</td>
<td>3 *</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>40</strong></td>
</tr>
</tbody>
</table>

* not total coverage

Source: Interviews with franchisees.

### Table 8.18

**Predominant Location of Responding Franchisees' Units**

<table>
<thead>
<tr>
<th>Location</th>
<th>No. Franchisees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prime, city centre</td>
<td>9</td>
</tr>
<tr>
<td>Urban/high street</td>
<td>22</td>
</tr>
<tr>
<td>Trunk roads</td>
<td>6</td>
</tr>
<tr>
<td>Rural</td>
<td>3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>40</strong></td>
</tr>
</tbody>
</table>

Source: Interviews with franchisees.
8.34 **Duration of Franchisees' Status**

Sixteen franchisees had been of such status for less than one year - a situation that was partly attributable to the recent initiation of several systems or of the use of the franchising method. Table 8.19 reveals the variation in the length of franchise relationship, from less than one year to between 12 and 20 years (a tenure enjoyed by four of the respondents).

Only three franchisees had previously held a franchise to which they were no longer party.

8.35 **Demographic Features of Single Franchisees**

The age of franchisees ranged over some forty years, with almost half of them being between 31 and 40 (See Table 8.20). Two-thirds of respondents were British born (see Table 8.21). Ten of the twenty-seven franchisees had undergone tertiary education, and had been awarded degrees, professional status (through exams), diplomas or similar awards. Twelve franchisees had taken no school or subsequent exams. (Refer to Table 8.22).

Twenty-one respondents had been in a position of managerial or supervisory responsibility immediately prior to becoming franchisees; another four had owned their businesses and had been accustomed to taking policy decisions and controlling their units. Seventeen franchisees had previously worked in hotels, restaurants or in related activities (see Tables 8.23 and 8.24).

An analysis of the operational involvement of franchisees' families is given in Table 8.25. Seventeen out of twenty-seven respondents had the working support of at least one member of the family, and in almost half the total examples, this was full-time support.
### Table 8.19  
**Length of Involvement of Responding Franchisees in their Current System**

<table>
<thead>
<tr>
<th>Years</th>
<th>No. franchisees</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than one year</td>
<td>16</td>
</tr>
<tr>
<td>more than 1 year - less than 3 years</td>
<td>11</td>
</tr>
<tr>
<td>more than 3 years - less than 6 years</td>
<td>4</td>
</tr>
<tr>
<td>more than 6 years - less than 12 years</td>
<td>5</td>
</tr>
<tr>
<td>more than 12 years - less than 21 years</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: Interviews with franchisees.

### Table 8.20  
**Age of Single Franchisees * **

<table>
<thead>
<tr>
<th>Years</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>21 - 30</td>
<td>2</td>
</tr>
<tr>
<td>31 - 40</td>
<td>13</td>
</tr>
<tr>
<td>41 - 50</td>
<td>7</td>
</tr>
<tr>
<td>51 - 60</td>
<td>5</td>
</tr>
</tbody>
</table>

* includes only one reference to 2 single master franchisees.

Source: Interviews with single franchisees.

### Table 8.21  
**Nationality of Single Franchisees * **

<table>
<thead>
<tr>
<th>Nationality</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>British</td>
<td>18</td>
</tr>
<tr>
<td>West European</td>
<td>6</td>
</tr>
<tr>
<td>Turkish Cypriot</td>
<td>2</td>
</tr>
<tr>
<td>American</td>
<td>1</td>
</tr>
</tbody>
</table>

* includes only one reference to 2 single master franchisees.

Source: Interviews with single franchisees.
Table 8.22

<table>
<thead>
<tr>
<th>Educational Levels of Single Franchisees</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>No formal exams</td>
<td>12</td>
</tr>
<tr>
<td>C &amp; G exams</td>
<td>2</td>
</tr>
<tr>
<td>4 - 5 O'levels</td>
<td>3</td>
</tr>
<tr>
<td>HNC/diploma etc.</td>
<td>4</td>
</tr>
<tr>
<td>Degree/professional exams</td>
<td>6</td>
</tr>
<tr>
<td></td>
<td><strong>27</strong></td>
</tr>
</tbody>
</table>

* includes only one reference to two single master franchisees.

Source: interviews with single franchisees.

Table 8.23

<table>
<thead>
<tr>
<th>Most Recent Employment Status of Single Franchisees Prior to Franchising</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>top management/professional</td>
<td>7</td>
</tr>
<tr>
<td>middle, lower management, supervisory</td>
<td>14</td>
</tr>
<tr>
<td>skilled manual</td>
<td>1</td>
</tr>
<tr>
<td>entrepreneur/owner of business</td>
<td>4</td>
</tr>
<tr>
<td>housewife</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td><strong>27</strong></td>
</tr>
</tbody>
</table>

* includes only one reference to 2 single master franchisees.

Source: interviews with single franchisees.
Table 8.24
Most recent sector of employment of single franchisees prior to franchising

<table>
<thead>
<tr>
<th>Sector of Employment</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Restaurants, catering</td>
<td>12</td>
</tr>
<tr>
<td>Hotels</td>
<td>5</td>
</tr>
<tr>
<td>Administration business</td>
<td>3</td>
</tr>
<tr>
<td>Selling</td>
<td>2</td>
</tr>
<tr>
<td>Manufacturing, commercial</td>
<td>4</td>
</tr>
<tr>
<td>none</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>27 *</td>
</tr>
</tbody>
</table>

* Includes only one reference to two single master franchisees.
Source: interviews with single franchisees.

Table 8.25
Single franchisees' Family involvement in Franchised Unit

<table>
<thead>
<tr>
<th>Family involvement in addition to Franchisee Working full-time</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 member family working part-time</td>
<td>3</td>
</tr>
<tr>
<td>1 member family working full-time</td>
<td>8</td>
</tr>
<tr>
<td>1 working full time + 1 part-time</td>
<td>3</td>
</tr>
<tr>
<td>1 working full time + 2 part-time</td>
<td>1</td>
</tr>
<tr>
<td>2 working full time</td>
<td>1</td>
</tr>
<tr>
<td>no family involvement</td>
<td>11</td>
</tr>
<tr>
<td></td>
<td>27 *</td>
</tr>
</tbody>
</table>

* includes only one reference to two single master franchisees.
Source: interviews with single franchisees.
Those respondents classified as multiple franchisees were less easy to categorize, for several reasons. A few were not able or willing to discuss business interests other than relating to their franchised units. Because of the variation in size and type of ownership of hotel and catering interests (from several dozen take-away outlets to several dozen major hotels), a classification based solely on the number of units would not have been meaningful. An assessment of the capital value of their properties, or of the annual turnover derived from their interests was possible in only the broadest terms. Lastly, their non-hotel and catering activities were similarly difficult to assess. Therefore, a general overall classification has been made, taking into account numbers and types of units, and of estimated dimensions as employers, generators of turnover, and of the capital involved in their businesses. A final factor that was included in this assessment was the relative status and bargaining strength of the multiple franchisee vis a vis each particular franchise system (see Table 8.26).

Two multiple franchisees were of such status ab initio, and founded their business specifically to franchise with a particular franchisor. Another two commenced franchising some twenty years ago as single franchisees with one unit, and their growth to multiple status was through the acquisition of further franchised units within the same franchise system. One franchisee had undertaken such status as an alternative to a straight leasing situation in respect of one unit that was separate from but synergistic to the organization's main function. The remaining six multiple franchisees had interests in franchised outlets which were in the same spectrum of activity as their main businesses but proportionately small to such interests, and used as a means of initiating diversification into alternative catering or take-away activities.
<table>
<thead>
<tr>
<th>Classification</th>
<th>No. of Franchisees</th>
</tr>
</thead>
<tbody>
<tr>
<td>small companies</td>
<td>4</td>
</tr>
<tr>
<td>medium-sized companies</td>
<td>3</td>
</tr>
<tr>
<td>large companies</td>
<td>3</td>
</tr>
<tr>
<td>non-profit making association</td>
<td>1</td>
</tr>
<tr>
<td></td>
<td>11</td>
</tr>
</tbody>
</table>

**Note:** Classification was based on an assessment of the number of units, their size and approximate worth, and other interests of the multiple franchisee.

**Source:** Interviews with multiple franchisees, company reports.
8.37 Franchisees' Investment and Financial Performance
8.371 Investment

An assessment of the value of franchised units in terms of franchisees' original and subsequent investment or of market worth proved difficult. The few audited accounts that were available for inspection either did not provide figures that could be isolated in respect of the franchised units, or did not provide an adequate basis for comparison because of a variation in accounting treatment of, for example, depreciation or re-valuation. Responses from multiple franchisees of long standing indicated a wide variation in the initial and subsequent investment in their franchised units over a period of, say, twenty years. Factors of size of units, location and condition of the premises obviously influenced their value, but also of significance were inflationary trends in property prices and building costs. Instances were given of some recently established units costing more than twelve times comparable units belonging to the same franchisee.

Figures given in Table 8.27 are based mainly on franchisees' own assessment of the value of their investment and whilst providing a general indication, should be treated only as such. The range of investment from less than £2,000 to more than £1 million per unit reflected the nature of the arrangement as well as the type of unit involved. Thus, one franchisee obtained a restaurant as a going concern together with an adjoining business for no investment other than a substantial sum of working capital into the other business, and the obligation to make a continuing rental payment for the restaurant premises to the owner (not the restaurant franchisor). Such individual arrangements, including management licences were not representative of normal investment levels, however, which were almost all from £10,000 upwards, depending firstly on whether the unit was a take-away outlet, restaurant or hotel, and secondly on the particular investment required in each system and in each particular site. The modal and median average investment per unit fell between an estimated £10,000 and £20,000, the latter average being £14,000. Figures showing franchisees' investment in their particular franchised system indicate the multiple holding of some respondents, eight of which had investments of more than £100,000.
Table 8.27  Estimated Investment in Franchised Units of Responding Franchisees

<table>
<thead>
<tr>
<th>Total £ invested</th>
<th>Franchisee's Investment per Franchised Unit, frequency</th>
<th>Franchisee's Investment in franchise system, frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>No capital investment</td>
<td>5</td>
<td>5</td>
</tr>
<tr>
<td>less than 2,000</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>2,000+ to less than 10,000</td>
<td>5</td>
<td>2</td>
</tr>
<tr>
<td>10,000+ &quot; &quot; &quot; 20,000</td>
<td>15</td>
<td>9</td>
</tr>
<tr>
<td>20,000+ &quot; &quot; &quot; 50,000</td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>50,000+ &quot; &quot; &quot; 100,000</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>100,000+ &quot; &quot; &quot; 250,000</td>
<td>1</td>
<td>4</td>
</tr>
<tr>
<td>£m + &quot; &quot; &quot; 1m</td>
<td>-</td>
<td>2</td>
</tr>
<tr>
<td>1m + &quot; &quot; &quot; 10m</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>10m + &quot; &quot; &quot; 30m</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>no response</td>
<td>3</td>
<td>3</td>
</tr>
</tbody>
</table>

Source: interviews with franchisees

Table 8.28  Estimated Franchise Fees paid by Responding Franchisees

<table>
<thead>
<tr>
<th>£</th>
<th>Frequency of Fee paid per unit</th>
<th>Frequency of Total paid by Franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>no fee</td>
<td>15</td>
<td>15</td>
</tr>
<tr>
<td>1 - 250</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>251 - 500</td>
<td>8</td>
<td>7</td>
</tr>
<tr>
<td>501 - 750</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>751 - 1000</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1001 - 2000</td>
<td>3</td>
<td>-</td>
</tr>
<tr>
<td>2001 - 5000</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>5001 - 10,000</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>10,001 - 50,000</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>50,001 - 150,000</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>no response</td>
<td>6</td>
<td>7</td>
</tr>
</tbody>
</table>

Source: interviews with franchisees
8.372 Franchise Fees (9)

Based on responses from franchisees, Table 8.28 provides data on the initial franchise fees paid to franchisors. Almost one third of respondents stated that they had paid no franchise fees. Of these, some were multiple franchisees to whom, it seemed, the franchise fee had been waived because of their negotiating strength. Others had joined a system during its initial formation, and were not charged a fee; still others, as management licensees, were not asked to make any such initial payment. The variation in fees per unit, from less than £250 to more than £10,000, reflects the type of unit (from take-away outlet to hotel) and the relative strength of the franchisor.

8.373 Continuing payments to Franchisors (10)

The frequency of use of different methods of continuing payment by responding franchisees to their franchisor is given in Table 8.29, together with an analysis of the amount of royalties charged, and an estimate of rental payments as a percentage of turnover. No valid quantifiable information could be obtained in respect of surcharges made by franchisors on supplies as their main means of obtaining revenue from franchisees.

Not only was there a variation between franchisors in the amount of royalty levied (from 2 to 7½% gross turnover in the case of take-away outlets and restaurants, and from 3 to 4% room revenue in the case of hotels), and a wide variation in levels of rental payment (from an estimated 8.6 to more than 31% of turnover), but also in whether or not a separate advertising charge (of 3% turnover in one system) was levied, and whether such fees were paid directly to the franchisor or to a separate fund. Thus any comparison between the basic amounts levied must include any compulsory advertising or other continuing charges. Any assessment of the merits of different franchisors or of the different methods of payment needs to take into account whether group services such as advertising are included within the basic royalty, surcharge on product or rental payment, or whether an additional charge or charges are levied.
Table 8.29
Analysis of Continuing Payments to Franchisors
by Responding Franchisees

<table>
<thead>
<tr>
<th>Method of Payment</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Royalty on turnover</td>
<td>18</td>
</tr>
<tr>
<td>Surcharges on supplies</td>
<td>13</td>
</tr>
<tr>
<td>Fixed rental payment</td>
<td>9</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Royalty on Turnover</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount levied</td>
<td></td>
</tr>
<tr>
<td>2 - 2½% gross turnover</td>
<td>6</td>
</tr>
<tr>
<td>4% &quot; &quot;</td>
<td>8 *</td>
</tr>
<tr>
<td>7½% &quot; &quot;</td>
<td>2</td>
</tr>
<tr>
<td>3 % gross room turnover</td>
<td>1 **</td>
</tr>
<tr>
<td>4% gross room turnover</td>
<td>1 ***</td>
</tr>
<tr>
<td></td>
<td>18</td>
</tr>
</tbody>
</table>

| Estimated Rental Payments as % on Turnover ****. |
|---------------------------------|-----------|
| %                               | Frequency |
| 6 - 10                          | 2         |
| 11 - 15                         | 1         |
| 16 - 20                         | 1         |
| 21 - 25                         | 3         |
| 26 - 30                         | 1         |
| 31 +                            | 9         |

* plus enforced levy of 3% of turnover for advertising funds.
** plus enforced levy of 1% room revenue for advertising, plus other fees for reservations etc.
*** plus other fees for reservations etc.
**** includes payment for rates and franchisor's return on capital investment.

Source: Interviews with franchisees.
Certain problems precluded a detailed, accurate assessment of franchisees' gross revenue. Two-fifths of franchisees had been operating their franchised units for less than one year and consequently could not provide trading figures for a full year. This problem could not be solved by scaling up existing figures to produce an annual turnover, because of the seasonality of trading conditions and the unrepresentativeness (as a basis for forecasting) of results obtained in the initial months of a newly-established business. To overcome this problem to some extent, a comparison was made of franchisees' actual turnover to date with that predicted for the given period by the franchisor; on the basis of the proven accuracy or otherwise of the forecast, adjustments were then made to the predicted turnover for the first year. No attempt was made to adjust the trading figures of young businesses within their first few years of operation.

Not all respondents were willing to reveal the turnover or profitability of their units. Some who were hesitant about giving overall figures, were willing to state lowest/highest turnovers achieved by units within their multiple holding, or to give an 'average' figure for all units. Thus, the data in Table 8.30 provide an indication of the broad order of magnitude of turnover applicable to franchised units and to franchisees. They are drawn from a variety of indicators provided by respondents, only in a few instances are figures taken from validated accounts.

The wide variation of turnover from less than £15,000 per annum to more than £1 million pounds reflects the different interests of franchisees (i.e. take-away outlets, restaurants or hotels), but although the lowest figures relate to take-away outlets and the highest to hotels, there was considerable variation between the same type of units (eg. restaurants) and between units of the same system or of the same franchisee. An instance was given, for example, of a very successful take-away outlet of a relatively small size, whose turnover was in excess of that given for a hotel within the survey. The modal and median average per unit fell between a range of £45,000 to £70,000 per annum, with the median falling at approximately £62,000.
Table 8.30

Estimated Turnover per annum of Responding Franchisees in 1976

<table>
<thead>
<tr>
<th>£ p.a.</th>
<th>Frequency of Estimated 'average' turnover per unit</th>
<th>Frequency of Estimated Total turnover per franchisee</th>
</tr>
</thead>
<tbody>
<tr>
<td>11,000 to 15,000</td>
<td>1</td>
<td>-</td>
</tr>
<tr>
<td>15,000 to 20,000</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>20,000 to 45,000</td>
<td>6</td>
<td>2</td>
</tr>
<tr>
<td>45,000 to 70,000</td>
<td>15</td>
<td>11</td>
</tr>
<tr>
<td>70,000 to 100,000</td>
<td>10</td>
<td>5</td>
</tr>
<tr>
<td>100,000 to 150,000</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>150,000 to 200,000</td>
<td>-</td>
<td>3</td>
</tr>
<tr>
<td>200,000 to 500,000</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>£5m to £1m</td>
<td>1</td>
<td>3</td>
</tr>
<tr>
<td>£1m to £2m</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>£2m to £5m</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>£5m to £10m</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>no response</td>
<td>3</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td>40</td>
<td>38 *</td>
</tr>
</tbody>
</table>

* Only 38 responses are recorded, because the total turnover in respect of two systems per two single master franchisees is combined in each case.

Source: Estimates and some validated figures provided by single and master franchisees.
Also revealed in Table 8.30 is the range of total turnover enjoyed by the responding franchisees, varying from less than £20,000 to between £5 and £10 million pounds per annum. The highest turnovers were not necessarily a function of the size or type of unit (eg. hotel), or of the multiple holding of a franchise, although three of the four respondents within the ranges of £1 to £10 million were multiple franchisees. The modal average per franchisee was in the £45,000 to £70,000 range, with a median average of almost £77,500 per annum which reflected the multiple holding of a number of respondents.

8.375 Pre-tax profit

Tables 8.31 and 8.32 provide an indication of the pre-tax profits achieved by franchisees, though being based on responses from franchisees which were only substantiated by audited accounts in a few instances, and depending upon different accounting treatment for the statement of profits, they should be treated as giving a broad indication only. Some franchisees made no provision for payment of a salary to themselves, neither did they set aside amounts for depreciation. In the case of some multiple franchisees with their own head office, the given figures did not include an appropriate contribution towards their own administrative expenses.

The modal and median average fell between £10,000 and £15,000 per annum, the latter being just over £13,000. However, included within this range and the two adjacent ranges were a number of respondents who had not made provision for some or all of the above-mentioned payments before arriving at the given profit figure. Thus a lower figure would reflect more accurately the true situation. The same caveats must be made in respect of the estimated pre-tax profit percentage on turnover; the modal average of 16 - 20% profit on turnover and the median average of just over 13% reflect a lack (in nine of the fifteen instances where the percentage was greater than 12%) of appropriate deductions.
### Table 8.31
Estimated Pre-tax Profit of Responding Franchisees in 1976

<table>
<thead>
<tr>
<th>p.a.</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>£5,000 loss to break-even</td>
<td>5</td>
</tr>
<tr>
<td>£1 profit to £2,000</td>
<td>1</td>
</tr>
<tr>
<td>£2,000 profit to £5,000</td>
<td>-</td>
</tr>
<tr>
<td>£5,000 &quot; £10,000</td>
<td>5</td>
</tr>
<tr>
<td>£10,000 &quot; £15,000</td>
<td>8</td>
</tr>
<tr>
<td>£15,000 &quot; £20,000</td>
<td>4</td>
</tr>
<tr>
<td>£20,000 &quot; £25,000</td>
<td>2</td>
</tr>
<tr>
<td>£25,000 &quot; £50,000</td>
<td>3</td>
</tr>
<tr>
<td>£50,000 &quot; £100,000</td>
<td>3</td>
</tr>
<tr>
<td>£100,000 &quot; £200,000</td>
<td>1</td>
</tr>
<tr>
<td>no response</td>
<td>8</td>
</tr>
</tbody>
</table>

**Note:** 12 responses include a lack of provision for one or more of the following: franchisee's salary, depreciation on franchised unit, a proportional or total payment for franchisee's head office expenses.

**Source:** Interviews with single and multiple franchisees.
Table 8.32

Estimated Pre-tax Profit as Percentage of Turnover of Responding Franchisees in 1976

<table>
<thead>
<tr>
<th>% turnover</th>
<th>Frequency</th>
</tr>
</thead>
<tbody>
<tr>
<td>up to 2%</td>
<td>1</td>
</tr>
<tr>
<td>2 - 5</td>
<td>5</td>
</tr>
<tr>
<td>6 - 8</td>
<td>3</td>
</tr>
<tr>
<td>9 - 11</td>
<td>3</td>
</tr>
<tr>
<td>12 - 15</td>
<td>3</td>
</tr>
<tr>
<td>16 - 20</td>
<td>8</td>
</tr>
<tr>
<td>21 - 25</td>
<td>1</td>
</tr>
<tr>
<td>26 or more</td>
<td>3</td>
</tr>
<tr>
<td>no response/not applicable *</td>
<td>13</td>
</tr>
<tr>
<td></td>
<td>40</td>
</tr>
</tbody>
</table>

* not applicable because there was no profit.

Note: 12 responses include a lack of provision for one or more of the following: franchisee's salary, depreciation on franchised unit, a proportional or total payment for franchisee's head office expenses.

Source: interviews with single and multiple franchisees.
8.38 Number of Persons Employed in Franchisees' Units

No precise figures could be produced for the average number of employees per franchised unit or per franchisee. Seasonal variations together with fluctuating ratios within the same unit of full to part-time employees would call for a much more detailed survey than was possible within the time available or the expected levels of co-operation from respondents. An estimate was made, in broad terms only, of the total numbers employed in the 212 units of the thirty eight franchisees interviewed. Including the operational involvement of franchisees and their families some 4,700 persons were estimated to be employed on a full or part-time basis.

8.39 Attitude to Franchising

8.391 Reasons for Becoming Franchisees

A wide variety of reasons for (or subsequently perceived benefits from) franchising were put forward by responding franchisees, most of whom gave several reasons and attached varying degrees of weight to them. Two reasons were most frequently mentioned: the franchised system's brand image, and the product itself. Franchisees perceived significant benefits arising from their being able to display an established trade mark and brand image which, to brand-loyal and potential customers, embodied a package of food, drink, accommodation (where applicable), service and surroundings of an established standard. This 'instant' market created by displaying a system's symbol etc. was regarded as a major advantage of franchising by respondents. Secondly, the fact that a franchised product had demonstrably or presumably been used, tested and proved in a defined market (11) was a substantial advantage of which most franchisees were aware, realizing the significant savings in time and cost resulting from the use of a system, procedures and product that was evidently applicable to a particular market. Both single and multiple franchisees emphasized these two reasons for joining a franchise system, which in the case of multiple franchisees were usually the over-riding causes for their taking on such a status.
A third reason, given by most single franchisees and those multiple franchisees with no previous experience of hotel or catering activities was the substantial advantage arising from the technical and operational expertise available through franchisor group services and based on accumulated experience. According to respondents, they placed considerable value on advice, training and active participation by franchisors during the initial stages of planning and opening a franchised unit. Such value diminished as the franchisee gained experience in operating his own business, and was of less value in respect of each additional unit opened by the franchisee. The more complicated the unit, the more value on such benefits was placed by franchisees. Thus in the case of an hotel franchisee, with no previous experience of hotel operation, a major reason for becoming a franchisee was stated to be the package of technical and operational expertise provided by the franchisor in designing, equipping and organizing the hotel. In the case of 'take-away' outlets, less emphasis was placed on this aspect.

Importance was attached by a number of single franchisees to the perceived freedom which franchising permitted them in the operation of their units. They stated that they entered into a franchise relationship in part to escape from the constraints of working as salaried employees within a normal (i.e. non-franchised) large organization, and to avoid the continual 'interference' from line and advisory management.

Schedule 8.1 summarizes the above responses of franchisees together with a number of other reasons given for entering into a franchise relationship. Schedule 8.2 summarizes why respondents selected a particular franchise system.
The following reasons (or subsequently perceived benefits) were suggested by responding franchisees. No weighting is attached to these responses, except that those listed 1 - 3 were given predominance by most respondents.

1. Brand image of franchise system and resultant 'instant' creation of a market for every franchised unit.

2. Product that had been tried, tested and found to be applicable to a defined market and the resultant saving in time and costs that would be otherwise incurred in experimentation.

3. Technical and operational expertise available from franchisor group services, based on accumulated knowledge and experience.

4. Ensuing freedom from employee status and constraints of working within a normal (i.e. non-franchised) large organization.

5. Chance to obtain 'free' training and experience in operating a business, using the franchisor's 'umbrella' to reduce risk.

6. Leverage of franchisor's name to obtain venture capital.

7. Anticipation of greater profitability within the franchised system than as an individual entrepreneur or salaried employee.

8. In instances where the franchisor provided all or a major capital contribution to a franchised unit (as in management license agreements), the elimination of the requirements for such investment by the franchisee.
9. Advertising and sales promotion of the product and/or system on a continual basis by franchisor on a scale that would be impossible for individual franchisee to achieve.

10. In respect of hotels, access to a reservation and referrals system (in some cases on a world-wide scale) that would not be available to an individual entrepreneur, thus providing initial custom and acting as a future insurance policy.

11. Cheaper alternative to an hotel management contract.

12. Leverage of franchisor's name to raise selling prices to levels remaining acceptable to consumers.

13. Research and development by franchisor in relation to product ingredients, equipment and to the market on a scale that would be impossible for individual franchisee to achieve.

14. Reliable supply of competitively priced products (food, liquor and other items) of an established standard by or through the agency of the franchisor thus ensuring continuity of quality and supply. Reduction of time and costs expended in the selection and purchasing of supplies, reduction in the amount of stocks required to be held and therefore the amount of working capital. A lessening of risk of non-delivery of items as a result of industrial action (because of the franchisor's need to keep the system operating).

15. Expectation that if the franchisee or his family were temporarily unable to operate the unit (for example because of illness) the franchisor would provide relief management.

Source: interviews with single and multiple franchisees.
Summary of Responding Franchisees' Motivation for Joining their Particular Franchise System

1. Favourable assessment of particular product or system within a defined market
   - through external observation of units
   - through personal experience as former employee
   - through personal connections with other franchisees or franchisor.

2. Favourable assessment of franchisor's capacity to provide the necessary support to the system and its members
   - through external observation of units
   - through personal experience as former employee
   - through personal connections with other franchisees or franchisor.

3. Familiarity with the product and system (as a former line manager, advisor or employee) and thus greater confidence in ability to establish an independent business.

4. Non-availability of comparable alternative products or systems, or non-feasibility of manufacturing/establishing them, accompanied by a desire to enter the particular market.

Source: Interviews with single and multiple franchisees.
Franchisees were questioned about their immediate and long-term intentions in respect of the franchised system to which they belonged. Whether the responses obtained were the result of considered forward-planning, or were dreams that were unlikely to materialize, or were primarily intended to give point to previous answers to questions, had to be judged in each case.

Five respondents stated that it was very probable that they would terminate their franchise arrangement within a year, and two in fact have done so, since December 1976. These franchisees suggested that they would cease their particular type of trading activity and move into a new area of business.

Eight single franchisees indicated that their franchising interest was likely to alter in significance, and that instead of it being their major source of income and predominant activity, it was probable that other entrepreneurial interests would be concurrently expanded, and possibly ultimately supersede their franchised activity.

Sixteen franchisees said that they were content to remain within their present franchised system, eleven of these had no specific intention of expansion through additional units within the system, whilst five entertained such ambitions.

8.4 CONTRACTUAL AND FINANCIAL TERMS OF AGREEMENTS

All responding franchisors and franchisees were questioned in detail about the contractual and financial terms of their agreements. Standard or particular contracts were analysed (where available). Documents relating to thirteen of the sixteen systems were closely examined.

Contracts varied considerably in their comprehensiveness, and in the degree of restriction which they placed upon franchisees. All tended to emphasize the obligations of franchisees and rights of franchisors, and most included details of franchisor obligations to provide defined services. The layout and presentation of franchise contracts was fairly uniform, and
all included a substantial amount of legal terminology. None were drawn up in a manner that led to an easy assessment of the respective rights and obligations of both parties. Most contracts included a few definitions, the majority of which defined trade marks, systems and food products essential to a particular franchise.

8.41 Duration, Notice, Termination
The duration of franchise agreements varied from one to twenty years, with eleven of the sixteen systems having standard contracts for more than five years. Four of these were open-ended agreements (three with a minimum fixed initial period of five years). In one system, examples were encountered of terms varying from ten to twenty years: the more recent franchisees being offered the shorter term.

Renewal terms were often multiples of the original duration (i.e. 3 year renewals to follow 3 year initial contracts, 5 year renewals to follow 5 year contracts), although longer initial terms of, for example, 10 years, tended to have subsequent periods of five year agreements.

There was a variation in periods of notice that could be given, from 2 months to 9 months, normally relating equally to either party to the contract. However, in circumstances such as a material breach of the agreement, a few franchisors claimed that a franchise could be terminated in as short a period as 48 hours. In general, franchise contracts included very little detailed reference to renewals or terminations. (12)

8.42 Remuneration to Franchisors
In almost all systems, franchisors normally required two types of remuneration: an initial sum paid by the franchisee plus a continuing payment.
Initial payment was normally termed a franchise fee, but in some instances was labelled as 'reimbursement of franchisor's expenses'. This payment was viewed by franchisors as having the two-fold purpose of being a means of recovering particular initial expenses incurred by each outlet and contributing to the franchisor's general expenses arising from establishing the system, whilst also giving an indication of the franchisee's degree of commitment. Payment of such fees (which varied from less than £250 to as much as £20,000) was normally made either with an application for a franchise or upon signing a franchise agreement. In cases where franchise fees were extensive, payment was normally allowed over an extended period (13).

Despite the standard requirement of specific fees in several agreements, in practice variation was found between franchisees of the same system. This may have been attributable, in part, to the period to which an agreement dated (in some cases early franchisees of a system made no payment), and in a few instances, to the negotiating strength of a franchisee; where a second or subsequent unit was held by one franchisee, the fee was sometimes reduced proportionately or waived altogether. Management licensees and a few multiple franchisees reported that they had made no payment whatsoever for franchise fees.

Whether payment was made for area franchises (and whether such franchises were granted) varied between systems. In one franchise there was a common practise of franchisees being granted specific areas, in which they had the option to develop a specified number of units. Normally a standard franchise fee was paid in respect of the aggregate agreed number, thereafter an increasingly large proportion of the fee was refunded to the franchisee upon the opening of each franchise unit within the area by a specified date. If the option were not taken up in time the area franchisee lost his rights to the area and did not receive any further refund. In another franchise system there was no difference between a standard and area franchise fee (or franchise): the variation in terminology was merely a sales technique to encourage potential franchisees.
Franquisors received income through one or more of the following methods: a basic royalty calculated on gross turnover or (in the case of hotels) on gross room revenue; an additional royalty or fee to cover, for example advertising expenses, or reservation costs in hotels; a premium on supplies which were manufactured by or purchased through the franchisor; a fixed rental payment. Table 8.29 summarizes the frequency with which each method was used in the sample and the amounts or percentages found in arrangements involving payment by royalty or a rental. The timing of such payments was noted in franchise contracts, normally being (in the case of royalties) one or two weeks in arrears after the end of each month; or (in the case of rental payments) varying between one month in advance and one month in arrears. Where payment was a royalty on turnover, the seasonality of trading was reflected in such payments which rose or fell according to the levels of business. Where payment was by a fixed rental sum, some franchisors varied the agreed payments according to expected seasonal changes in trading.

No verifiable information was obtainable in respect of the three systems whose main payment to the franchisor was through a premium on supplies (14). The franchisors were unwilling to communicate on this aspect, whilst franchisees variously estimated a mark-up on wholesale prices of from 30% to 50% on certain items. No mention was made in the relevant franchise agreements of any such premium being levied. In two of these three systems franchisees were compulsorily supplied by the franchisor with all consumable and disposable products sold in the units. Thus premiums may have been added to all products or merely to the major items sold. In the third system, the franchisor applied a mark-up on certain food products which were the major sales items, and which compulsorily had to be purchased through the franchisor. No variation was traced amongst franchisees in the amount of premium charged to different respondents in respect of identical products. Thus, unlike the
situation relating to the franchise fees, there appeared to be no account taken of the relative bargaining strength of participants or the duration of each particular relationship; neither did the varying levels of product consumption or the size of deliveries seem to affect such premiums charged. Payment to the franchisor was either by cash on delivery or stipulated within a defined period.

In instances where a separate compulsory advertising levy was charged it was usually payable at the same time as the basic royalty. However, whereas the basic royalties were retained by the franchisor to offset administrative costs and to provide a profit, in some systems the advertising levy was separately treated. In such cases, a special fund was usually set up, and controlled either by a body representing both the franchisor and franchisees or by a separate agency. Advertising levies were found to be made upon all franchisees irrespective of their status or geographical location in such systems.

In one system, franchisees contracted to participate in a maximum of four special promotions per annum. Such promotions were estimated by the franchisor to cost the franchisee an additional 1% of gross revenue each year; this payment was sometimes referred to as a local advertising levy.

Additional levies were payable by some of the hotel franchisees within the survey. In two systems, one or more payments were required for group reservation facilities, central training resources, sales outlets or computer facilities, irrespective of the particular franchisee's use of such services. Payment was made either as a fixed amount per available letting room, or as a fixed percentage of room revenue. In another system, payment was linked to the franchisee's actual use of such services.
8.423 Additional Premiums on Supplies

Apart from some franchisors charging a premium on supplies to franchisees as a main source of income, some franchisees suspected their franchisors of obtaining additional revenue by this method. No thorough examination could be made of this claim, for reasons already stated, but one franchisor whose income was declared to be from a royalty payment also acknowledged the retention of a 3% premium on all purchases supplied to franchisees. A number of franchisees gave instances of equipment and signs supplied by their franchisor at prices which were significantly above those charged elsewhere for products which they claimed to be identical.

As some franchisors tied their franchisees to all or most food and liquor products, as well as to disposable items, cleaning materials, operating equipment and capital items such as fixtures, furnishings and cooking equipment, numerous opportunities existed for premiums to be added to items, or for franchisors to receive a discount from suppliers.

8.43 Obligations of Franchisees

To a large extent the obligations of franchisees mirrored the rights of franchisors, particularly in connection with four important restrictions on operation, including the source of supplies, type of product offered for sale, selling prices charged and hours of opening. Obligations placed upon franchisees were normally stated within franchise contracts, but in some systems the entire content of an operations manual was specifically included as part of the contract, thus making numerous detailed requirements into legally enforceable contractual obligations upon the franchisee.

8.431 Tie on Supplies

Although there was a wide variation in the extent to which franchisors tied their franchisees for supplies, such a restraint was fundamental in some degree to those franchise
systems involving take-away outlets and restaurants, though not to those involving hotels. The degree of tying within the first two types of units ranged from a complete tie on all consumable and disposable products and virtually all equipment, to one that related to only a few specified items of food and equipment. Within any one system there were frequently a number of arrangements permitting various degrees of freedom. For example, a franchisee might be tied to the franchisor (or a subsidiary company) for the supply of the main grocery, bakery and convenience food items; be directed to two or three nominated suppliers for frozen food, butchery products, disposable items and chinaware; and be given complete freedom of choice within overall guidelines of standards required for fresh fruit and vegetables and furnishing fabrics.

A number of contracts contained the proviso that franchisees might buy consumables, disposables or other commodities through alternative suppliers if the quality were equivalent to that required by the franchisor and if the price of such products were 'materially more favourable' than that charged by the franchisor or by a supplier stipulated or nominated by him. This freedom was not permitted, however, in respect of those systems or those products on which franchisors obtained their main revenue through imposing a premium, or on such products as were classified as being of a secret formula. Though some franchisors permitted freedom of purchase on certain items of equipment, in practice such freedom was nugatory there being no available alternative supply other than through the franchisor.

8.432 Tie on Product

Fundamental to all systems was some restriction on the product (i.e. the total product encompassing food, liquor, accommodation (where applicable), service and surroundings. However the extent of restrictions varied considerably between the types of unit and between the different systems. In general, the least restraint was placed upon hotel franchisees who, provided they respected overall policies of the franchisor, had considerable discretion over the component parts of the total product, for instance freedom to decide what items should appear on the menu.
At the other extreme were franchisees of take-away outlets or restaurants with very limited menus, some of which had no discretion whatsoever over menu items, portion sizes, methods of service nor over the internal decor of their unit. Such franchisees were regulated by detailed clauses in their contracts which, for instance, forbade the sale of other than standardized portions, of products in other than prescribed composite dishes, or of products which were not purchased from agreed sources. Some were forbidden to add a single additional food or beverage item to the menu, or to sell items such as cigarettes or confectionary, or to omit any stipulated items from their menus without prior consent from their franchisor.

In addition, one franchisor laid down a required minimum annual order of certain basic food items which if not complied with could result in the termination of the franchise. Others obliged their franchisees to add to their menus such extra items as they, the franchisors, thought fit, whether or not the franchisees deemed suitable the given items to their particular market circumstances and whatever the investment required or likely return upon it.

An overall assessment of responses from franchisors and franchisees and of such contracts as were available for analysis, suggested that four of the sixteen systems examined were very restrictive over the product, six allowed substantial latitude and six could be classified somewhere between the two extremes.

8.433 Tie on Selling Prices

Whilst some systems required franchisees to conform to franchisor pricing policy, others permitted complete freedom to system members. The tendency was for stricter control to be placed on take-away outlets and restaurants but for latitude to be allowed to hotel franchisees. Three systems permitted complete discretion to franchisees. Three allowed substantial price freedom but requested franchisees to consider recommended prices or to charge prices which were not significantly different from those in other franchised units.
in the system. In the other ten systems franchisees were obliged to respect pricing policy laid down by franchisors for all or specified menu items. Of these ten systems, five stated an exact price for all or most menu items; two stipulated a minimum and maximum level and three required franchisees to respect a maximum retail price for all products.

Certain exceptions were permitted within these strict pricing policies. One franchisor stated that adherence to pricing policy should continue only as long as the franchised outlet was making a profit. Some latitude was allowed on certain sundry items which were not fundamental to a system's image, and negotiations on prices were permissible within a few systems.

A few contracts contained clauses obliging franchisees not to impose extra charges, such as a service charge, without franchisor consent.

8.434 Tie on operating hours

Restrictions on operating hours were enforced by half the franchise systems, and discretion allowed in the other half systems. Because of the nature of their activity, hotels were not subject to any such restrictions. In some cases the operating hours of a franchised restaurant or take-away outlet were determined by third parties, such as landlords (as part of the conditions of a lease) or local authorities.

8.435 Initial Provision and Subsequent Maintenance of Premises and Equipment

Except in the case of management licence agreements, the provision by franchisees of premises acceptable to the franchisor was an essential part of the arrangement. The degree to which franchisees were obliged to obtain franchisor consent in relation to the suitability of the site, external structure and appearance of the building, internal structure, layout and decor, varied according to the different systems. Some franchisors obliged franchisees to observe detailed, strict
plans and specifications by submitting their own plans in advance either to the franchisor or to architects, designers, shopfitters etc. who had been approved by the franchisor.

Once approval has been gained and the unit had become operational, most contracts forbade franchisees from making any alterations to the structure or overall design of their units without franchisor approval.

Whilst all contracts touched upon the issue of the franchisee's responsibility for maintenance, repair, renewal or redecoration, the precision of such clauses and the strictness with which they were enforced varied considerably in the sixteen systems examined. Whilst some agreements merely required franchisees to maintain what (in their opinion) were reasonable standards of decor, others stipulated that franchisees comply with 'any reasonable request' by the franchisor for renovation or renewals. The necessity for agreements to be more specific on these matters was suggested by the recent introduction by one predominant franchisor, and the intended introduction by another major franchisor, of a separate agreement or additional clauses to this end.

8.436 Provision of Staff and Service

Not always stated within agreements but implied in each case was the obligation upon franchisees to provide themselves or through the agency of employees continuous service of an appropriate standard. Such phrases as 'efficient, courteous and high quality service' or 'competent, sober and reliable service' were used in some contracts, thus illustrating the difficulty of defining required standards of service. In three contracts franchisees were obliged to employ as managers of franchised units, only those who had been trained by the franchisor or by approved trainers. In a fourth contract a similar requirement was applicable to every member of staff who served the public with the franchised menu items.
Training was offered by some franchisors at special centres, either to franchisees themselves or to their managers or employees. Such training was optional (except in the above-mentioned instances) and in two systems a training fee was payable to the franchisor for such services. Normally, however, franchisees were expected to pay the salary and expenses of trainees but the training programme itself was a service included within the franchise 'package'.

Some contracts obliged franchisees to ensure the appropriate dress and conduct of their employees (for example, to wear given uniforms, not to smoke on duty or chew gum). In a few agreements, franchisees were forbidden to employ staff who had recently been in the employment of the franchisor or of other franchisees within the system.

8.437 Advertising, Promotion and Maintenance of the System's Image

In systems where an advertising royalty was compulsory franchisees obviously were bound to make a financial contribution to the advertising activity. Some systems required a defined amount of local advertising to be undertaken by the franchisee, but in most cases this was optional. If local advertising (through advertisements, literature or signs) were undertaken by franchisees, prior approval of the copy or of the type of sign was normally required by the franchisor.

In some franchise contracts, franchisees were obliged to actively participate in any promotional programmes organized by the franchisor, including the distribution of advertising material, point of sale merchandise, or the discounted sales of certain menu items.

Various degrees of tightness were found amongst franchise systems in the obligation upon franchisees to maintain the obvious identify of their unit as part of the franchise system. Whilst some franchisors required strict compliance with all standardized layouts and decor etc., others permitted (or
did not prevent) considerable variations in colours, furnishings, internal and external signs and fascia. (15) The display by franchisees of the system's trade mark through certain external and internal signs was usually an essential part of the arrangement, such signs being provided free by the franchisor or loaned throughout the duration of the agreement or purchased via the franchisor (and required to be relinquished upon termination).

8.438 Payment to Franchisor

All franchise contracts included clauses obliging franchisees to make defined payments to the franchisor at defined periods, including (where applicable) an initial franchise fee and one or more continuing payments. In some systems franchisees were obliged to reveal certain financial data to their franchisor, either through allowing access to their unit's books of account or by providing an independently audited statement. Information required by franchisors depended to some extent on the method by which they received payment from franchisees. Some franchisees were obliged to reveal their gross turnover; others to state the amount of the main raw food product ordered and subsequently sold (for example, number of chickens), the cost price of such products, selling price and names and addresses of suppliers.

8.439 Other obligations

A variety of other obligations of a legal and operational nature were usually included in contracts as well as conditions relating to termination.

Franchisees were required, in most agreements, to ensure that they had obtained all necessary planning consents, that they held legal title to the premises, that all rates and taxes were duly paid, that they complied with local legislation including (where applicable) licensing laws. Almost all contracts obliged franchisees to keep their unit(s) in an hygienic and tidy condition, and some specifically mentioned the relevant legislation with which they had to comply.
The majority of contracts obliged franchisees to obtain suitable insurance cover, and in some agreements specific reference was made to the type of cover (e.g. public liability) and sum to be insured. Often franchisees were required to insure with specified or well-known companies and to be willing to show their policy to the franchisor. Some agreements required the franchisee to indemnify the franchisor in the case of an action by a third party.

An operational obligation that was frequently placed upon franchisees was a complete adherence to the franchisor's operating manual, whatever amendments the franchisor thought fit to make and usually giving very short periods of notice of any such changes (in one case of three days). In two systems franchisees were required to respect the policy and other decisions made by groups of franchisee and franchisor representatives. Several agreements obliged franchisees not to permit music, gaming, entertainment or coin-operated machines on their unit's premises without specific authorization from the franchisor.

In some systems, obligations were placed upon franchisees not themselves to divulge any of the system's operating methods, formulae or trading figures and to be responsible for preventing their employees from so doing.

In a number of instances franchisees were obliged to devote their full-time working attention to their franchised unit or units, and were prohibited from undertaking any other business without prior approval from the franchisor. Most contracts forbade franchisees from assigning their franchised interests without prior consent from the franchisor.

Upon termination, some franchisees were prohibited from operating a similar business within a specified distance and within a specified time. If the franchised unit were sold to a buyer outside the franchise system, some contracts required franchisees not only to remove and return to the franchisor
all identifying signboards etc. but to undertake to remove any resemblance of the unit to the system. Thus some franchisees were obliged in those circumstances to redecorate internally and externally and to re-furnish and equip the unit at their own expense.

8.44 **Rights of Franchisees**

Attention paid within franchise contracts to the rights of franchisees was scant in comparison with that given to their obligations. Some rights were understood by both parties and implied within the agreements, but not stated, for example, a franchisee's right to financial sovereignty over his unit and thus his right to take a profit (or obligation to bear any loss).

Depending on the wording of agreements and on the existing attitude of both parties to an arrangement, some franchisees' 'rights' were in practice difficult to distinguish from franchisors' 'rights'. Thus the provision by the franchisor of group services to aid franchisees was often worded in contracts and viewed by franchisors as a means of retaining control over franchisees and the franchised product. Therefore certain 'services' in one system could be viewed as franchisee rights, and in another system as 'controls' or franchisor rights.

8.441 **Brand Image, Trade Mark, Special Formula etc.**

All contracts contained specific reference to the franchisee's right throughout the duration of the agreement to operate under the franchisor's brand image, using such trade marks and special formulae and procedures etc. as the franchisor incorporated within the franchised system. In some contracts detailed descriptions were given of particular products essential to the system's image.

8.442 **Area Exclusivity**

In only three of the agreements examined were franchisees accorded specific area exclusivity, such area either being described verbally in the contract or outlined on an appendaged
map. A number of franchisees were confident of the existence of a gentlemen's agreement with their franchisor which, franchisees maintained, precluded the establishment of another unit of the same system within their particular market area. Some claimed to have (unwritten) sovereignty over a certain area, for example a small town, or to have the (unwritten) right of first refusal of any projected franchised unit within their area. One franchisor customarily notified all franchisees of the location of every new unit within the system that had been sanctioned.

8.443 Termination

In only one agreement was the right accorded to franchisees to terminate should the franchisor breach a contractual obligation, and subsequently fail to remedy such within a specified time. In one other agreement, termination could be initiated by the franchisee if the franchisor went into voluntary liquidation or was judged to be bankrupt. No other contracts referred to franchisees' rights in such instances.

8.45 Obligations of Franchisors

These to some extent mirrored the rights of franchisees or, as mentioned above, were treated as franchisor rights. Franchisor obligations were classified into two main types: those relating to the implementation of the franchise concept to each franchised unit, and those relating to the period thereafter. Both the pre-opening and post-opening obligations were defined with varying precision in different agreements.

The pre-opening obligations essentially included the provision of a total 'business package' incorporating a branded product (i.e. complete product of food, service, environment etc.), advice and assistance in the construction alteration and decor of premises and advice and training in the operating policies and methods to be implemented in the franchised unit.
The post-opening obligations included the continuing provision of expertise in such areas as marketing (encompassing advertising, sales promotion, market research and product research), purchasing, technical advice and general business advice concerning operating problems.

8.451 Provision of Conceptual Formula

All franchise contracts referred to the obligation upon franchisors to provide (or the rights of franchisees to receive) detailed information and assistance towards the implementation of a franchised unit identical to, or comparable with the franchised concept. Normally such information was described in broad terms only within franchise contracts; but more detailed examples of advice and assistance were often given in promotional literature. Whilst some franchisors offered what amounted to a 'turn-key' operation (through undertaking responsibility for site location, selection, specifications for construction or alteration, design, inventories of equipment and consumables, and implementation of systems and procedures), other franchisors offered either a less defined concept or less assistance in its implementation.

Included as an essential part of the concept of the more standardized franchise systems was an operating manual incorporating a detailed breakdown of operating procedures, standards and controls. In systems where such manuals were provided, they represented the sum of the knowledge and experience of the franchisor, gained directly through the franchisor's directly-owned units or indirectly through franchisees.

8.452 Assistance in Opening Franchised Unit

All franchisors undertook to give some degree of pre-opening training to franchisees and/or their managers or employees. A wide variation was found amongst systems in the extent of training offered, ranging from one to two days to a maximum of thirty days. The type of training offered also differed from formal classroom instruction at training centres (in four systems), formalized on-the-job training at designated
units within the franchise network (in two systems) and on-the-job training at the franchisee's own unit. In some systems such training was compulsory, in most it was optional.

Almost all contracts obliged franchisors to provide assistance during the opening period of each franchised unit, but detailed descriptions of such assistance were few.

8.453 Provision of Marketing Expertise and Assistance

Though held out by franchisors, and expected by participants in franchising, that marketing advice and assistance was an inherent part of the benefits of joining a franchise system, few agreements contained more than broad references to its provision by franchisors. Thus the offered marketing services, including advertising, sales promotion, market research and product research, were not subject to any detailed description of the frequency with which they would be undertaken or to broad indications of the level of expenditure upon them. An exception to the latter was found however, amongst those systems which compulsorily levied an advertising royalty, in which case there was an indication of the level of expenditure. In such contracts clauses were usually included which obliged the franchisor to allocate all such sums to advertising or promotion, and dictated the manner in which these sums should be administered.

8.454 Supply of Products

Offered by some franchisors as a benefit to franchisees, the supply of all or some products used or sold within franchised outlets was perceived primarily as a control to benefit franchisors and the system (and indirectly franchisees). Being viewed by participants as a control, and couched in that context in most agreements, it has already been examined as an obligation upon franchisees.
Though offered in broad terms, the provision of assistance and advice by franchisors in respect of operating problems and general business problems of franchisees was not subject to detailed provisions. Thus precise obligations upon franchisors, such as the availability or frequency of visits by franchisor representative, were found infrequently in franchise contracts.

In some systems the offer was held out to franchisees to provide them with current data about trading levels generally prevailing within the particular system.

Ownership of Franchise System

Emphasis was normally placed in franchise agreements on the franchisor's right of ownership of the franchised system, brand image, trade mark, trade secrets and sometimes of the physical ownership of external or internal signs temporarily loaned to franchisees during the currency of the agreement. This ownership usually extended to the operating manual which franchisees were required to return upon termination.

Alteration of Operating Conditions

Allied to such rights, were those found in a number of agreements which gave latitude to franchisors to extend or reduce the menu, to amend the operating manual, to alter stipulated or recommended selling prices or to increase the price of supplies. Also found were clauses which gave the franchisor the right to prohibit operation of a new unit until inspection had taken place and consent given; and (in one agreement) of the right of a franchisor to establish another franchised unit 'in the near vicinity' of an existing unit.
8.463 Access to Franchised Units and Records

In all contracts that were examined, franchisors retained the right of access to franchised premises (at all reasonable times), so that standards could be assessed. Several contracts (particularly those where payment to franchisors was based as a percentage on turnover) stipulated the right to inspect the franchisee's records and books of account. In some contracts, franchisees were required to produce certified accounts to the franchisor. In one agreement the franchisor specifically claimed the right to talk to the employees of franchisees.

8.464 Control over Sale or Assignment of Franchised Units

Included in a number of contracts examined were clauses enabling the franchisor to exercise first option to purchase a franchised unit that was for sale or to buy the unit's equipment. Also found were clauses which gave the franchisor right to refuse permission for the assignment of a franchised unit to another party, though this was usually modified by the statement that such permission should not be 'unreasonably' withheld. In one contract the franchisor maintained the right not to have to defend such a refusal.

8.465 Termination

In most contracts there were a number of provisions which gave the franchisor the right to terminate the agreement should the franchisee commit, and fail to rectify within a specified time, one or more stated breaches of the agreement. Examples of such breaches which were normally included were non-payment of dues to the franchisor, contravention of operating methods and policies, bankruptcy or liquidation, cessation of operation or material alteration in the structure of power within a franchisee company.

One contract gave the franchisor the right to a specified compensatory sum (either a fixed amount or twice the royalties paid during the previous year, whichever was the greater)
should termination result from violation by the franchisee of any obligation or covenant; and an additional specified amount if, upon termination, the franchisee retained trademarks or signs without proper authorization.

8.47 Disclaimers

A few disclaimers were found in the contracts that were examined. The most common was the disclaimer by franchisors of the necessary accuracy of any information given to franchisees (either verbally or in writing), and the refutation of any liability upon the franchisor for any consequences arising out of reliance placed upon such information.

Some franchisors disclaimed liability to third parties for the franchised product, except for the normal liability as a supplier of the raw or pre-prepared products. Others disclaimed responsibility in the event of circumstances beyond the franchisors' control for an uninterrupted supply, of those products for which there was a tied supply to the franchisor. In some agreements there were clauses which disclaimed liability on the part of the franchisor for debts of the franchisee, and which pointed to the lack of any obligation by the franchisor to treat as confidential such information as was provided by the franchisee.

8.48 Summary of Obligations and Rights of Two Parties

The discrepancy between the obligations and rights of franchisors and franchisees has been demonstrated, not only in respect of the difference in extent, but more particularly in the difference in the precision with which the respective obligations and rights of franchisors and franchisees were defined in most franchise arrangements.

Table 8.33 provides a summary of the generally obtaining responsibilities and rights of franchisors and franchisees, analysed according to their operational, financial or legal content.
Table B.33 Summary of Generally Obtaining Responsibilities and Rights of Franchisor and Franchisee

<table>
<thead>
<tr>
<th>Franchisor:Franchisee</th>
<th>FINANCIAL Responsibilities</th>
<th>OPERATIONAL Responsibilities</th>
<th>LEGAL Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>To provide initial concept and maintain brand image of system through marketing, advertising and control.</td>
<td>None in respect of franchisees.</td>
<td>As supplier of products to comply with normal obligations in respect of descriptions.</td>
</tr>
<tr>
<td></td>
<td>To provide, on a continuous basis, group services and advice.</td>
<td>To agreed initial payment for concept and advice (usually).</td>
<td>To agreed continuous payment from franchisee.</td>
</tr>
<tr>
<td></td>
<td>To maintain continuous supply of goods (where applicable).</td>
<td>Rights</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>To survey unit and (in many cases) to have access to books of account etc.</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Franchisor:Franchisee</th>
<th>FINANCIAL Responsibilities</th>
<th>OPERATIONAL Responsibilities</th>
<th>LEGAL Responsibilities</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>To operate the unit in compliance with the system's policies and procedures, as stated in contract, including obligation in respect of purchasing and selling, training of staff etc.</td>
<td>To operate the unit in a semi-independent manner, having the right to determine day-to-day procedure, staffing matters, and some discretion on product</td>
<td>To performance by franchisor of such obligations as stated within franchise contract.</td>
</tr>
<tr>
<td></td>
<td>To provide adequate funds for the purchase/building of the unit and its contents, as found acceptable by franchisor, and for working capital.</td>
<td>Rights</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To pay initial and continuing fee to franchisor as agreed.</td>
<td>To make a profit or bear a loss.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>To provide subsequent funds for alterations, re-equipment etc. of unit as required by franchisor.</td>
<td>Rights</td>
<td></td>
</tr>
<tr>
<td></td>
<td>As owner of property.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Rights
8.5 PERFORMANCE OF TERMS BY TWO PARTIES

8.51 Performance By Franchisors

As mentioned elsewhere, the inherent difficulty of defining in quantitative or qualitative terms the services to be rendered franchisees by franchisors, and the resultant lack of precision in respect of obligations upon most franchisors, rendered impossible a detailed assessment of the degree of compliance of franchisors with their contractual terms. However, a broad appraisal was possible, based on the opinions of franchisees and of franchisors in respect of their own performance.

8.511 Compliance with Pre-Opening Obligations to Franchisees

The implication that the concept had been tested and proven successful by franchisors, prior to its being franchised, was found in general terms to be accurate in all but one system. Fifteen of the sixteen systems had initially opened directly operated units either to test the feasibility of the concept and to establish suitable operating procedures and equipment etc. prior to inviting franchisees to join the system, or as the main method of operation, with franchising adopted later as an alternative method. In the case of the one franchise system in which no pilot unit had been tested by the franchisor the system subsequently ceased operating as such. (16) However, not all the franchised systems had been pre-tested in similar environments or for a fully representative trading period. Some systems had been tried in countries or particular localities whose marketing environment differed from that in which franchisees were invited or permitted to establish their units. In one system, highly responsive to seasonal trading, some fifty franchised units had been opened, before a full year's trading figures had been obtained by the pilot units.

The obligation of franchisors to supply the necessary detailed specifications, policies etc. to enable franchisees to establish units identical with or similar to the prototype
franchised unit, was in broad terms undertaken in all the cases examined. However, considerable variations in the extent of such aid was found to exist not only between but also within systems. Such intra-system differences depended upon the rate of growth at any one time of franchised and/or directly-owned units and the extent of available head office or regional resources for development. Thus, for example, whereas some franchisees stated that they had received considerable assistance from their franchisor in the selection of a suitable site for the franchised unit (including an active search by the franchisor and the benefit of his wide experience as to the feasibility of such a location), other franchisees claimed that they had merely received a 'rubber-stamp' approval (in some cases without the franchisor having visited the site). Some franchisees questioned the objectivity of the franchisor representative in approving a particular location, in those circumstances where the representative received a commission on the implementation of every new unit and was thus influenced by his own short-term financial gain rather than the long-term viability of the unit.

Whilst some franchisors offered from within their own organisation the services of designers, planners, shopfitters etc., others recommended to franchisees approved specialists, for whose services the franchisees had to pay. In those circumstances, franchisor 'assistance' was perceived by franchisees in the context of 'control'.

Wide differences were found amongst the systems examined in the comprehensiveness of the 'blue-print' for the organisation of the unit. Whilst some franchisors provided voluminous operating manuals which included product specifications, normal operating methods, controls, advice on dealing with various situations etc., others contained their total assistance in such matters on a few sheets of instructions concerning, for example, the maintenance of certain items of equipment, or basic menus.
Initial training to franchisees or their unit managers likewise varied between instruction which was mainly concerned with practical handling of the consumable products and equipment etc., to instruction in managerial skills. 'Training sessions' at the franchisee's own unit, according to some respondents, consisted of assistance from the franchisor representative in physically preparing the unit for opening by cleaning or painting the premises, rather than any training for operation, or of brief 'courtesy calls' to demonstrate the franchisor's awareness of the franchisee. Similarly, assistance at the initial opening of the unit was reported to vary widely from a brief, formal visit from a senior executive at the official opening, to the continual presence of field staff over an extended period of several days or weeks. Promotional assistance with the opening of the unit also varied from a brief insertion in the press by the franchisor, announcing the addition of another unit to the system, to a full-scale promotional event organized by the franchisor to generate wide publicity for the particular unit (as well as of the system), through various media.

8.512 Compliance with Post-Opening Obligations to Franchisees

The performance of franchisors varied in their obligation to maintain the system's brand image, through advertising and promotion and control of participants, and an implied obligation to maintain the marketing position of the system through market research and development of the products and equipment.

In those systems where an advertising levy was made on franchisees and the funds allocated to advertising and promotion, franchisors performed their overall obligations to provide such services. However some franchisees disputed the effectiveness to them of their franchisor's performance. For instance, where the majority of franchisees were located in other countries or in other regions of a country, some franchisors' advertising media were seen to be focussed on benefiting the majority, with little or no benefit to the far-flung individual franchisee, despite a proportionately
similar (or actually larger than average) levy paid by him.

Where no specific contribution was made to advertising and promotion by franchisees, the franchisor retained wide discretion in the funds allocated to such purposes, with a resultant significant difference (in proportional terms) between various franchisors and in the satisfaction recorded by franchisees of different systems.

Similarly the extent of control over system participants - and thus the franchisor's compliance with an obligation to maintain the brand image - was seen to vary considerably. The franchisor's instruments for enforcing standards within units - field staff by whatever name - were reported by franchisees to differ widely in the frequency of their visits to units and in the duration and effectiveness of such visits. Whilst being dependent to some extent on their individual characteristics, strengths and level of authority their capacity to control their given units was also seen to be influenced by their span of control, and by the status of a particular franchisee vis a vis the franchisor.

The controlling function of such visits was clearly perceived in some systems, particularly in the hotel franchises. In two hotel systems the visiting representative assessed several hundred separate factors and made a subsequent recommendation, based upon the cumulative total points obtained, either for the continuation or ultimate termination of the franchise (if rectification of faults were not made). In other systems such visits were seen by franchisees to be perfunctory demonstrations of the franchisor's interest. The majority of franchisors claimed that their aim was for each franchisee to be visited by a franchisor representative every four to eight weeks. The majority of franchisees indicated that such visits occurred every six to sixteen weeks.
In some cases, the infrequency of visits was ascribed to the franchisee's long-standing status and experience of the operation or to his 'special' relationship with the franchisor, thus obviating the need (or the effect) of such control by field staff. In others it was a function of geographical remoteness from the majority of units or to the fluctuating span of control of the field staff, some of whom had responsibility jointly for directly-operated and franchised units, and for a fluctuating ratio of developing:established units. Responses indicated a span of control by field staff ranging from 1:5 to 1:35, though, depending on the above factors, this ratio in itself gives only a broad indication.

An assessment at certain intervals, of the continued applicability to their market of the franchised products, seemed to be undertaken by only a few companies together with research into new products and equipment.

Reference has been made above to the availability of franchisor field staff as instruments of control. Such staff, together with line and specialist management at head office or regional headquarters, also had a function as instruments by which the franchisor's obligation to provide general advice and information might be discharged to franchisees. Such advice and information was reported by a number of franchisees to be either difficult or impossible to obtain. Instances were cited of unfulfilled requests for guidance on employment law, instruction in drawing up staffing schedules, information on V.A.T. regulations, advice on suitable equipment and assistance in dealing with local planning authorities.

Most franchisees stated that they were not provided with data on overall trading trends within their systems or on normal operating ratios, despite, in some systems, a known availability of such statistics and requests to their franchisor for such information.
In systems where franchisors had offered purchasing services or advice, all had substantially performed such an offer. Criticisms were voiced by franchisees, however, on the poor quality, taste or appearance of certain products supplied by or for some franchisors, for which no alternative source of supply or product was permitted. In one major system, respondents were particularly critical of the down-grading over a number of years of the major food product sold within the units. Another source of complaint was in respect of the inferred obligation of the franchisor to suggest or to stipulate the purchase of equipment only in such quantity as was necessary for a given unit. Some franchisees pointed to the considerable over-equipping into which they had been compelled by their franchisors.

8.52 Performance by Franchisees

An assessment of the extent of compliance by franchisees with their contractual obligations was less difficult to make than in the case of franchisors, due to the detailed nature of such obligations in certain, though not all, respects.

8.521 Maintenance of Brand Image

There were many and varied instances of franchisees whose units or methods of operation did not adhere to the required brand image of the system as defined by the franchisor. In some instances this appeared to be due to a genuine entrepreneurial reaction to fill a perceived market gap and to adapt to local requirements. In other cases, the contravention of franchisor standards or methods of operation appeared to arise from a desire for short-term financial gain.

Non-adherence by franchisees to the required brand image ranged over a number of aspects, from substantially altering the market at which the unit had originally been aimed, to minor adaptations of the product. The following examples are illustrative of a franchisee's adjustment to local demands or desire to fill a perceived market gap: a substantial alteration of
menu content and preparation methods (to meet demand and expand sales); an increase in portion size (to provide better value for money); the avoidance of tied (franchisor-supplied) products (to obtain better quality); the introduction of newly-designed menu cards (to stimuli interest); the development of radically different entertainment (to diversify and boost sales); the purchase of new furniture and fittings (to adjust to or encourage a new market); the installment of new external and internal signs (to stimulate interest).

The following examples are given of non-compliance with franchisor policy which seemed to stem not from a desire to create better-satisfied customers or encourage a new market, but from a franchisee's aim to improve short-term profitability: purchase of supplies outside the tie (because, being of inferior quality, they were significantly cheaper); a reduction in portion size (to cut costs); the elimination of a stipulated garnish or accompaniment (to reduce costs); the substitution of products in a state that was not permitted eg. frozen instead of fresh meat, dried instead of frozen vegetables (to cut costs); reduction in staffing levels (to lessen labour costs); a narrowing of the menu range (to reduce the amount of food stocks and thus working capital); the introduction of a service charge (to raise revenue).

Apart from non-compliance with existing franchisor policies, methods and products, examples were also recorded of franchisees who were unwilling to adapt to new or future requirements of their franchisor. Where such adaptations involved capital expenditure by franchisees, such as in the refurbishing and redecorating of a unit or in the purchase of new equipment, and where a temporary loss of revenue was likely (because of a total or partial closure for alterations), franchisees were normally unwilling to observe obligations for redecoration such as 'as may reasonably be required'. The reasonableness of the demand was an issue that was difficult to resolve.
CHAPTER 9

ASSESSMENT OF FACTORS INFLUENCING THE FOUR CATEGORIES OF CONTRACTUAL ARRANGEMENTS AND COMPARISON OF SUCH ARRANGEMENTS

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9.1 INTRODUCTION

In the previous four chapters attention has been paid to the profiles of respondents and to analyzing the financial and contractual terms found within the surveyed systems. In this chapter a summary is made of the nature of the two main parties in each of the four types of contractual arrangement, and an assessment made of other factors influencing the arrangements including an overall appraisal of the proposed and executed input by each party, the effects of other parties within or adjacent to the arrangements, the business and economic environment in which each type of arrangement operates and the alternative options open to either of the two main parties. The dynamics of the four types of arrangement are explored, taking into account the initial bargaining position of the two parties and the subsequent changes in their positions during their working relationship.

9.2 ASSESSMENT OF CATERING CONTRACT ARRANGEMENT (1)

9.2.1 Nature of the Two Main Parties

In overall terms catering contractors are seen to have a well-established and significant position as operators of a particular business method within the general economy and within the catering industry. Their penetration of economic activities is restricted, in the main, to employee feeding within industrial and commercial enterprises in Britain, although expansion into other sectors, geographical regions and other diversification of interests is taking place.

Contract catering activity is found to be dominated by four major contractors whose characteristics are generally comparable with each other and, except in respect of scale, are on the whole representative of the generally obtaining characteristics of medium and small contractors.
There was found to be a wide diversity of activities, backgrounds and size of client companies within the survey, and a wide difference in the number of units operated by a contractor for any one client and in the attitudes of clients towards the catering activity and related arrangements. All responding clients were found to be parties of substance, enjoying evident dimensions of size and status in their particular field of activity.

9.22 Input to the Contractual Arrangement

The initial input by contractors to the arrangement is the design and implementation of a suitable system, procedures and organisation (and in some cases of plans and specifications for the building or alteration of premises) for the provision of such catering services as are required by clients. The subsequent and continuing input by contractors includes the provision of appropriate staff, purchasing of adequate supplies, and the availability of advice and assistance in technical and operating matters, as well as the overall management.

Detailed reference has previously been made to the variation in financial and contractual terms of responding contractors, and to their differing capacities to offer services and various abilities to perform what they held out to clients. Bearing in mind these differences and the variation in client requirements, contractors are seen in overall terms to provide a service that continues to benefit clients, but whose major input is to some extent consumed upon the implementation of the required system including the definition of standards, methods and policies.

The initial and continuing input by clients to the contractual arrangement is the provision of premises, facilities and equipment in and with which the contractor operates, and a supply of potential employee-customers plus an agreed management fee and reimbursement of expenses or agreed subsidy. Reference has been made elsewhere to the extent to which various clients complied with their obligations to provide a suitable environment and facilities on a continuing basis, and to their sometimes equivocal
attitude towards the provision of catering services with its attendant financial responsibilities. Thus the input by clients, though varying in extent and adequacy, is seen in overall terms to be a continuing and tangible one, whose value is not extinguished by time or consumption.

9.23 Effect of Other Parties on the Contractual Arrangement

Apart from the contractor and client, a number of other parties are normally involved in such contractual arrangements, including the unit manager, the contractor's field supervisor, the client's employees, suppliers, and in some cases, the central catering control within a client's group. The roles and relationships of these parties (2) are depicted in diagram 9.1 and a summary is given in Table 9.1 of their actual or potential interactions. Both the diagram and matrix illustrate the somewhat complicated situation caused by the dependence of the two main parties (the contractor and client) upon the unit manager's operating and financial performance for the respective gratification or execution of their contractual and financial expectations or obligations; and (in the case of the client) a dependence upon the unit manager to satisfactorily supply part of the client's employment package to his employees or to satisfy patients, students etc.

Table 9.1 reveals the problems arising from circumstances where, by dint of frequent contact, a client becomes involved with the day-to-day catering operation and intervenes in the employer: direct employee relationship between contractor and unit manager, thus changing policies, altering operating conditions, and creating a divided loyalty on the part of the manager. Also illustrated are the effects upon the contractor of complete or partial rejection by a client's employees of the catering element of their employment package, such rejection sometimes being completely unrelated to the contractor's operating performance, but possibly materially affecting the contractor's remuneration or continuity of the contractual arrangement.
Diagram 9.1: Relationships of Main Participants in, or Adjacent to Catering Contract

- **Hirer of agent, supplier of potential customers, policy maker**
- **Agent for supply of raw products, manpower, goods and services and for receipts and expenditures.**
- **Employee for client's policy, receipt of revenue for some aspects.**
- **Supplier of goods as requested, awarder of discount on goods supplied.**
- **Purchaser as agent for client; recipient of discount on goods supplied.**
- **Contractor's line manager carrying out client's policy.**
- **No direct relationship, suppliers: consumers of products.**

- **Client Employee-Customer**
- **No formal relationship unless involved in trade-union negotiations over fringe benefits within the group.**

- **Unit Manager**
  - **Recipient of goods as requested by unit manager or contractor.**
  - **Supplier of goods as requested by unit manager or contractor.**

- **Other Unit Managers in Client Group**
  - **Line managers selling goods and services to semi-captive purchasers.**
  - **Recipients of catering elements of employment package.**

- **Contractor**
  - **Employer, transmitter of goods and services and enforcement of client's policy, receipt of some revenue.**

- **Employee**
  - **Direct employer, no formal relationship; frequent informal contact.**
  - **No formal relationship; frequent informal contact.**

- **Other External Participants**
  - **Contractor's suppliers.**
  - **Consumers of element of employment package.**

- **Diagram Notes:**
  - [Diagram details and relationships explained in text format.]
<table>
<thead>
<tr>
<th>Contractor</th>
<th>Client</th>
<th>Unit Manager</th>
<th>Client Employees</th>
<th>Suppliers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contractor’s financial performance affects subsidy required from client; Contractor’s performance affects quality of catering services forming part of client’s employment package to client’s employees; and thus affects relationship between client and client’s employees. Contractor may terminate contract.</td>
<td>Contractor determines policies and procedures for transactions those laid down by client, which affect the framework within which the unit manager acts. Contractor lays down limits of manager’s authority and responsibility. Contractor is responsible for providing, or for ensuring that client provides, adequate equipment and facilities with which, or in which, the unit manager performs his required function. Contractor’s financial performance may directly affect client employees by resulting in an increase in service prices.</td>
<td>Client’s financial performance affects the products, services, and environment of which client employees are consumers. Contractor’s ability to ensure client’s compliance with current terms affects the end product consumed by client employees. Contractor’s financial performance may directly affect client employees by resulting in an increase in service prices.</td>
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<tr>
<td>Client establishes level of capital expenditure and operating budget, thus determining overall terms, environment, equipment and extent of catering services provided. Such budgets may restrict contractor’s ability to provide services required by the contract, or by client employees; client’s inability or disinclination to provide funds for improvements may directly affect contractor’s revenue (where lease linked to turnover or food costs) by inhibiting increased use of services or not preventing a reduction in such use. Client’s continuation of contract directly affects contractor’s revenue through fees and (usually) through receipt and retention of all or part of any surplus charged by suppliers to suppliers. Any terminate contract. If client has professional catering expertise, regulations and standards of performance may be expected from contractor.</td>
<td>Client’s frequent or long-term contract may result in the client’s assumption of client management. Client’s ability to control, and therefore to direct, and to conform with policies of contract executives in other units.</td>
<td>Client’s appointment of managing director and external contractors may lead to the contract manager’s assumption of client management over unit managers, and increase in the direct control of the client’s managing director. Client may intervene in such matters as pricing strategy, menu compilation, and catering procedures and purchasing activities.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unit Manager is directly responsible for the operating and financial performance of his unit, plays a significant role in determining the contractor’s compliance with agreed terms of contract, and in influencing the contractor’s standing with client. Any terminate contract. Unit manager influences contractor’s revenue received from client (if linked to turnover or food costs), and influences operating costs.</td>
<td>Unit manager is directly responsible for the financial performance and catering provisions. Any terminate contract.</td>
<td>Unit manager is directly responsible for the financial performance, and catering provisions to client employees. Unit manager may contribute to the client’s impositions as an employer held by client employees.</td>
<td></td>
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<tr>
<td>The rate of acceptance of catering services by client employees directly affects contractor’s revenues (if calculated on a turnover or food costs) and may influence contractor’s ability to reduce在这种情况下对供应商的某些优惠。</td>
<td>The acceptance or rejection of catering services by client employees affects unit manager’s performance in eyes of contractor.</td>
<td>The acceptance or rejection of catering services by client employees affects unit manager’s performance in eyes of contractor.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Client employees may not be involved in any decision affecting catering services. Client employees may not be informed of any changes to the catering services. If client employees complain directly to client about catering services, client must take appropriate action with contractor or unit manager.</td>
<td>Contractor’s operating performance directly affects the products, services, and environment of which client employees are consumers. Contractor’s ability to ensure client’s compliance with current terms affects the end product consumed by client employees. Contractor’s financial performance may directly affect client employees by resulting in an increase in service prices.</td>
<td></td>
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</tr>
<tr>
<td>Suppliers normally allow contractors from one to three types of discount on goods purchased. In general, these discounts may be of all or part of the discount as free shipping, the full amount or part of the discount, or a significant part of the contractor’s total revenue.</td>
<td>Due to the system of allowing discounts, the financial advantages accruing from the system to suppliers, the unit manager may be limited in his discretion whether or not to charge suppliers. The quality of goods supplied and the efficiency of delivery directly affects the manager’s performance.</td>
<td>The quality of goods supplied directly affects client employees’ opinion of the extent of catering services, and thus their opinion of the unit manager, contractor and indirectly of their employer, the client-owner of the unit.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Contractors operating performance affects subsidy required from client; Contractor’s performance affects quality of catering services forming part of client’s employment package to client’s employees; and thus affects relationship between client and client’s employees. Contractor may terminate contract.</td>
<td>Contractor determines policies and procedures for transactions those laid down by client, which affect the framework within which the unit manager acts. Contractor lays down limits of manager’s authority and responsibility. Contractor is responsible for providing, or for ensuring that client provides, adequate equipment and facilities with which, or in which, the unit manager performs his required function. Contractor’s financial performance may directly affect client employees by resulting in an increase in service prices.</td>
<td>As agent of client, contractor discriminates the extent to which each supplier’s services are used. Contractor is responsible for ensuring compliance of quality of supply, reliability of delivery, etc. Contractor may terminate orders.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

* The document appears to be a summary table of key interactions and agreements between contractors, clients, unit managers, and suppliers, highlighting the financial and operational responsibilities of each party. The text is dense and technical, focusing on contractual obligations and performance metrics. *
The financial links between the client, contractor and suppliers are also shown, and indicate the ramifications upon the unit manager's choice of supplies, the significance of an alteration in demand for supplies, and the effect upon the contractor's income resulting from the widely prevailing system of the allocation of discounts by suppliers to contractors, and the practice enjoyed by many contractors of retaining all or part of such discount and not transmitting it to the client.

9.24 General Environmental Factors Affecting the Two Parties

Mention has previously been made of the client's contribution to the contractual arrangement, without which catering contractors would be unable to continue their business as contractors per se. The requirement of catering contractors for the provision of sites, buildings, fixed equipment and an adequate supply of potential customers (being the clients' employees, patients or students etc.) in order to sustain their existence (without a fundamental change of activity) emphasizes the importance of the client's role. Not only is the client a 'partner' in the contractual arrangement but simultaneously the provider of the major pre-requisites to operation of site, capital and a potential market for catering services. As most contractors have been predominantly involved in companies in the industrial and commercial sectors of the economy, they are particularly dependent on the overall business health of such sectors, and liable to be considerably affected by economic or political factors affecting their clients.

Partly in response to such recent problems in industry and commerce generally (3), which have resulted in the demise, prolonged closure, part-time functioning, or large scale redundancies in certain industries or businesses, and partly in response to a perceived market gap, some contractors have begun to increase their penetration of other sectors of the economy and have widened their geographical coverage to overseas markets. In addition, some have begun to diversify into other business activities. This catholicism in the acceptance of client types has resulted in a very significant extension of potential clients with available sites, capital resources, and potential customers for catering and other services, which has greatly increased the contractor's potential market.
The supply of clients wishing to employ the services of catering contractors may be affected by a number of factors such as inflation, legislation, government regulations, trade union activities, and the generally prevailing attitude to such contractual arrangements.

General inflationary trends in Britain have resulted in substantially increased operating costs incurred in the provision of catering services, which have normally been passed on in full or in the main to the contractors' clients, through automatic transmission or more frequent re-negotiation of budgets. This increase in required catering subsidy is likely to cause clients to reconsider their policies towards the provision of catering services or towards the employment of contractors. The greater financial burden upon clients may either underline a need for continued catering expertise (in the form of contractors) to control expenditure, or cause clients to assume direct management of the catering operation (thus eliminating the payment of management fees) or to close down such services altogether.

The last-mentioned alternative seems unlikely in the light of the currently imposed wage restraint, which has caused employers to consider alternative means of remuneration to employees, including the provision of catering services where none were previously available, or an improvement to existing services, thus possibly increasing the contractors' market or extending the services required.

Recent legislation on employment practice including the remuneration of employees, redundancy payments etc (4) together with pressure from some trade unions have been factors influencing companies in whether or not to employ catering contractors. Thus whether parity in pay, in fringe benefits or working conditions is or is not to be maintained between a company's main workforce and its catering employees, is an issue that in some circumstances governs the decision on whether or not to employ a contractor.
Finally, the general acceptance in industry and commerce of the catering contract arrangement as a well-established method of providing catering services to employees and other categories of people is a factor that is likely to be of some influence over prospective clients.

9.25 Alternative Options Initially Open to the Two Parties

A summary is contained in Diagram 9.2 of the alternative options open to either party, other than entering into a mutual contractual agreement. As indicated above, the very nature of the contractor's business necessitates dependency on a supply of clients, and thus his options are restricted to locating other clients, unless a fundamental change is made to the contractor's activity. However, the contractor's market is normally restricted only by questions of the viability of each contract and not by factors such as the particular market sector in which the client operates or the brand image of a given client or unit.

Being an ancillary facility to the main business activity of the client, and being a subsidized rather than profit-making element within the client's company, the catering services are unlikely to be considered of primary importance. Thus a client may elect to discontinue such services or to delegate the responsibility for them to an existing company executive, or may choose to purchase expertise in the market place in the form of a directly-employed catering manager or advisor. If the client chooses to continue providing catering services, his options of direct management normally reveal the disadvantages of the necessity to recruit and retain staff and the lack of purchasing leverage; the only other alternative resolving such disadvantages being to employ another contractor.

9.26 Dynamics of Relationship

Within the contractual arrangement the initial status of both contractor and client is found, in broad terms, to be roughly comparable. Each enjoys a substantial reputation, evident dimensions of size including units owned or operated, number of employees, human and financial resources and financial capacity. In circumstances where a client owns a number of units at which catering services are required, and where the client simultaneously employs another contractor and/or directly operates one or more units
the client’s position vis a vis the contractor is relatively stronger, due to greater experience as a client and/or greater awareness of operating and technical conditions (often through a central catering control established within the client group). Clients with a particularly prestigious reputation or with units of a prestigious nature are seen to enjoy an added status in the eyes of contractors.

Diagram 9.2 summarizes in general terms the initial negotiating positions of contractor and client. It reveals the stronger overall position of the contractor, attributable both to the client’s evident desire not to devote his resources to a perceived complex activity ancillary to the main purpose of the client company (being one that requires specialized operating and technical skills as well as access to a continuing supply of specialized employees and provisions) and to the contractor’s experience of the contractual arrangement itself. The result of this negotiating position is manifested by the terms of the contractual agreement which normally reveal a bias in favour of the contractor because of the safeguarding of his management fee, and the omission from standard contracts of precise obligations upon the contractor.

The subsequent position of the two parties during their working relationship is broadly outlined in Diagram 9.3. The client’s position vis a vis the contractor has improved because of two main factors. The first is the consumption by the client of an important part of the contractor’s initial input to the arrangement (i.e. the implementation of the required catering system). The second is a consequent widening of options open to the client, who may retain the system implemented by his contractor, terminate the contractual arrangement and install direct management, although the subsequent direct employment by the client of contractor’s staff formerly allocated to the client’s unit, is prevented by clauses in most contracts (usually for a period of six months). However, the necessity in such altered circumstances for the client to assume responsibility for the recruitment and retention of catering employees and for the selection and purchase of supplies, is a disadvantage perceived by clients, and an influence to maintain the status quo.
Diagram 9.2

Initial Negotiating Position of, and Likely Outcome Between Catering Contractor and Client

**Contractor**

- **Status Influenced by**
  - Reputation as catering contractor, in terms of operating and financial performance; stability and continuity; 
  - Dimensions of market penetration, number of units under contract, number of employees, turnover and profit, and extent of group resources.

**Options**
- Main disadvantages
  - Enter agreement with other clients: Terms may be less favourable to contractor; difficult to forecast client's likely adherence to terms; Time-consuming to locate and negotiate.
  - (a) With broadly similar requirements:
    - Need to compete with other contractors and with clients' policy of direct management.
  - (b) From other business sectors with different requirements, eg, hospitals:
    - Need to develop new expertise at group and unit level; Need to develop reputation.
  - (c) In different geographical areas, eg, overseas:
    - Need to develop special local expertise; Necessary to extend or establish new group services.
- **Other Influencing Factors**
  - Diversification into new business activities, eg, contract cleaning.
  - Perceived willingness to comply with client policy and requirements; Flexibility in negotiating terms; Availability of other potential clients; Short-term nature of contracts.

**Client**

- **Status Influenced by**
  - Reputation, stability and continuity of business; Perceived ability to fund agreed subsidy, pay contractor's fee and reimburse contractor's expenses; Potential employees-customer at given unit and required services; Potentiality of other units within client's group; Concurrent employment of other contractors and/or direct management of other units.

**Options**
- Main disadvantages
  - Employ other contractor: May have inferior reputation, be perceived as less effective; May offer less favourable terms.
  - Directly employ catering manager:
    - Reliance on manager's individual ability to design and implement blue-print of operation; No access to ready supply of managers; Lack of specialist advice and services in technical and operational matters.
  - Manage catering services through client's existing executives (with no specialist catering expertise):
    - Lack of professional expertise in design and implementation of catering services; No access to continuing supply of managers; No purchasing leverage.
  - Close down catering services:
    - May reduce productivity; May cause employee unrest; Likely to restrict recruitment and retention of employees.

**Negotiating Positions**
Contractor enjoys a slightly stronger negotiating position, due to greater experience of the contractual arrangement, and client's evident need for catering expertise.

**Terms of Agreement**
Rights and obligations of each party approximately equally balanced.
Clients, on the whole, are seen to be of a conservative nature, preferring to retain the services of a known contractor (providing that the contractor has performed adequately) and preferring not to assume total responsibility for an activity which they regard as being complicated and time-consuming.

There is, however a different relationship between a contractor and those clients with a central catering control and/or wide experience of client status or direct management of the catering function. In this case the client's evident expertise in, or knowledge of catering, allows such a client a stronger negotiating position in respect of the contractor, particularly as such clients are normally those with a number of units (actually or potentially able to be put to contract), a large number of employees and often a well-known and prestigious business reputation. The potentially larger financial rewards to contractors from such contracts and the prestige accruing to the appointed contractor are accompanied normally by higher expectations on the part of the client in relation to the contractor's operating and financial performance. The demonstrated more active approach of such clients, and their ability to compare one contractor's performance with that of another concurrently employed contractor or with the results from a directly-administered unit, creates ab initio, a more powerful position and provides ready alternative options to employing a given contractor. The relative ease with which some such clients can undertake direct administration of catering services is negated to some extent by the very reasons for their employment of contractors (for example because of employment costs attributable to catering staff or problems of wage differentials between catering employees and the main workforce).

Apart from changes in their relationship arising from the degree of satisfaction enjoyed by each party in the other's performance, the position of the two parties is seen not to alter to any degree. The existing expertise of such clients makes less valuable the initial implementation by the contractor of the catering system, and thus its consumption is of less significance to their subsequent positions vis a vis one another.
### Diagram 3.3

**Position of Catering Contractor and Client During Their Working Relationship**

#### CONTRACTOR

<table>
<thead>
<tr>
<th>OPTIONS</th>
<th>STATUS influenced by</th>
</tr>
</thead>
<tbody>
<tr>
<td>Main disadvantages</td>
<td>Demonstrated capacity as contractor to provide required operating and financial performance; Reputations, stability and continuity; Dimensions in terms of market penetration, number of units under contract, number of employees, turnover and profit, and extent of group resources.</td>
</tr>
</tbody>
</table>

#### CLIENT

<table>
<thead>
<tr>
<th>OPTIONS</th>
<th>STATUS influenced by</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loss of flexibility and perhaps retained discount on supplies; opportunity to cooperate</td>
<td>Demonstrated ability to provide adequate funds; General business reputation, stability and continuity; concurrent employment of other contractors and/or direct management of other units; Potentiality of other units within client’s group.</td>
</tr>
</tbody>
</table>

#### CONTINUING INPUT

| (a) With broadly similar requirements, in other businesses (e.g. hospitals) | Provision of premises, fixed equipment, supply of potential customers and/or payment of agreed subsidy; Exposure to operating losses; Commitment to pay contractors fees, reimbursable expenses; Commitment to provide funds for renovations etc. as agreed. |
| (b) With different requirements, in other businesses (e.g. hospitals) | Provision of premises, fixed equipment, supply of potential customers and/or payment of agreed subsidy; Exposure to operating losses; Commitment to pay contractors fees, reimbursable expenses; Commitment to provide funds for renovations etc. as agreed. |

#### OTHER INFLUENCING FACTORS

| (a) New technical and operational expertise and reputation | Genuine or equivalent attitude to provision of catering services on-site; Capacity and willingness to comply with financial obligations; Availability of competing contractors; Extent of in-house experience of contractual agreements and specialist skills. |
| (b) New technical and operational expertise and reputation | Genuine or equivalent attitude to provision of catering services on-site; Capacity and willingness to comply with financial obligations; Availability of competing contractors; Extent of in-house experience of contractual agreements and specialist skills. |

#### NEGOTIATING POSITIONS

- Improvement to client’s position, due to consumption of contractor’s ‘blue-print’ of operation, improved feasibility of alternative options, greater experience of the contractual arrangement, and necessity for contractor to re-negotiate contract.

#### TERMS OF AGREEMENT

- Rights and obligations of each party approximately equally balanced; pressure on contractor to contain costs and fees.
As a long-established method of conducting business, the concept of contract catering was found to be readily understood both by participants and by non-participants within or outside the hotel and catering industry. Catering contractors were seen, in broad terms, to be meeting a need amongst a wide and increasingly extended spectrum of types of clients, mainly for the provision of catering services to clients' employees but also to other categories of people and including a wider range of services such as the provision of accommodation and leisure facilities.

Resulting from concentration within the catering contract sector, four companies were found to predominate and were seen to be increasing in size and influencing other contractors in a number of respects.

A detailed analysis of currently prevailing terms revealed that 'cost plus' catering was widely used (subject to agreed fixed budgets), and that a variety of fee structures were used to calculate the contractors' fees, the most common being a fixed management fee in addition to the reimbursement of costs. In general contracts were for an indefinite period, but usually were for a minimum initial six to twelve months, with a three month period of notification of termination. Contractual documents were found to be relatively brief, with few detailed obligations placed on either party, and weighted in favour of contractors by dint of the protection of at least part of their management fee (whatever the outcome of their performance), the transmission to the client of all or most costs, and the lack of detail governing the contractors' expected performance.
The stronger bargaining position of contractors was attributable to two factors: their experience as contractors and the normally prevailing inexperience of clients in such a role; and the widely-held attitude of clients that catering was a complex activity requiring specialized technical and operating knowledge and experience, which would be over-demanding on the human and financial resources of the client's existing organization, and would be better met by buying in a contractor's services.

This predominant position of contractors was balanced to some extent by several factors, including the complete dependence of contractors on an adequate supply of clients with suitable premises, a sufficiency of potential customers and adequate financial resources; other factors included the ancillary nature of catering to a client's main business activities, and the alternative options open to a client (possibly including direct management of catering services or the closure of such facilities).

The potential for growth of catering contract arrangements was seen to be very extensive, due to the widespread acceptance of such a business method, and to the catholicism of contractors in their choice of client type as well as their ability and willingness to undertake a wide range of catering and ancillary activities, and to penetrate new markets within Britain and overseas.

The relationship between contractor and client was seen normally not to undergo any radical change caused by the business development of either party during the course of time. However, the consumption by the client of the contractor's initial blue-print of operation was found to be a potential factor for the alteration of the balance of power, leading to possible termination of the relationship; and the effect of the unit manager's interactions with the client, client's employees and the contractor was also seen to be of considerable significance. The necessity for frequent renegotiation
between the two parties and the short periods of notice for termination evidenced the relative ease with which clients could impose a final sanction upon their contractor, and thus negated to some extent the financially secure position of the contractor.

A number of differences were found to exist between single and multiple clients in their relationship with a contractor. The former, in broad terms, tended to allow considerable discretion to their contractor in financial and operating matters, and appeared not to accord catering and its related arrangements with a high degree of importance. Multiple clients, however, frequently had directly-employed catering co-ordinators to control and monitor the activities of one or more contractors. Often they had considerable trade union activity amongst their employees, and in such circumstances catering was often used as a bargaining counter between the employer (ie. the contractor's client) and employees (ie. contractors catering customers), this resulting in strict conditions being placed on contractors and greater importance being attached to the catering activity.

In the main literature relating to catering contractors (5) only a few areas of direct comparability with this study are found. Information on the contractual arrangement per se or on the relationship between the two main parties is limited, but substantial agreement exists on a number of related aspects or in respect of minor details. Thus for example, Koudra's findings concerning the general characteristics of the four major contractors and his suggestions regarding the attitudes of clients towards the provision of catering services and employment of catering contractors support those contained in this work. His appreciation of the disproportionate influence exercised by multiple clients in relation to contractors also supports the contentions of this researcher. Koudra's predictions of the lack of any real growth of the major contractors within their main traditional market have been proved inaccurate by subsequent data collected by this researcher. Simi-
larly, indications in this study of the average length of contractual relationships between contractors and their respective clients put into question Koudra's estimates, and suggest that such relationships in general are considerably shorter than he indicated.

9.3 ASSESSMENT OF HOTEL MANAGEMENT CONTRACTUAL ARRANGEMENT (6)

9.31 Nature of the Two Main Parties

The existence of hotel management contractors as a genus of operators within the general economy and within the hotel industry is a recent occurrence both in a world-wide and British context. Indications have been given of the very small current extent of such contractual arrangements within the parameters of this survey, and reference made to the proportionately rapid growth of hotel management contracts at the present time.

Amongst responding contractors per se there was no marked difference in size or market penetration within the geographical limits of the survey but taking into account their overall interests (i.e. including wholly-owned and operated hotels, and noting to a lesser extent their other business interests) there was a very wide variation in the size and significance of respondents. There was also found to be a wide difference in the intentions of contractors towards the utilization of management contracts as a long-term business method. One quarter were assessed as using such arrangements for ad-hoc or short-term reasons, whilst three quarters were classified as entering into management contracts as a planned, long-term, alternative business activity.

Little primary data could be obtained on the nature and status of clients, and likewise information from contractors about their current or potential clients was limited. A mere handful of clients in this country were assessed as having current long-term intentions towards client-status in general or in respect of a particular contractual arrangement, or having formulated a policy to undertake such a role in the future; whilst clients with overseas interests were seen potentially to be
more plentiful, and likely to undertake a contractual arrange-
ment for a medium or long-term period.

9.32 Input to the Contractual Arrangement
A major initial input by contractors to the contractual
arrangement was in many cases the provision of extensive advice
on and assistance with, the building of a projected hotel,
including monitoring plans and specifications and over-seeing
their implementation. Also of fundamental importance (whether
an hotel was newly-built or merely taken over) was the defi-
nition and implementation by contractors of detailed policies,
standards, procedures and systems in accordance with the
client's overall policies and the particular circumstances of
each hotel. The subsequent and continuing input by contractors
to the arrangement was a capacity to attract guests and thus
generate revenue for the client, and to provide continuing hotel
and ancillary services through adequate management and control,
and through the provision of suitable staff, supplies and
general expertise.

Detailed reference has already been made to the different fin-
ancial and contractual terms offered by contractors and the
variation in their capacity to execute what they held out to
clients. In general, however, a contractor's performance was
measured by financial results attributable to the client.
Although a substantial part of the contractor's initial input
(i.e. assistance and advice in respect of the hotel environment
and systems) was consumed by the client upon implementation,
the continuing nature of the contractor's contribution - a
return on the client's capital - was of fundamental importance
and of a tangible nature. The initial and continuing input
by clients to the contractual arrangement was the total or
major part of initial and working capital for the purchase of
an existing hotel or of a site and the subsequent construction
and equipping of an hotel, together with exposure to financial
risk and a commitment to provide additional funds for re-
investment as agreed. In circumstances where a client's hotel
was operated under the brand name of a contractor, the client
made an additional contribution to the arrangement by providing increased exposure and market penetration for the contractor's name and pre-empting the contractor's competitors.

Reference has been made elsewhere to the extent to which clients adhered to their financial and contractual obligations, and to the problems arising from an equivocal attitude on their part to the medium or long-term duration of the relationship. Whilst individually varying in their input to the arrangement, in broad terms clients were seen to make a major continuing and tangible contribution (in the form of fixed assets). Their continued commitment to exposure to financial risk, though still a potential contribution to the arrangement, was normally less significant after the initial years of operation (during which operating losses were likely to be sustained by the hotel, and additional funds for working capital were likely to be required).

9.33 Effect of Other Parties on the Contractual Arrangement
The major participants in, or adjacent to the contractual arrangement include the contractor, client and hotel manager together with the hotel employees and guests(7)In circumstances where an hotel is operated under the brand name of the contractor and/or the client, the managers of other hotels owned or operated by the contractor and/or the client may be affected by such arrangements. Diagram 9.4 reveals the roles and relationships of these parties, and points to a lack of any formal relationship between the client and the contractor's directly-employed hotel manager operating the client's unit, although such manager plays a very significant part in providing the client with a return on his investment, and influencing the overall value of the hotel, should the client wish to realize his assets.
Diagram 9.4

Relationships of Main Participants in, and Adjacent to Hotel Management Contract.

hirer of agent: policy maker

agent for supply of manpower, raw products and finished services; instrument for provision of guests and revenue.

Client

Contractor

employee

direct employer

no formal relationship

employee and employer instrument for (direct or as providing agent) part services and instrument for obtaining transmission of revenue policy, part policy-maker.

Client's Hotel Manager of directly owned and operated hotel

employee

manager

Hotel Employees

normal employee: manager relationship

normal manager: employee relationships; medium for provision of services and receipt of revenue

Contractor's Hotel Manager of directly owned and operated hotel

employee

manager: employee relationship

normal purchaser: seller role; provider of revenue

normal seller: purchaser role; providers of services

Guests
The matrix in Table 9.2 gives a summary of the interactions that were found to occur between parties within or adjacent to hotel management contract arrangements. In respect of the interactions between client, hotel manager and contractor, reliance has also been placed on the findings of Eyster (8), based on a much wider survey than was possible within the parameters of this study. Eyster's findings on the tripartite relationship accord to a large extent with the researcher's findings in respect of the interactions between catering contractors, clients and unit managers, and with the more limited information that could be obtained on the relationship of hotel management contractor, client and unit manager within the British context.

Apart from the obvious prime importance of direct contractor: client interaction, those of the hotel manager with the client and contractor were of considerable significance. Thus in situations where a more frequent contact was made between client and hotel manager than between contractor (or his representative) and hotel manager, there was a possibility of the client assuming direct authority over the manager, leading to a potential divided loyalty on the part of the hotel manager.

9.34 General Environmental Factors Affecting the Two Parties

Essential to an hotel management contract is the use by a contractor of a site and hotel building owned by another party. Thus contractors per se are completely dependent upon a supply of clients who are both able to provide these prerequisites to operation and willing to enter such contractual arrangements. Contractors are therefore subject not only to factors normally affecting hotel operators (such as the general economic climate, legislation affecting hotels, or the particular component factors in any given situation determining the viability of a particular hotel) but also to factors influencing the availability and suitability of potential clients. Hence contractors per se are directly affected by the economic and political climate in countries where they wish to operate, by the availability of suitable existing hotel stock or of sites, and capital for hotel development, and by
the attitude of potential clients towards the contractual arrangement (influenced by their perceived need for expertise and the generally prevailing reaction to, and experience of management contracts).

The economic and political climate in Britain within the last decade has varied in respect of hotel building and operation, from being substantially encouraging in the form of government grants and loans for the construction or extension of hotels (9) to producing a neutral or discouraging effect (for example by not introducing more favourable, tax treatment for hotels comparable to that of other countries or in other industries in Britain (10)).

Such a climate has resulted in a situation which has affected hotel management contractors in various ways. The increase in hotel building arising from the government's Hotel Development Incentive Scheme has changed the nature of hotel stock, particularly in some areas, so that there has been a significant increase in the number of large modern hotels, such as would be feasible to operate under management contract. In addition the precipitate nature of some hotel building (undertaken in certain cases without reference to demand or to concurrent building by competitors), together with the recent period of economic depression in British business (resulting in a reduction in domestic demand for hotel services) has caused a period of considerable over-supply of hotel accommodation, particularly in some areas. This, combined with the inexperience of those newly-involved in hotel ownership and operation, produced a fund of properties suffering from various operational and financial problems, thus being a potential market for management contractors on a short or long-term basis.
Since the period of rapid hotel development there has been a virtual halt in building new hotels, attributable to the non-feasibility of the majority of such ventures caused by rising costs of land and construction, market resistance to increased selling prices and a continued reluctance by institutional lenders to invest in hotel properties unless at a higher than normal rate of interest. This has deterred hotel companies from expansion through new building and encouraged them to undertake management contracts instead, whilst at the same time restricting the overall supply of new hotels in Britain as a potential market for contractors.

The supply of potential clients for hotel management contractors is likely to have been increased by the effects of inflation and legislation upon existing independent hotel owners. Many have been subject to the twin pressures of reduced profit margins and a need for considerable capital expenditure (11), and therefore are likely to be influenced to seek external advice and assistance. A move by independent hoteliers to obtain economies of scale and a brand identification has been evidenced by the formation and growth in recent years of hotel consortia (12). These have been primarily for marketing purposes, but also have made available to members the benefits of group purchasing leverage and general advice. The need for independent hoteliers to gain marketing assistance has been further underlined by the trend towards concentration within the hotel industry and the growth of brand identification, wide scale advertising, reservation systems and referral links amongst the medium and larger hotel groups. In the U.S.A. similar pressures have been an important factor in the expansion of hotel management contracts (13) and are therefore considered to be a potential influence on such arrangements in this country.

However, an important factor influencing the supply of clients is the generally prevailing attitude towards hotel management contracts or alternative methods of obtaining external managerial, marketing and purchasing advice and assistance.
Whilst there is some collective experience in this country of
the implications of membership of a consortium or of referral
links, there is only a very limited knowledge and understand-
ing of the alternatives of hotel franchising or hotel manage-
ment contracts. This, therefore, is likely to have a circular
effect: until more is known about such arrangements they are
unlikely to gain a significantly increased number of adherents.

Overseas, a number of factors have influenced the actual and
potential supply of hotels available to management contractors.
There is increased wealth amongst various governments, groups
and independent businessmen in developing areas such as the
Middle East, North Africa, other parts of Africa and South
America. Greater international aid has been channelled into
the development of tourism in a number of countries. This
availability of capital and rising demand for hotel accommod-
ation and ancillary services from local inhabitants, foreign
businessmen and tourists has resulted in considerable hotel
building in such areas.

In addition to the availability of such newly-built hotels,
and the supply of established hotels (rendered less competi-
tive by the marketing links of competitor hotels and there-
fore requiring marketing and management expertise), demand for
contractors' services has been further influenced by a general
lack of indigenous expertise in the design and implementation
of hotel buildings and systems, within many of the countries
where hotels are being developed. The need for expatriate
expertise, either on a long-term basis or in a caretaker role
until local expertise has been created, therefore has provided
a market for management contractors, franchisors, individual
hotel managers and hotel companies interested in wholly-owning
and operating hotels in overseas' locations. However, the
general political climate in some of these countries has not
been favourable to foreign ownership of properties and busi-
nesses; and the buying-in of advisory and managerial expertise by
individually employing experienced architects, engineers, and hotel managers etc. excludes the continuing benefits of group marketing, purchasing and co-ordinated expertise.

Though hotel management contract arrangements have been favoured by a number of developing countries as a means of combining local ownership with foreign expertise, the implementation of such contractual arrangements has been subject to various problems. Management contractors have had to assess such factors as geographical inaccessibility, difficult communications, the potentiality of international or civil war, racial or national policies against expatriates, differences in local customs, trade barriers and financial controls (14). Such factors have influenced the detailed contractual and financial terms of management contracts in addition to bearing a major influence on the rejection or acceptance of such an arrangement.

9.35 Alternative Options initially open to the Two Parties

Mention has been made of the potential supply of hotels in Britain and overseas, available to contractors. But whereas some contractors are free to consider more or less any hotel on its potential viability as a managed operation, those contractors who maintain a standard brand image are much more restricted. The available supply of hotels to such contractors is confined to properties which are, or could be made to be, sufficiently in accord with the prescribed overall image and detailed specifications of construction, layout and decor etc. Contractors with extensive hotel interests or those who aim at a particular market segment are also restricted to considering only those properties which fit into their existing pattern of distribution or within the broad definition of their market.

The available options open to contractors are also influenced by whether contractors employ other business methods (such as ownership and operation of hotels) or are contractors per se.
If they are in the latter category they are thus completely reliant upon a supply of client-owned hotels, and the pursuit of alternative options would involve a radical change in their nature (i.e. by diversifying into other contractual activities or by embarking into a capital-intensive role as owner-operator of hotels, or by becoming a franchisor). If contractors are of the former category their dependence upon the provision by clients of hotel premises is less marked; and having existing substantial capital resources, easier access to funds and a more permanent involvement in the hotels being operated, their alternative means to growth through the purchase or lease of premises or through establishing a franchise network is likely to present fewer problems than to contractors per se.

These options and their attendant disadvantages are summarized in Diagram 9.5, as are the alternatives open to clients. Depending on the availability of other means of group affiliation, and on their need for operational management and for continuing widespread, effective marketing services, clients are less restricted in their choice of action.

9.36 Dynamics of Relationship
In broad terms hotel management contractors and clients are seen to be of an approximately equal initial status vis a vis one another. The contractor's status depends primarily on his reputation as a contractor to provide an adequate operating and financial performance, or on his reputation as a hotel owner-operator, plus his evident dimensions in terms of market penetration and human and financial resources. The client's status is primarily based on his reputation and perceived capacity to provide adequate funds (and thus environment and facilities for the hotel operation) and a stable and continuous business interest in the project. The negotiating position of clients who concurrently own and/or operate one or more hotels (and particularly where they direct the activities of a chain of hotels or where their hotels enjoy a prestigious reputation or location) is enhanced by their
knowledge and experience of hotel operation, and by the additional potential market penetration offered to the contractor if such hotels can be linked to, or branded in the name of the contractor.

The initial negotiating positions of contractor and client are depicted in Diagram 9.5, which summarizes in general terms the status of both parties, their proposed contribution to the arrangement, the alternative options available to them and other influencing factors. In broad terms their positions are approximately equal, though in circumstances where the client has no experience of hotel operation (as a client or as an operator in his own right), and where the contractor has wholly-owned interests and is not solely dependent upon clients for the continuation of his enterprise, the contractor’s position becomes stronger. These circumstances being the more usual, a more dominant position for the contractor has been shown in the diagram. The resultant contractual terms offered by contractors to clients demonstrate their usually stronger position, by the transfer of all or most financial risk to clients, and by the safeguarding of at least part of the contractor’s management fee. However, the importance attached by both parties to the enterprise to which the arrangement relates, as a complex business activity in its own right with potentiality for profit and capital appreciation, together with the approximately equal status of the two parties is shown by the generally obtaining comprehensiveness of the contractual terms and the broadly equal distribution of rights and obligations.

The subsequent position of contractor and client during their working relationship is shown in general terms in Diagram 9.6. Ignoring individual reactions of any two parties to their respective performance of obligations to one another, the diagram illustrates an improvement in the client’s position with the passage of time. A substantial part of the contractor’s input has been consumed following the planning and implementation of an hotel in its entirety and/or the establishment of detailed policies and systems. Likewise, the contractor’s
Diagram 9.5

Initial Negotiating Position of, and Likely Outcomes Between Hotel Management Contractor and Client

<table>
<thead>
<tr>
<th>CONTRACTOR</th>
<th>CLIENT</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>STATUS</strong></td>
<td><strong>STATUS</strong></td>
</tr>
<tr>
<td>Influenced by</td>
<td>Influenced by</td>
</tr>
<tr>
<td>Reputation as hotel owner-operator and/or contractor; stability and continuity</td>
<td>Reputation, stability and continuity as business entity; Perceived ability to supply adequate initial and continuing funds for implementation and operation of hotel; concurrent employment of other contractors and/or direct management of own hotels; Potential additional hotels for operation.</td>
</tr>
<tr>
<td>DIMENSIONS: Market penetration, number of hotels under operation, number of employees, capital, turnover and profit and extent of group resources.</td>
<td></td>
</tr>
<tr>
<td><strong>PROPOSED INPUT</strong></td>
<td><strong>PROPOSED INPUT</strong></td>
</tr>
<tr>
<td>Blue print of construction/alteration, equipping hotel; suggested policies, procedures etc. and implementation as agreed; concluding operation, management and control of hotel; Provision of suitably trained employees; capacity to attract guests through advertising, promotions, referrals etc.; Availability of advice and assistance in technical and operational matters; generation of revenue to client.</td>
<td>Major or total initial capital for site, building, contents and working capital; commitment for future re-investment as agreed; Exposure to financial risk, including operating losses; commitment to pay proportion of contractor's fee irrespective of trading outcome; Means of increasing exposure to contractor's name and brand image and pre-emption of competition.</td>
</tr>
<tr>
<td><strong>OTHER INFLUENCING FACTORS</strong></td>
<td><strong>OTHER INFLUENCING FACTORS</strong></td>
</tr>
<tr>
<td>Ability to expand sales/market penetration by eg. direct management; Availability of other potential clients; Flexibility during negotiations and willingness to accede to client requirements; Perceived ability to resolve potential conflicts of interests with directly-managed hotels;</td>
<td>Genuine or equivocal attitude to proposed duration of contract; Desire for long or short term trading benefits; Capacity and willingness to comply with financial obligations; Availability of marketing and sales resources; Usually long-term nature of contract.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>OPTIONS</th>
<th>OPTIONS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enter agreement with other clients</td>
<td>May have inferior reputation; may not be perceived as cost effective; may offer less favourable terms.</td>
</tr>
<tr>
<td>(A) in broadly similar market</td>
<td></td>
</tr>
<tr>
<td>Lack of potential clients with suitable hotels; Terms may vary in scale of client's requirements and volume of business</td>
<td></td>
</tr>
<tr>
<td>(B) in different geographical area eg. overseas.</td>
<td>Need to adjust to different operating conditions, demand etc.</td>
</tr>
<tr>
<td>Need to extend or establish new group service facilities</td>
<td></td>
</tr>
<tr>
<td>(C) in substantially different market eg. oil rig management, construction camps</td>
<td>Necessary to develop new specialised expertise and reputation.</td>
</tr>
<tr>
<td>Become franchisee</td>
<td>Need to research and develop franchise scheme, administrative procedure; Time consuming to locate and vet franchisees and sites</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>Purchase or lease hotels</td>
<td></td>
</tr>
<tr>
<td>Substantial capital requirements; Exposure to financial risk; Need to find suitable existing hotels or sites.</td>
<td></td>
</tr>
</tbody>
</table>

**NOTES:**
- Approximately equal status of contractor and client. Both expect to have broadly equal balance of power. Client's reliance on initial blue-print of operation results in improved position for contractor.
- **TENTS OF AGREEMENT:**
  - Rights and obligations for each party clearly defined and equally distributed.
  - A balance is struck in financial obligations imposed on client.

- **OUTCOMES:**
  - Success franchising
  - Conversion of marketing relationships to include advertising, promotion, and referrals, and assistance in technical and operating matters.
  - Directly employ a hotel manager
  - Adopt other contractor

- **CHALLENGING FACTORS:**
  - Lack of hotel franchise systems available; need to recruit, train, and retain own employees; need to accede to franchisees' policies and conditions.
  - Few existing constraints; may not be accepted for membership; need to recruit, train, and retain own employees; lack of comprehensive group services and advice.
  - Sell/lease out hotel
  - End to or reduction in financial and operating involvement; loss of control, power.
initial efforts to attract guests to the hotel by advertising, sales promotion, reservation systems etc., may become less valued once customer-loyalty has been built up towards a given hotel.

Though limited by contractual constraints (normally included by contractors in their agreements to prevent early termination of the relationship without good cause) the choice of alternative actions open to clients becomes more feasible, especially to clients with a short term contract. Being in possession of an established hotel and enjoying the benefits of implemented systems and of previous marketing services, the options of direct management or of affiliation to marketing consortia or the establishment of referral links are tenable.

When the time comes for re-negotiation, the contractor's position is weaker than during the initial negotiations, and is also likely to be affected by competitor contractors (who may be more interested in the potentially higher financial rewards from a going concern than from one necessitating conception and nourishment during infancy). Such an improvement in the client's position vis-à-vis the contractor is manifested by more favourable terms such as a lower percentage management fee requested by the contractor, subordination of such fee to an agreed percentage return to the owner on his capital investment, equity participation by the contractor, and shorter renewal periods for the contractual arrangement (15).

Mention should be made of the particularly weak position of a contractor whose client's intentions towards a given hotel are of a short-term nature. If the client's real intention is to achieve a capital gain through the sale of an hotel, the contractor is in a 'catch twenty-two situation'. If good operating and financial results are achieved by the contractor, the client is tempted to sell (thus terminating the contractor's interest); if bad results are obtained, the client is influenced to appoint another contractor. To redress the situation, some contractors include provisions in their contracts requiring clients to obtain their consent before selling their property, or stipulating the retention of their contractual
### Position of Hotel Management Contractor and Client During their Working Relationship

<table>
<thead>
<tr>
<th>Contractor</th>
<th>Client</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Options</strong></td>
<td></td>
</tr>
<tr>
<td>Terminate contract and ignorance of terms.</td>
<td></td>
</tr>
<tr>
<td>(1) Enter agreement with new client. May be a lack of suitable hotels; terms may be less favorable. Need to improve on competitor's terms. Difficult to foresee client's degree of compliance. Time-consuming to negotiate.</td>
<td></td>
</tr>
<tr>
<td>(A) with broadly similar market. Lack of supply of clients with suitable hotels.</td>
<td></td>
</tr>
<tr>
<td>(B) in different geographical area e.g. overseas. Need to adjust to different operating conditions, demands, etc. Need to extend or establish new group services.</td>
<td></td>
</tr>
<tr>
<td>(C) with substantial difference in new market. Specialized expertise and reputation required.</td>
<td></td>
</tr>
<tr>
<td>(2) Become franchisee. Need to research and develop franchise scheme and administrative procedure. Time-consuming to locate and win franchises and sites.</td>
<td></td>
</tr>
<tr>
<td>(3) Purchase/lease hotels. Substantial capital requirements; exposure to risk; need to locate suitable existing hotel or sites.</td>
<td></td>
</tr>
</tbody>
</table>

| **Status** |
| Demonstrated ability as contractor to provide required operating and financial performance; reputation, stability and continuity as owner-operator; dimensions in terms of market penetration, number of hotels under operation, number of employees, capital, turnover, profit, and extent of group resources. |

| **Continuous input** |
| Operation management and control of hotel; provision of manpower, capability to attract guests through advertising, promotion, referral etc. Availability of advice and assistance in technical, operational matters; generation of revenue to client. |

| **Other influencing factors** |
| Ability to expand sales and/or market penetration by e.g. direct operation. Availability of alternative clients with suitable hotel; ability to resolve potential conflict of interest with directly-managed hotels; willingness to adjust to changes in client policy; flexibility in re-negotiating terms. |

| **Negotiating position** |
| Client's position enhanced by consumption of contractor's initial input of blue print of operation and disadvantages to contractor of alternative actions. Contractor's position influenced by favourable terms of agreement, and usually a long-term contract. |

| **Terms of Agreement** |
| Greater concessions made by contractor to client, including transfer of some financial risk to contractor. |

| **Options** |
| Main disadvantages: |
| Terminate contract and ignorance of terms. |
| (1) Enter agreement with new client. May be a lack of suitable hotels; terms may be less favorable. Need to improve on competitor's terms. Difficult to foresee client's degree of compliance. Time-consuming to negotiate. |
| (A) with broadly similar market. Lack of supply of clients with suitable hotels. |
| (B) in different geographical area e.g. overseas. Need to adjust to different operating conditions, demands, etc. Need to extend or establish new group services. |
| (C) with substantial difference in new market. Specialized expertise and reputation required. |
| (2) Become franchisee. Need to research and develop franchise scheme and administrative procedure. Time-consuming to locate and win franchises and sites. |
| (3) Purchase/lease hotels. Substantial capital requirements; exposure to risk; need to locate suitable existing hotel or sites. |

| **Status** |
| Demonstrated ability to finance project on initial and continuing basis; general business reputation, stability and continuity; concurrent employment of other contractors and/or direct management of own hotels; potential additional farms for hotels. |

| **Continuous input** |
| Supply of initial and continuing funds; exposure to financial risk; commitment to pay proportion of contractor's fee irrespective of trading outcome; means of additional exposure of contractor's brand to public (in some cases) and pre-emption of competition. |

| **Other influencing factors** |
| Genuine or equivocal attitude to agreed duration of contract; desire for long or short term trading benefits; willingness to comply with financial obligations; availability of competing contractors; unusual long-term nature of contract. |

| **Negotiating position** |
| Client's position enhanced by consumption of contractor's initial input of blue print of operation and disadvantages to contractor of alternative actions. Contractor's position influenced by favourable terms of agreement, and usually a long-term contract. |

| **Terms of Agreement** |
| Greater concessions made by contractor to client, including transfer of some financial risk to contractor. |
interests under the new ownership, or imposing substantial penalty clauses for early termination.

9.37 Summary of Findings and Comparison with Those of Surveyed Literature

The method of operating and financing hotels by hotel management contracts was found to be a new phenomenon in other than a few ad hoc arrangements, and was still a rare occurrence in Britain, though being increasingly used by British companies overseas. Due to the scarcity of such contractual arrangements in this country, the concept of hotel management contracts was not widely understood either by those within the hotel and catering industry or by a wider public.

In broad terms, hotel management contractors were seen to be meeting the needs of a variety of client types in arrangements which varied in duration from a short to long-term contract, and which included a diversity of roles ranging from the complete planning and implementation of new hotels to that of undertaking a salvaging operation of existing hotels suffering from financial or managerial problems.

Contractors operating management contracts within the parameters of this study were found to be few in number with, as yet, few hotels under contract. A wide difference was seen to exist between the overall size of those companies operating as contractors, some being chains or groups with world-wide interests in both directly-owned and managed or franchised hotels, and some being small independent contractors per se with no ownership of hotels. The group resources of these contractors varied extensively, some including very substantial assets, vast organizational establishments and a very wide range of expertise in technical and operating aspects.

Significant differences were found to exist between those clients with an intended medium to long-term arrangement with their contractors, and those with an intended short-term arrangement (as a salvaging or bridging operation).
An analysis of the terms governing hotel management contractual arrangements pointed to the generally obtaining comprehensiveness of standard management contracts, including precise definitions of financial and other terms, and detailed clauses relating to the financial and legal obligations of each party in given circumstances. There was, however, a general lack of definition in respect of operating standards and policies to be adhered to by contractors, indicating the difficulty of qualitatively and quantitatively defining services and environmental aspects. Fee structures were found to differ considerably, varying with the contractor and with each contract. Remuneration to contractors was more frequently calculated as a percentage of gross revenue plus a percentage of gross operating profit, and most frequently ranged from 2 to 5% of turnover plus 5 to 20% gross operating profit. The duration of management contracts normally ranged from ten to thirty years, though in the case of the small independent contractors it was more frequently five years, and was for even shorter periods where a 'salvage' operation was undertaken.

Contracts tended to be weighted in favour of contractors, evidenced by a lack of defined operating obligations, the transfer of financial risk to clients combined with relative safeguarding of the contractors' fees, and the long duration of many agreements with early termination possible, only in the case of substantial non-performance of terms. This more dominant position of contractors was found to be attributable to their normally relatively greater experience than their clients in such contractual arrangements; and to their clients' realization of their own inadequacy to provide technical, operating and managerial expertise in a business which was a major investment and potential profit centre, and involved a complex, twenty-four hour, year round activity, requiring supporting group services such as substantial advertising and promotional activities.
Although contractors and clients tended to measure the success of their arrangement almost entirely by their current respective financial returns, their relationship and the future performance of a given hotel were seen to be significantly affected by the tripartite interactions of client, hotel manager and contractor's head office. Depending on whether the managed hotel was identifiably operated under the name of either party, such interactions were also seen to have a potential effect on the other hotel interests of contractor or client.

Contractors, especially those with no direct ownership of hotels, were found to be in a particularly dependent position upon a supply of clients with adequate funds and hotel premises. They were thus affected not only by environmental factors which normally influenced hotel operators but also by factors influencing the attitudes and needs of prospective clients.

Potential growth in hotel management contract arrangements was seen to be very extensive in the context of certain developing areas of the world, where a demand for technical and operating expertise in hotel development and management was found to be combined with available capital and sites, and an acceptance of the contractual arrangement as a method of business. Growth of management contracts in Britain was also seen to have potential, particularly amongst existing independent hotels, but to be affected by the negative or neutral attitude of owners, towards client-status within an arrangement that was not widely tested in this country.

The most relevant work to these findings is that by Eyster (16), which examines in the context of the U.S.A. a number of similar aspects of the hotel management contract arrangement to those explored in this study. The extensive use of hotel management contracts in the U.S.A. and thus the large sample in Eyster's research, and the economic and attitudinal
differences between that country and Great Britain suggests that whilst Eyster's findings may be used as a basis for a broad, general comparison, no detailed comparison of the two studies would be valid.

An analysis by Eyster of the numerous contractual and financial terms currently obtaining in such arrangements substantially supports the findings of this researcher, though indicating slightly less favourable terms enjoyed by contractors in the U.S.A. (such as more generally imposed pre-determined levels of contractor performance, and less financial risk on the part of clients). Eyster's assessment of the attitudes of the two main parties to one another and his examination of the shifts in power resulting from the tripartite relationship including the hotel manager provide support to the related aspects of this researcher's theories concerning the interactions of participants in the contractual arrangement, and concerning the initial and subsequent positions of contractor: client.

Similarly, Eyster's assessment of the external economic and business factors causing the initial development of hotel management contracts within the U.S.A. accord in most respects with those outlined by this researcher for influencing the implementation of the few existing British arrangements in this country. The enormous difference in scale between such developments in the two countries as demonstrated by the two studies is likely to be mainly attributable to a significant difference in the American and British tax treatment of investment funds and income (thus influencing the supply of clients with a supply of hotels) and to the difference in prevailing attitudes towards management contracts of both hotel companies and potential clients in the two countries.
9.4 ASSESSMENT OF TIED HOUSE CONTRACTUAL ARRANGEMENT (17)

9.41 Nature of Two Main Parties

Brewery companies as a whole enjoyed a long-established and significant position within the general economy and within the hotel and catering industry. Their multiple role as producers, shippers, bottlers and distributors at wholesale and retail level, and their dual position as owner-operators of managed houses and landlords of tied trade outlets gave them very dominant status. Indicative of their overall size were their dimensions in terms of capital, number of distribution outlets, number of employees, gross revenue and net profit. Five major brewery companies were predominant in the industry. Their characteristics were for the most part comparable with each other, but tended to differ from those of smaller breweries, particularly in the relationship existing between brewer and tied house tenant.

The policies of responding brewery companies towards the tied house system were seen in general to be of maintaining the status quo in terms of numbers of tenanted houses, but of introducing a more commercial approach in their dealings with such tenants. There was found to be a tendency amongst major breweries of requiring a higher fixed rental payment from tenants, reducing to some extent the controls exerted over a tenant's business, enforcing such obligations as were retained in the contractual arrangements and in some cases requiring from tenants a larger capital contribution.

In general, tenants enjoyed a very modest status in contrast to the breweries, particularly during their initial negotiations with them. Most responding tenants lacked formal education and formal training, and brought to the contractual arrangement only modest capital resources together with their own (and families') labour. Most tenants initially lacked tangible indicators of status as employers in their own right or as generators of revenue and profit (18).
9.42 **Input to the Contractual Arrangement**

A detailed account has been given of the variations found to occur amongst breweries in their ability to offer and execute contractual terms and commonly expected services. In broad terms, all breweries satisfied an initial and continuing obligation to provide two major contributions to the arrangement: the supply of licensed premises in which the tenant could operate, and the provision of all or most supplies for the tenant to sell. Hence the major input by the brewery is seen to be both tangible and continuing, and is not consumed during the course of time by the tenant.

Reference has been made to the tenant's initial and continuing input to the arrangement in the form of their own motivated labour, small capital involvement, exposure to operating costs, commitment to pay a rental (through an agreed, fixed sum and, in some cases, an additional payment of a premium on supplies) and their position as a tied outlet for their breweries' products. Though varying in the extent of their particular adherence to terms and in their individual contributions, in general tenants are seen to make a continuing and tangible input, evidenced by their operating activity and by their financial returns to their breweries.

9.43 **Effect of Other Parties on the Contractual Arrangement**

Apart from the brewery and tenant, and the brewery's representatives such as a district manager (19), the other parties involved in or affected by the brewer-tenant relationship include directly-employed managers and other tenants of the same brewery company, managers and tenants belonging to other breweries, and customers. Their roles and relationships are shown in Diagram 9.7, and their interactions summarized in the matrix in Table 9.3.

Both the diagram and table indicate the direct relationship and interactions between the brewery and other parties, and point to the brewery's powerful and comprehensive position. Except for the normal roles of purchaser and seller between customers and tenants or managers, no direct relationships usually occur between the other parties. However, ad hoc
Diagram 9.7

Relationships of Main Parties in, or adjacent to, Tied House System

- Brewer
  - property
  - landlord
  - tenant
  - retailer
  - wholesaler
  - policy maker
  - entrepreneur in charge of 'own' business
  - recipient of gross revenue

- Tied House Tenant
  - no formal relationship unless on tenant liaison committee
  - supplier of brewer's product
  - entrepreneur in charge of 'own' business
  - recipient of gross revenue

- Public House Manager
  - unit manager
  - tenant manager
  - entrepreneur in charge of 'own' business

- Customers
  - purchasers of goods and services
  - providers of revenue

- Customers
  - purchasing of goods and services
  - providers of revenue

- Customers
  - purchasing of goods and services
  - providers of revenue

- Customers
  - purchasing of goods and services
  - providers of revenue

- Customers
  - purchasing of goods and services
  - providers of revenue
relationships may be formed by the creation of pressure groups amongst tenants or managers (both intra and inter-company), and the interactions created by the one group upon the other may be far-reaching, as they may be upon a given brewery or breweries in general.

Whilst such interactions are significant, the effects of any one tenant or manager upon fellow licensees of the same brewery through their effect upon customers is minimal. The overall lack of standardization of licensed premises (each being an individual package of range of products, services, facilities and environment) results in the lack of other than a very generalized brand image pertaining to each brewery and its outlets. Thus the creation of customer loyalty is likely to centre on a particular licensed public house rather than on the brewery outlets as a whole, though there may be exceptions in the case of premises where trade is mainly transient, in which case customer choice is influenced by the image previously created by other licensees of the same brewery.

9.44 General Environmental Factors Affecting the Two Parties

The tied house arrangement between breweries and tenants, is primarily affected by the economic and legislative environment in which it operates, its very existence being dependent upon continued government acceptance of the tied house concept, and the extent of brewery outlets being governed to some extent by liquor licensing legislation. The series of government reports on the brewing industry (20) produced recommendations for significant changes to be made to the tied house system (including a reduction in brewery control) and to licensing legislation. In Scotland some significant alterations to licensing law have recently been implemented, which may have a substantial effect upon the status of tied tenants in that country (21). In England and Wales no reform has been introduced as yet, but the publication of such proposals, together with a general trend towards commercial egalitarianism, has resulted in significant changes within the tied house system, including a slackening of brewery control over certain supplies of liquor and a reduction in the prevalence of levying a premium on supplies to tenants.
By placing some restraint on the expansion of public houses, liquor licensing legislation to some extent both restricts the growth of, and protects the existence of the tied house system. It is therefore an important influence on the number of tenants who may enter into arrangements with breweries, and on the overall policies of breweries towards their total distribution network.

The generally prevailing terms of tenancy arrangements, the attitude of participants and the extent of the breweries' interest in tied houses have also been affected significantly by such factors as the expansion of alternative distribution outlets for liquor sales, by inflation, and by concentration within the brewing industry.

There has been a significant increase, in recent years, in the number of restricted on-licences (in hotels and restaurants) and in the number of club licences (22). In addition there has been considerable growth in the number of off-license outlets such as discount stores and supermarkets which has increased the breweries' market for free-trade sales of canned and bottled beer and other products. Together these have reduced the proportion of sales from public houses, many of which are owned by tenants. Changes in the buying practise of consumers are influenced not only by the greater availability of liquor through these alternative outlets, but also by the price-cutting strategies of some, which have served to underline the inability of tenants to compete as long as the breweries maintain a policy of price differentials between free and tied trade outlets.

Inflationary trends in operating expenses attributable to licensed premises have had a two-fold influence. Breweries have experienced increased costs in their directly-managed outlets arising from greater expenditure on staffing within such units and on district administration necessary to control them. Combined with an imposed restraint on retail prices in such outlets (23), this has resulted in a move to turn unprofitable or marginal properties to tenancy, and has thus affected the ratio of direct:tenanted houses within the brewer-
ies' estate. At the same time, tenants have been affected by rising operating costs which have put pressure on their margins and resulted in their being less willing or less able either to pay an increased 'dry' rent or to undertake capital expenditure. The issue of rent increases has been further exacerbated by the recently acquired ability of breweries to raise their rental charges (following a period of imposed rent restraint), and by the re-structuring of the remuneration from tenants carried out by some breweries following the abolition of 'wet' rent payments which has necessitated an increase in 'dry' rent to compensate. Inflation, and particularly the rise in rental charges have been the source of major discontent amongst tenants, and have resulted in friction within the brewer:tenant relationship and have contributed towards the growth of tenant pressure groups.

Another factor which has resulted in significant changes to the contractual arrangement has been the relatively high cost of capital, which has influenced breweries to invest in their managed outlets (from which a higher return from both wholesale and retail margins may be expected) in preference to their tenanted premises. As indicated above, tenants have likewise been reluctant to undertake capital expenditure without reasonable assurance of an adequate return, such assurance being unlikely where tenants enjoy a very brief security of tenure. Rising consumer expectations for better facilities and for an improved environment in licensed premises have further underlined the need for capital expenditure. To rectify this situation there has been a trend by breweries to extend the duration of tenancies thereby encouraging greater investment from tenants in their houses. In some cases, long leases have been offered to tenants, thereby altering their status within the contractual arrangement.

The creation and growth of inter and intra-company tenant pressure groups within the last few years has undoubtedly influenced the contractual and financial terms between breweries and their tenants, and following the recent formation of the National Union of Licensed Victuallers (24), is likely to continue to do so. The more militant tenants have demanded the removal of brewery ties on the supply of wines and spirits and even the abolition of the tie on the supply of
beer - the latter tie in particular being regarded by breweries as fundamental to the tied house arrangement.

Concentration within the brewing industry has been instrumental in affecting the brewer-tenant relationship. Whereas there was previously a paternalistic attitude prevalent amongst small, family-owned breweries whose directors and top executives had a close relationship with tenants of long-standing, the tendency towards amalgamations and take-overs of small breweries has resulted in a reduction of such ties and given way to a more business-like relationship between the two parties.

Another important factor influencing the tied house system is the availability of prospective tenants. Indications were that most responding breweries enjoyed substantial waiting lists of applicants, whose varying temperaments and skills could in the main, be matched by brewers to appropriate premises and markets.

9.45 Alternative Options Initially Open to Two Parties

The difference between the positions of brewery and tenant is well-illustrated by the more feasible options open to the breweries than to tenants (see Diagram 9.8).

Most breweries have an existing alternative method of distribution to that of the tied house system through their directly-managed outlets (constituting additional tied outlets for the breweries' products). Although such a distribution channel could not quickly and effectively replace the tied house system, the existence of a core of directly-employed public house managers, of district managers to control such outlets, of existing group services geared to the needs of the managed
estate, and of the existing capital investment in distribution outlets, indicates that such a change in distribution channels would be feasible at least in respect of a small proportion of units, and certainly could be used as a negotiating weapon vis a vis any one tenant. In addition, the reported abundant supply of prospective tenants applying to some breweries provides those breweries with a ready alternative to continuing a contractual arrangement with any given tenant. Mention has been made of the considerable increase in the proportion of brewery sales through free trade outlets (including on and off-licenses), which thus provide alternative and expanding channels for liquor distribution, at the same time as reducing to some extent the tenants' significance as distribution outlets.

Options open to tenants reveal significant disadvantages. Though differing in detail, the terms offered by other breweries are broadly similar, and tenants are thus unlikely to improve substantially their position by entering into contracts with another brewery. In terms of business independence, tenants are unlikely to desire to step back into a managerial position, either with a brewery or as manager for another tenant. Thus, if tenants wish to remain in the brewery trade, the only real alternative for them is to consider purchasing a free house. The considerable capital expenditure necessary for such a move, the restricted availability of such houses, and the consequent exposure to financial risk are substantial disadvantages.

9.46 **Dynamics of Relationship**

The initial negotiating positions of brewer and tenant are summarized in broad terms in Diagram 9.8. The very substantial status of the brewer in contrast to that of the tenant, and the proposed input by the brewer (encompassing the majority of capital for the business and the supply of products) together
Diagram 9.8

Initial Negotiating Position of, and Likely Outcomes Between Brewer and Tied House Tenant

**BREWER**

- **STATUS** influenced by:
  - Reputation on producer, wholesaler and retailer; ownership of brand name; lengthy experience in brewery trade.
  - Dimensions in terms of extensive production and delivery systems, extensive ownership of distribution outlets, substantial employer, significant generator of revenue and profit.

- **OPTIONS**
  - **MAIN DISADVANTAGES**
    - Need for expansion of outlets
    - Pressure on brewery to reduce operating costs; need to compensate for turnover in tenants.
  - **ADVANTAGES**
    - Pressure from tenant groups, a government to retain dual distribution system; increased requirement for capital resources; exposure to operating costs; problem: Need for reliable motivated unit and area management.
  - **PROPOSED INPUT**
    - Substantial capital contribution of site, building and bulk of contents; licensed outlet for liquor sale; supply and delivery of all/most products to be sold/continued advertising and promotion to stimulate sales.
    - Availability of some technical and operating advice and assistance.
  - **PROPOSED OUTPUT**
    - Small capital contribution for tenancy fixtures & fittings & working capital; Con labour & motivation to boost turnover; reduce costs, improve service; exposure to operating costs & problems including staff employment; continuing payment of 'dry' rent and continuing purchase of all/most supplies and 'wet' rent if applicable.

- **OTHER INFLUENCING FACTORS**
  - Ability to attract suitable applicants for tenancies; Policy towards and capability for expansion via directly managed outlets; Short-term nature of contract.

- **NEGOTIATING POSITION**
  - Heavily dominated by brewery, due to his ownership of outlets, role as producer, wholesaler and competing retailer, lengthy experience, feasible alternatives and to the conservative insubstantiality of tenants. Lack of alternative options and need for frequent renewal of contract.

**TENANT**

- **STATUS** influenced by:
  - Age or limited business experience and reputation as entrepreneur; Amount of previous experience in brewery trade (often nil or negligible).
  - Dimensions in terms of small capital available, difficult access to finance, and usually not an employer or revenue and profit generator in own right, no ownership of units.

- **OPTIONS**
  - **MAIN ADVANTAGES**
    - Freedom, authority; Restricted opportunity to increase earnings.
  - **ADVANTAGES**
    - Need for large capital investment; Exposure to risk; Scarcity for skill & experience in public house management; Restricted availability of such premises.
  - **OTHER INFLUENCING FACTORS**
    - Personal suitability for role as tenant, i.e. as semi-independent businessperson; Ability as to geographical location; Attitude to alternative options.

- **NEGOTIATING POSITION**
  - Heavy dominated by brewery, due to his ownership of outlets, role as producer, wholesaler and competing retailer, lengthy experience, feasible alternatives and to the conservative insubstantiality of tenants. Lack of alternative options and need for frequent renewal of contract.

- **TERMS OF AGREEMENT**
  - Almost no negotiating ability on part of tenant, except in respect of amount of 'dry' rental.

*excluding substantial companies in position of tenants.*
with the tenant's short tenure and frequent reliance upon the brewery to renew his contractual agreement results in the brewer's substantially more powerful position. This is further indicated by the relative lack of feasible alternatives open to an individual prospective tenant in contrast to those open to a particular brewery. The effect of the brewer's dominance is revealed in standard contracts which emphasize the rights of breweries and obligations of tenants, whilst almost totally ignoring the rights of tenants and obligations of the breweries. Further emphasis is given to the brewer's powerful position by an almost complete lack of negotiating ability allowed to tenants, who must accept or reject the offered terms, but may not alter them.

The subsequent position of the two parties during their working relationship is shown in Diagram 9.9. In practical terms, the tenant's status has improved, resulting from his demonstrated capacity as a 'semi-independent' entrepreneur, including tangible evidence of his role as employer and generator of turnover and net profit. His knowledge and experience as a licensee have increased substantially, perhaps through training, advice or assistance offered by the brewery, and certainly by day to day exposure to trading conditions (during which time he has been protected to some extent by the brewery's guidance).

Although the tenant's status has changed over a period of time, and his input to the contractual arrangement is likely to have increased (through his creation of customers loyal to his outlet, and thus an increase in revenue and payment to the brewery(25)), the contractual and financial terms governing the particular arrangement remain substantially the same.

The brewery's status has not altered and the brewery's continued input to the arrangement - that of the major capital investment and all or most liquor supplies - remains both essential and tangible. The tenant's alternative options to continuing the contractual arrangement with his brewer present greater difficulties, than do those of the brewer. Hence, within the relationship, the position of brewer and tenant does not materially
Diagram 9.9
Position of Brewer and Tied House Tenant During their Working Relationship

**BREWER**

**STATUS**
Influenced by
- Demonstrated capacity as producer, wholesaler & retailer; Demonstrated capacity as landlord; Continuity & market performance of system; Dimensions in terms of ownership of production & delivery facilities; number of tenants & employees, financial performance.

**OPTIONS**
- Renew tenant's tenancy
  - Main disadvantages: Tenant may be ineffective and losing/not increasing sales volume; Tenant may be contributing terms of agreement; Brewer obtains only wholesale margins plus 'dry' rental.
- Recruit other tenant
  - Time-consuming to interview & vet; Difficult to forecast potential performance; Brewer incurs only wholesale margins plus 'dry' rental.
- Change tenants outlets to direct management & establish new houses under direct management
  - Pressure from tenant groups, government, against such trends; Increased requirements for capital; Additional exposure to risk; Increased need for reliable motivated unit & area management.
- Increase sales via free trade outlets
  - Lack of control over distribution outlets; Need to recruit more free trade representatives.

**OTHER INFLUENCING FACTORS**
- Desire & capacity for growth by directly managed outlets. Impact of competing methods of liquor distribution on off-licence sales, supermarkets etc.
- Popularity of brewer with prospective tenants; Attitude to tenant's desire for growth. Short-term contracts.

**TENANT**

**STATUS**
Influenced by
- Demonstrated capacity as tenant-liquorist in terms of authority & responsibility; role as employer & generator of revenue & profit; Perceived capacity to influence local customer loyalty; Dimensions of small capital available, no ownership of unit, no separate source of supplies.

**OPTIONS**
- Renew tenancy
  - Main disadvantages: Depend upon brewer to renew tenancy/depend on brewer to fix realistic 'dry' rental
- (a) for same premises
  - (b) for other premises
- Become brewery employed manager for own/brewery
  - Constrains on freedom & authority; Restrictions on increasing earnings.
- Become owner of Free House
  - Need for large capital investment; Exposure to risk; Restrictions on availability of such outlets.
- Become tenant of other brewery
  - Terms offered may not be substantially different.

**OTHER INFLUENCING FACTORS**
- Reaction to brewer controls over tenant's business; Realization of own capacity as entrepreneur, a personal effect on local market; Extent of capacity to adjust outlet to local demands; Desire to increase unit holding/move to better outlet.

**TERMS OF AGREEMENT**
- Tenant's negotiating ability remains minimal. External forces cause slight improvement in tenant's status and elimination of harsher terms.
alter during the course of time, although the self-esteem and expectations of the tenant may undergo considerable changes. This discrepancy between a tenant's business development and his relatively static and subordinate position demonstrated by the unchanging nature of his individual contract with his brewer is perceived to be an important element in the cause of tenant unrest. Although reference has been made to generally prevailing changes in the terms governing the brewer: tenant relationship, these have been instigated by external causes (including collective action by tenants) rather than from cognizance of development within individual relationships.

9.47 Summary of Findings and Comparison with those of Surveyed Literature
As a long established and extensively-used method of distribution by breweries, the tied house system was seen to be an arrangement whose concept and organization were widely understood by participants and the general public. Such a contractual arrangement was seen in broad terms to have met the needs of breweries, their tenants and the consuming public for more than two centuries and though undergoing certain important changes, was found to be an arrangement that, overall, was still desired by participants and prospective participants.

Following concentration within the brewing industry, five major breweries were found to predominate, whose relationships with their tenants differed to some extent from those of the smaller breweries, and whose overall group resources covered a wider range of services and expertise (though these were not necessarily either specifically offered to, or used by tenants).

Payments to the breweries was normally based on a dual system of 'dry' plus 'wet' rent, calculated respectively as a fixed monthly sum plus a premium on supplies, though there was a move by some major companies to eliminate the levy of a premium on supplies and to be paid a 'dry' rent only. The duration of tenancy agreements was found to vary between one and three years, with a one year period for notice of termination,
although a number of respondents enjoyed three year tenancies and six months' notice of termination. The standard tenancy contracts of the responding breweries exhibited considerable similarity with each other, being drafted in comparable terms, with a similar layout and content, emphasizing tenants' obligations and breweries' rights.

Most breweries maintained a strict tie on the supply of beer, wines and spirits to their tenants, and the smaller companies also controlled their supply of minerals, fruit juices and tobacco.

The dominant position of the breweries was seen to result from their almost complete control over their tenants' supplies of liquor, their ownership of distribution outlets and their experience of tenancy arrangements; such dominance being manifested in tenancy contracts which were heavily weighted in their favour, and in the relatively short periods of tenure permitted to tenants. Except for some manoeuvrability in respect of the 'dry' rental payment, most tenants on an individual basis enjoyed no negotiating ability with their breweries.

Potential growth of the tied house system was found not to be restricted by a lack of prospective tenants, but to some extent by restrictions on the overall number of licences issued for public houses by licensing justices, combined with the policy of breweries not to alter significantly the ratio of tenanted: directly-owned outlets within their respective estates, and by the lesser returns to be gained on capital investment in tenanted houses compared to those obtained from managed outlets.

The main significance of other parties involved in or affected by the brewery:tenant relationship was found to be the potential effects of pressure groups of either tenants or public house managers upon each other or upon their own brewery or breweries in general. Such pressure together with the possibility in England and Wales, of fundamental changes being brought upon the tied house system and upon its participants through suggested changes to legislation, or through governmental regulations were seen to be important environmental
factors that had influenced existing arrangements and were likely to continue to do so.

These forces external to individual relationships between brewers and tenants were found to be the causes of significant changes to the contractual arrangements, rather than the realization by brewers of the dynamics of each relationship. The perceived growth in business development of tenants was found not to be acknowledged by breweries either through changes in contractual terms or through significant changes in practice.

Although the context of the four governmental reports mentioned in the surveyed literature (26) was substantially different from that of this study (being concerned with the breweries and public issues, rather than the brewery:tenant arrangement), a number of areas covered by the reports provide a useful basis for comparison with this researcher's findings.

Substantial differences were found to exist between the findings of the Monopolies Commission and those of this researcher in respect of brewery policy towards tenants and in the details of their contractual arrangements. As both surveys included the major breweries (then six, now five) and some smaller breweries, such differences are not attributable to a sample bias but to a significant change in brewery policy during the decade or so between the two studies. Thus it seems that the former paternalistic attitude of brewery companies towards their tenants (mentioned by the Commission and evidenced by the system of 'wet' rent payments, very short periods of tenure, strict controls and obligations upon tenants, combined with a lenient interpretation by the brewery, and lack of enforcement of the harsher terms) has given way to a more commercial outlook. At least among the major breweries this is evidenced by the elimination of the 'wet' rent and increased 'dry' rent which puts more risk upon the tenant (and allows potential for greater rewards) and by a permitted longer period of tenure, a reduction of the number of controls and detailed obligations, and a less lenient interpretation of such controls and obligations as are retained.

The suggestion by the Monopolies Commission/that tenants lacked entrepreneurial drive must be questioned in the light of responses obtained in this survey, which indicate that at least a significant minority
of tenants now do not accord with this description. Likewise
the findings in respect of average turnover and profit of tenants,
reported by the National Board for Prices and Incomes, have been
outdated by this research, (28).

It is suggested that the act of publishing the government
reports in itself contributed to the various differences which
have been found to occur within the tied house system, between
the 1960s to early 1970s and now, together with other external
forces, such as the growth of collective bargaining amongst
licensees, as outlined by Hawkins (29). The content of the
brief article by Hawkins substantially accords with the findings
of this researcher in respect of the reasons for changes in the
brewer:tenant relationship, illustrates some of the contractual
changes which this researcher has indicated, and provides
material which supports the conclusions in this study of the
potential significance of interactions between groups of licensees.

9.5 ASSESSMENT OF FRANCHISING (30)
9.51 Nature of Two Main Parties
Franchisors in general were found to be a relatively new
phenomenon in the business environment, and (with one notable
exception) in the hotel and catering industry. The size and
status of individual franchisors varied widely. A few fran-
chisor companies had extensive interests in franchising and
in supporting comprehensive group services; other companies
directly owned and operated a substantial number of outlets but
enjoyed a minimal interest as franchisors per se. Some fran-
chisors of currently small dimensions were either in the process
of initial development of their system, or merely enjoyed a
very limited representation within the parameters of this study,
whilst having very extensive interests in a wider context. In
general, most franchisors displayed substantial characteristics
of total company size and resources, and of an extensive
interest in directly-owned and operated and/or franchised outlets
of one or more systems. Their attitude towards franchising
was seen to vary between those who displayed long-term intentions
towards using franchising as a major if not exclusive method
of system innovation or significant expansion, and those who
were seen to use franchising as an ad hoc or short term measure to overcome specific problems. However, no evidence was found amongst the few, well-established organizations in which the franchising method was used to a significant extent, of any substantial degree of re-purchasing by the franchisor of franchisees' outlets so that they might be operated on a directly-owned and operated basis by the franchisor.

Franchisees were found to be of two distinct types: single franchisees and multiple franchisees. Respondents in the first category were found in general to lack formal educational attainments and formal training of relevance to their franchised activity. Most had not been self-employed and therefore lacked tangible indicators of their capacity as employers in their own right or as generators of revenue and profit. The majority of those interviewed had prior relevant experience within an hotel or catering activity and/or had been in a supervisory or middle management position within or outside the industry. The most frequent reasons given by franchisees within the survey for becoming franchisees hinged on the perceived safety of operating a business that had been previously tested and found viable and on the supporting services provided by the franchisor, together with the notion of consequent independence or semi-independence.

Multiple franchisees (31) within the survey had widely different interests which ranged from those whose entire business was devoted to multiple outlets of one given franchise system, to those with world-wide interests in one or more industries or economic sectors and franchised outlets for one or more franchise systems. Some franchisees had grown to multiple status through gradual development of outlets within one system (having initially been single franchisees) whilst others had assumed such status through acquisition or development of franchised outlets on a large scale. All multiple franchisees showed evident characteristics of size, status and business expertise; some had extensive group resources of their own for development and operational management. The motivation for substantial companies to become
franchisees was found to be mainly that of desiring to enter
a given market without the time-consuming and expensive necessity
of developing their own system, and then having to compete against
the system which they were emulating. The attitude of franch-
isees in general towards their franchising arrangement exhibited
certain dichotomous traits. Most stated that the units opera-
ted by other members of the franchise system should be controlled
more closely; and most suggested certain changes which ought
to be made to particular products or to the total concept of
the system. However, at the same time, the majority of fran-
chisees acknowledged minor and in some cases major departures
in their own units from the system's standardized procedures
and products, and stated their resentment over controls that
could be or were exercised over them by their franchisor. A
number of franchisees also said they were unwilling to imple-
ment innovations that had been suggested or required by their
franchisor in order to render the products or total concept
more closely in accord with demand. Thus the majority of fran-
chisees were of the opinion that they, themselves, should be
allowed discretion to operate their units in accordance with
particular demands of their local market and in a manner which
they considered suitable, whilst regarding such actions by others
as likely to blur the system's image and to cause unfortunate
repercussions amongst system members.

9.52 Input to the Contractual Arrangement

Though variations were found in the proffered contribution to
a contractual arrangement by franchisors, and in their ability
to execute such services and such obligations as were agreed,
in broad terms all franchisors within the survey made a major
initial contribution to the arrangement by providing a complete
business package (including the plans, design, equipment and
stock inventory, policies, systems, methods and training to
operate the given unit) and an entree to an 'instant' market,
through permitting the use by the franchisee of an established
brand identification. The nature and extent of the continuing
contribution by franchisors to the arrangement was more variable.
Some franchisors made a continuing contribution by providing
all or a significant proportion of goods to be sold by the franchisee; others undertook no such activity, or merely supplied one particular ingredient. Some franchisors made a continuing input to the arrangement by providing extensive advertising and promotional services including, in the case of hotels, tangible evidence of such activities in the form of room reservations transmitted via, or directly attributable to the franchisor; others made only a token contribution to the arrangement by limited activities in this field.

The franchisor's continuing input in the form of advice and assistance in operating and technical matters was more evidently available in some systems than in others, and was more likely to be required in units involving complex activities of production, selling and management (such as in hotels) than in units involving only a simple process of selling a restricted range of pre-prepared products (such as in some 'take-away' outlets). Hence franchisors were seen to vary between those whose continuing contribution to the arrangement was perceived to be essential and tangible, and those whose continuing input was perceived as inessential or ineffective (due either to lack of activity or to its intangible or unquantifiable nature).

Though varying in the extent of their initial contribution to the contractual arrangement, in broad terms franchisees provided the site and premises through which the franchisor's products could be sold (32) together with a small initial payment. As a continuing contribution franchisees agreed to provide their own or hired labour to supply the franchisor's goods and/or services, and agreed to exposure to operating costs, to financial risk, and to making a regular payment to the franchisor, either as a percentage royalty on turnover or as a premium on supplies. The continuing input by franchisees varied with their particular environment and operating and financial capabilities, but in general terms may be divided between a quantifiable contribution (in the form of a payment to the franchisor)
and an unquantifiable contribution (in the form of a tied outlet for the franchisor's products, thus pre-empting competition, and the effect of a motivated labour force on the consuming public and thus on the system's brand image).

9.53 Effect of Other Parties on the Contractual Arrangement
The parties involved in, or affected by the franchising arrangement are shown on Diagram 9.10, and include, as well as the franchisor and franchisee, other franchisees within the system, managers of units owned by the franchisor, unit managers directly employed by franchisees and customers (33). The diagram indicates both the comprehensive nature of the franchisor's role towards franchisees (as owner of the concept, as supplier (in some cases) of products to be sold and as contractual controller of policies, operating methods etc) and the franchisor's role towards directly-managed units. Table 9.4 summarises in broad terms the interactions between the principal participants in a franchise system. It points to the considerable interdependence arising from membership of a system in which the existence of standardization and consistent brand image are an integral part (though varying in degree). The likely effect upon system members resulting from the actions towards consumers of those operating distribution outlets is clearly indicated. Also shown are the different consequences upon the franchisor and upon franchisees of over-development of a given area, and the different interests of the two main parties in sales maximization on the one hand, and profit maximization on the other. The potential effect of franchisee pressure groups upon other parties is also indicated.

9.54 General Environmental Factors Affecting the Two Parties
Franchise systems, and thus the two parties, are subject to many external influences similar to those affecting non-franchised systems, but such factors often affect franchise systems differently from non-franchised systems and may influence to a significantly different degree the two parties to each arrangement. In addition, franchise systems are further influenced by external factors which directly relate to franchising per se.
Diagram 9.10  Relationships of Main Participants in or adjacent to Franchise System

Owner of tied distribution outlet, contractually governed instrument for transmission of goods and services, contributor to franchisor income, contractual controller of goods and services

Franchisor

employee-agent for transmission of goods and services, direct employer, collector of revenue

Single Franchisee

as for single franchisee

purchasers of goods and services, collector of revenue

Customer

Key: ...... signifies no formal relationship.
Changes in the levels of consumer spending, or alterations in consumer habits (such as an increase in purchasing 'take-away' food or decrease in eating out), or changes in food preferences (such as a decline in eating fish and rise in the consumption of pizzas) affect both non-franchised and franchised systems. However, franchise systems, consisting of numerous, separately-owned units, present two characteristics: rapid implementation of a new concept to cater for a perceived new market; and subsequent difficulty in fundamentally changing such a system to meet altered demands. Thus changes in consumer patterns create conditions of specific significance to franchising per se.

Where such changes occur on a wide-spread basis, in broad terms both franchisors and their respective franchisees are equally affected. But if these changes occur on a local or regional basis they are likely to be of major significance to franchisees within those areas (whose business interests are concentrated therein) whilst being of less importance to franchisors (whose interests are likely to be spread over a wider geographical area and may include activities in other systems or markets). Thus environmental factors such as regional or local unemployment, redevelopment, or the non-acceptance in certain areas of food products or systems which are generally widely-accepted, affect franchisors and franchisees to a significantly different degree.

Factors influencing the availability of suitable sites for development of units affect franchise systems as they do non-franchised systems, but also have a further dimension in their particular effect upon franchisors and franchisees. Such factors include competition from other businessmen for available sites, local planning regulations (including in some cases restrictions on the use of premises), regulations affecting the erection of signs and other branding material, and permitted trading hours. Depending on the extent to which these factors occur on a local or wide-spread scale, they may affect only a few franchisees or be of significance to an entire franchise system. If there are wide-spread regulations restricting the
number of sites suitable for unit development or causing substantial alterations to be made to the standard external image of system units (by imposing planning and advertising restraints), the market penetration of a given system is likely to be severely retarded, thus affecting both the franchisor, existing franchisees and prospective franchisees. Similarly, a generally obtaining restriction on trading hours reduces the sales volume of system units (thereby affecting the franchisor's income obtained from a royalty on turnover or premium on supplies), and also is likely to influence both the viability of existing units and the development of the system through the impact upon prospective franchisees.

The choice of site open to a franchisee is affected not only by the normal environmental factors influencing the feasibility of a given site, but also by constraints imposed by a franchisor's existing or planned network of distribution outlets, thereby further reducing the number of sites which the franchisee may consider. Where a franchise system requires, for the success of its units, the fulfillment of either a combination of numerous factors and/or of particular specialized factors (for example for hotels or units in highway locations), the relative scarcity of suitable sites considerably affects franchisee expansion and thus growth of the franchise system.

The supply of suitable franchisees for participation in hotel or catering franchises is affected by three categories of environmental factors: those influencing general attitudes towards working in the hotel and catering industry; those affecting attitudes towards self-employment and franchising as a method of entrepreneurial activity; and those bearing upon the suitability of individual franchisees for such a role. The first category includes broad issues of relevance to franchised and non-franchised interests within the hotel and catering industry, such as the general image of employment within the industry, government policies towards hotel or catering businesses, and the attitude of financial institutions towards funding such activities. The supply of suitable franchisees is further influenced by prevailing attitudes to working as a direct employee (affected by income tax and wage restraint policies), by the climate affecting small businesses in general (including
government policies and attitudes of lending institutions), by the level of unemployment, and by the general knowledge and understanding of the franchising method amongst potential franchisees.

The suitability of prospective franchisees for such a role is influenced by the extent of their own or the availability of loaned capital and by the particular characteristics of a given franchisee, including his capacity to undertake a quasi-independent role on a prolonged basis. Whereas the amount of capital involved in a 'take-away' outlet or the majority of franchised restaurants is relatively small, and thus unlikely to pose a serious obstacle to intending franchisees, this is not the case for those wishing to embark on a hotel franchise or to join a restaurant system in which an extensive and sophisticated inventory of storage, production and service equipment is required. The general reluctance shown by financial institutions to invest in hotel and catering ventures or in those involving franchising has been an important factor in the lack of growth amongst franchise systems requiring such very substantial investment.

Also of particular consequence to the franchise arrangement are general inflationary trends, which fall primarily upon franchisees (through their exposure to fixed and operating costs in their outlets) but which also affect franchisors either directly (in their wholly-owned outlets and in system administration costs) or indirectly (through their long-term effect on the viability of all franchisees within a system). The direct burden upon franchisees of rising operating costs is underlined by the franchisees' customary inability to avoid such additional expenditure or to pass it on to customers. In circumstances where franchisors supply the bulk of products to be sold or used by the franchisee, any additional costs incurred by a franchisor are normally passed on to franchisees. However controls exercised by franchisors often prevent franchisees from raising their selling prices, and frequently impose operating standards which prohibit, for example, any reduction in staffing levels, portion sizes or levels of lighting, and thus preclude a decrease in
related costs. Thus, whilst franchisees are prevented from maintaining or improving on their existing profit margins, franchisors are able to pass on their production or handling costs of supplies and, by basing their income as a percentage of franchisees' turnover, not on franchisees' profitability, are linked to, but protected from, inflation. Thus inflation may emphasize the difference in exposure of the two parties and, particularly where a franchisor is perceived to be charging higher prices for supplies than in the market place, may be instrumental in causing a fundamental rift between a franchisor and his franchisees.

Such pressure on franchisee margins has been a factor causing some franchisees to fall behind in re-investment in their units, with a resultant deterioration in their standards of decor and hygiene and down-grading of the franchise system's image. Reactions of franchisors to this situation have included the introduction, in recent contracts, of more precisely defined obligations relating to redecoration etc., and have prompted moves by franchisors towards demonstrating in their wholly-owned units the financial advantages to franchisees resulting from re-investment in such units.

Legislation and regulations affecting hotels, restaurants and 'take-away' units in general, similarly affect franchise systems, by regulating the activities of franchisees in their units (for example in respect of employment practices and hygiene) and thus influencing their individual viability, and by their impact on a franchise system as a whole. In common with other chain interests, any publicity given to abuses by one or more franchised units of such legislation, is likely to damage the image of the whole system.

Competitive hotel, catering or 'take-away' systems are likely to affect members of a given system, though the extent of their influence depends on the product and on the overall distribution and respective market shares of the competing organizations. Thus where competitors are perceived to offer a challenge to
an existing franchise system, this affects both the franchisor and franchisees; whilst the implementation of a few competing outlets in a restricted area is likely to be of significance only to franchisees in the same catchment area.

A further factor influencing the two parties has been the establishment of a few intra-company franchisee groups, in the major franchise systems, formed to channel franchisee opinion (and in some cases dissatisfaction). Though as yet not displaying significant strength, such a group in one franchise system has been given the chance to influence that company's marketing and purchasing policies and expenditure. In two other systems franchisees meet regularly to discuss amongst themselves and with franchisor representatives, common problems and policies affecting the systems as a whole. Whilst the impact of such groups is minimal in comparison with those established in the U.S.A., their existence is a factor which may have ramifications in the future.

9.55 Alternative Options Initially Open to Two Parties
The courses of action open to the two parties as an alternative to entering a mutual franchise agreement are summarized in Diagrams 9.11 and 9.12, referring respectively to single and multiple franchisees. The options open to the franchisor depend on his existing interests in wholly-owned and operated outlets (the viability of which as the sole method of distribution for the system determine his dependence on using franchisees). The availability of suitable prospective single and multiple franchisees is also a significant factor.

The dependence of single franchisees on their franchisor's proposed input, and their relatively insignificant status leads to a dearth of suitable alternative options for them in the role of 'independent' entrepreneurs. Multiple franchisees (ie. those commencing negotiations with a franchisor as a multiple franchisee, and excluding those reading such status by gradual acquisition subsequent to single franchisee status) are shown to have more feasible alternatives open to them, which however offer disadvantages stemming from expenditure of time and money.
Diagram 9.11

Initial Negotiating Position of, and Likely Outcome Between Franchisor and Single Franchisee

**Franchisor**

<table>
<thead>
<tr>
<th>OPTIONS</th>
<th>main disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Retain status quo</td>
<td>Inability to increase market penetration of particular regions, areas or sites; restriction on growth in turnover and profit; Pre-emption by competitors.</td>
</tr>
<tr>
<td>Locate other single franchises</td>
<td>May be restricted availability of suitable applicants; May not have suitable site/unit or may have other locality; Time-consuming to vet.</td>
</tr>
<tr>
<td>Locate multiple franchises</td>
<td>As immediately above, may dilute system image; May have too strong a negotiating stance and obtain significant concessions.</td>
</tr>
<tr>
<td>Establish directly-owned and managed units</td>
<td>Greater drain on human resources and franchisor capital; Slower to penetrate market; Greater exposure to risk; Need to find sites; Need to locate suitable unit management.</td>
</tr>
</tbody>
</table>

**SINGLE FRANCHISEE**

<table>
<thead>
<tr>
<th>OPTIONS</th>
<th>main disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Remain/become employee of employer</td>
<td>Constraints on freedom; no opportunity to build equity; or increase earnings.</td>
</tr>
<tr>
<td>Remain/become independent operator</td>
<td>No or limited experience; time consuming and costly to create business; exposure to risk; no group resources for support and inability to compete with established systems.</td>
</tr>
<tr>
<td>Join other franchise system</td>
<td>Limitations on choice of franchise system of particular products, markets or geographical areas may be unfavorable by franchisor; may offer harsher terms.</td>
</tr>
<tr>
<td>If hotel owner, join a consortium</td>
<td>May not offer a wide enough span of services, or sufficient competitive advantages, limitations on choice of consortia or regional penetration.</td>
</tr>
<tr>
<td>If hotel owner, hire a management contractor</td>
<td>Less control by owner over day-to-day administration; may be more expensive than franchising; may involve long-term agreements.</td>
</tr>
</tbody>
</table>

**STATUS**

- **Franchisor:** Ownership of concept, initiator of system, experience of system; Established system, head office organization, continuity and stability; Dimensions in terms of market penetration, substantial no. of units, participation franchises, directly-employed staff, generator of turnover, profit; More substantial amount of capital than franchisee.

- **SINGLE FRANCHISEE:** No or limited business reputation or experience as entrepreneur; No or limited experience of catering/hotel trade; Dimensions in terms of small capital available; difficult access to finance; not an employer in own right; nor generator of turnover; no ownership in units.

**PROPOSED INPUT**

- **Franchisor:** Tried and proven concept, thus a reduction in risk, time and cost; Blue-print of premises, decor, layout, equipment, inventory, policy, methods; Initial & continuing market acceptance of product through brand image; Availability of group resources for advertising, purchasing, technical assistance, training etc. Producer of, or agent for supplies. Possible financial leverage for franchises.

- **SINGLE FRANCHISEE:** All or substantial amount of capital/labor &/or responsibility for hiring employees; Motivation to maximize sales and provide best possible goods & services; Responsibility for operating costs; Exposure to financial risk; Continuous payment of royalties &/or premium on supplies &/or rent; Initial payment of franchise fees; Provision of suitable site and asked exposure of system to public.

**OTHER INFLUENCING FACTORS**

- **Franchisor:** Ability and desire to expand throughout ownership and operation; Experience of assessment of franchising method; genuine/equivalent attitude to long-term franchising arrangement; Ability to attract abundance of suitable prospective franchisees.

- **SINGLE FRANCHISEE:** Suitability of personality, desire for independence but compliant; Need for effective organization; Desire for membership of particular franchise system; Flexibility in respect of operating locality or particular site; Desire for future expansion.

**NEGOTIATING POSITION**

- **Franchisor:** Substantially in favor of franchisor because of status, experience, and feasible alternatives; dependence of franchisee on franchisee’s input and disadvantages of franchisee’s options.

**TERMS OF AGREEMENT**

- **Franchisor:** Because of franchisor dominance, almost no negotiating possible by franchisee. Terms emphasize franchisor rights and franchisee obligations.
Diagram 9.12

Initial Negotiating Position of, and Likely Outcome Between Franchisor and Multiple Franchises

**FRANCHISOR**

- **OPTIONS**
  - Maintain status quo
  - Locate more single franchises
  - Establish directly owned and managed units
  - Locate other multiple franchisees

- **PROPOSED INPUT**
  - Tied and proven concept and thus a reduction in risk, time and cost
  - Blue-print of proven success, layout, equipment, inventory, policies, methods.

- **OTHER INFLUENCING FACTORS**
  - Ability and desire to expand through direct ownership and operation.
  - Need for particular sites or area/regional penetration.
  - Genuine/equivalency attitude to long-term franchising.
  - Desireability of concept to single/multiple franchisees.

- **NEGOTIATING POSITION**
  - More evenly balanced than in case of single franchisees, because of multiple’s evident status and expertise.

- **TERMS OF AGREEMENT**
  - Greater negotiating capacity and therefore better terms in franchise contract in favour of multiple franchisee than in respect of single franchise.

**MULTIPLE FRANCHISEE**

- **OPTIONS**
  - Retain status quo and ignore
    - perceive a lack of particular franchised market segment’s franchised concept.
    - Develop own concept/identity or
      - a new concept/identity or
      - a compatible concept
      - own units.

- **PROPOSED INPUT**
  - All or substantial amount of capital.
  - Availability of existing site(s) or resources to locate site(s).
  - Responsibility for operating costs and profits, including employment of unit managers and staff.
  - Exposure to financial risk.
  - Expertise in business management is possible in relation to similar system, responsibility for group resources (e.g., training, area supervision).
  - Initial payment of franchise fee.
  - Ongoing payment of franchise royalty and/or premium on sales and/or net.

- **OTHER INFLUENCING FACTORS**
  - Desire for participation in particular system and viable alternative systems.
  - Capacity to initiate and develop similar systems of own.

- **NEGOTIATING POSITION**
  - Fewer, because of multiple’s evident status and expertise.

- **TERMS OF AGREEMENT**
  - Greater negotiating capacity and therefore better terms in franchise contract in favour of multiple franchisee than in respect of single franchise.

* = ‘instant’ multiple franchisees, not including those who have grown to such status by gradual acquisition of units subsequent to single franchise status.
A summary of the initial bargaining position between the franchisor and single franchisee is depicted in Diagram 9.11. This reveals the normally much more substantial status of the franchisor in contrast with that of the franchisee, the more feasible alternative actions open to the former, and (encompassed within the franchisor's proposed input) a vital element in the franchisee's potential success: that of access to the total business package including plans, training and use of the concept's brand image, resulting in an 'instant' market. Thus the dominance of the franchisor vis a vis single franchisee is manifested by an almost total lack of bargaining ability on the part of franchisees, whose choice is that of either entering into a franchise agreement on the franchisor's terms or not entering into the agreement at all. Resulting from this lack of equality in negotiations, standard contractual agreements tend to be heavily weighted in favour of the franchisor, with considerable detailed emphasis given to franchisee obligations and franchisor rights, whilst only generalized obligations are placed upon the franchisor and few rights are specifically accorded to franchisees.

Diagram 9.13 indicates the changes normally occurring within the franchisor: single franchisee relationship during the course of time (34). Once the franchised unit has been established as a going concern, one of the major contributions by the franchisor (that of the blue print of the operation) has been consumed by the franchisee.

Likewise, the franchisor's input to the arrangement, of the ability to attract customers through advertising, promotion and sustaining the brand image is perceived by most franchisees to lose its major importance. Once customers have been drawn to a particular unit franchisees tend to attribute their sustained loyalty to the franchisee's own performance and not to the general image of the system, developed and controlled by the franchisor. The franchisee has gained knowledge and experience of the franchised product and system, and has
Diagram 9.11 Position of Franchisor and Single Franchisee during their Working Relationship

**FRANCHISOR**

**OPTIONS**
- Main advantages
  - Continue relationship with franchisees
    - Franchise may have lost motivation, be unwilling to adapt to new requirements and/or be contravening terms of agreement.
- Recruitment of other franchisees
  - Franchisee may be insufficient, quality of suitable applicants difficult to forecast.
- Establish new directly-managed outlets and/or buy-back franchise units
  - Franchisee investment needed, heavy drain on group services; need for motivated unit management;
    - Opposition from existing franchisees.
- Diversify into other markets or concepts
  - Franchisee’s need to develop new systems, using capital and human resources.
  - Exposure to risk.

**INFLUENCING FACTORS**
- Desire and capacity for growth through franchising and/or directly managed units; need for new outlets.
- Franchisee’s experience in growth and annexes to new policies by existing franchisees; external pressures such as franchisor’s pressure groups, potential legislation to reduce franchisee dominance.

**NEGOTIATING POSITION**
- Improved franchise position because of reduced reliance on franchisor expertise, feasible alternative actions to franchisee’s, and perceived reduction in franchisor input.
- Franchisor still dominant because of terms of franchise contract.

**TERM OF AGREEMENT**
- Franchisee’s individual negotiation of terms still minimal, but in practice is under less control.
- Group action by franchisees gives rise to some benefits.

**SINGLE FRANCHISEE**

**OPTIONS**
- Main disadvantages
  - Desire for full independence and/or expansion may be frustrated.
- Franchisee contrôle by agreement, franchisee restricted to acceptable standard.
- Continue; payments to franchisor may be appreciated to franchisor’s continuing input.
- Franchisee may prohibit/fringe such growth; need to change role and responsibilities as part of control improves.

**INFLUENCING FACTORS**
- Maintenance of brand image through advertising, promotion and control of system; availability of group services (technical and operating advice and assistance; supply of products (in some cases); financial commitment in some cases) through own or ownership of premises.

**NEGOTIATING POSITION**
- Franchisee may prohibit/fringe such growth; need to change role and responsibilities as part of control improves.
- Probable problems in terms of agreements; likely to be geographical restrictions on opening new units; need to build up customer loyalty if new.

**TERM OF AGREEMENT**
- Franchisee’s individual negotiation of terms still minimal, but in practice is under less control.
- Group action by franchisees gives rise to some benefits.
gained status as an employer, generator of turnover and profit and as an entrepreneur capable of retaining customer-loyalty. The franchisee's input to the arrangement is likely to have increased, due to a greater volume of sales (and hence increased revenue to the franchisor). The options open to a franchisee after a period of time become more feasible, owing to his acquired experience and confidence as an entrepreneur and as the operator of a particular hotel or catering system, and to his improved financial status.

Assessed overall, the position of a franchisee in relation to his franchisor undergoes substantial changes. However, the written terms governing a franchisee's position are not normally adjusted to suit the altered situation, either during the currency of an existing agreement or subsequently upon renewal of a contract. The alternative actions open to a franchisee are frequently restricted by contractual clauses which, after termination of the franchise agreement, prohibit, within a prescribed geographical and temporal limit, the operation of a similar outlet to that which was franchised. In practice, though not necessarily formally acknowledged or even realized, franchisors tend to acknowledge the increased stature of an experienced franchisee by permitting him more freedom of action in the operation of his unit through less frequent supervision, more personal liberty (for example to develop other business interests), and a reduced likelihood of implementing harsh measures for non-compliance with terms, despite their contractual currency.

9.562 Franchisor: Multiple Franchisee

The initial negotiating position of franchisor and multiple franchisee is shown in Diagram 9.12. It indicates the more substantial status of the multiple franchisee than of the single franchisee and shows the greater proposed contribution to the arrangement by the multiple franchisee, including a capacity to accelerate market penetration by the availability of one or more existing sites or units in advantageous positions, and by access to certain developmental resources within the
multiple franchisee's organization. Thus the initial status and input of the two parties is of a broadly equal nature. The options open to either party are also approximately balanced, each having certain disadvantages deriving from the expenditure of time and resources that would be necessary to develop alternative methods of operation to that of franchising.

Thus the balance of power between a franchisor and multiple franchisee is far less unequal, than in the case of single franchisees. Where multiple franchisees have prior experience of the franchising arrangements either as franchisees of one or more other systems or as franchisors in their own right, their position vis a vis the franchisor is further improved. Their approximate equality is normally manifested by a greater negotiating flexibility allowed to multiple franchisees, resulting in their achieving more favourable terms or being permitted significant departures from the standardized image.

The position of the two parties during their working relationship is depicted in Diagram 9.14, and reveals different characteristics to that between franchisor and single franchisees. Whereas the latter normally undergo a significant improvement in status, multiple franchisees usually do not, being ab initio substantial business entities with general, if not specifically applicable operating experience. The proposed input of the franchisor has been consumed to a great extent (as occurred with single franchisees) but the lesser initial reliance of the multiple franchisee on the franchisor's experience and group resources, suggests that such consumption is less significant as a factor affecting their relative positions, and may be balanced to some extent by the franchisor's consumption of certain of the multiple franchisee's developmental resources. Thus the passage of time does not substantially alter their positions in relation to each other, except in circumstances where the franchisor has conceded significantly
advantageous terms to the multiple franchisee during initial negotiations. For example, an increase in the relative power of a multiple franchisee may result from permitted substantial expansion of his interests so that they subsequently represent a significant proportion of the outlets within the total franchise system; or the franchisee's right to deviate from a standardized menu or house style may in time result in the growth of a sub-system with a separate identity, likely to challenge the franchisor's brand image, and instrumental in affecting the power structure within the system. Whilst there is not usually a modification of the agreed written contractual and financial terms during the course of their working relationship, in practice, the franchisor may defer to the evident power of the multiple franchisee by reducing control over his units and by consulting him on aspects of policing affecting the system.

9.57 Summary of Findings in Respect of Franchising and Comparison With Those of Surveyed Literature

Other than in a few, notable exceptions, franchising (as defined earlier) was found to be a relatively recent phenomenon in the general economy and in the hotel and catering industry. The concept of franchising and the respective roles of participants were found not to be properly understood by the public in general, nor by those within the hotel and catering industry nor, in a few cases, even by those engaged in franchising.

In broad terms franchisors and franchisees were seen to be meeting their mutual needs and those of the public. However considerable variations were found amongst franchisors and franchisees in their genuine or equivocal attitude to franchising as a long-term method of expansion and as a long-term relationship between them.

Franchisors within the parameters of the study were found to be few in number, though some had very extensive interests in one or more systems within and/or outside Britain. The group
resources of the larger franchisors included substantial assets, comprehensive organizational establishments and a wide range of expertise available on a variety of operational and technical aspects. Franchisees were found to be of two basic types: single and multiple franchisees, whose characteristics and status vis à vis the franchisor were significantly different.

An examination of the terms generally governing franchise arrangements showed that one of two methods was used to remunerate franchisors: either a premium on supplies or a percentage based on gross revenue. In the case of the first method, which was less prevalent, all or a substantial proportion of supplies were tied to the franchisor. No validated information could be obtained as to the amounts received by the franchisor. Where payment was based on total gross revenue a levy of from 2½ to 7½% was normally charged with (in addition to a royalty of 4% levy) 3% on turnover required by one system for advertising or marketing purposes. Where payment was calculated on gross room revenue it was 3 or 4%. Initial franchise fees payable to franchisors varied extensively according to the unit being franchised; those normally charged for restaurant and 'take-away' outlets were in the region of £250 to £750, those for hotels were from £5,000 upwards. Franchise agreements were most frequently of five or ten years duration.

Contractual terms governing franchisees varied in the extent of their detailed stipulations; the most precisely defined arrangements being those where comprehensive operating manuals were expressly included as part of the legally binding franchise contract. Franchisors in general were found to substantially execute their initial agreed contribution to franchise arrangements by the provision of a 'complete business package'; but considerable differences were found in the subsequent fulfillment by them of their obligation to provide group services (including marketing and managerial assistance) and in their capacity to control franchisees' standards and enforce franchisees' contractual obligations.
Contracts were found to be weighted in favour of franchisors, with emphasis placed on franchisors' rights and franchisees' obligations, indicating the dominant position of franchisors resulting from their ownership of the concept, experience in its implementation and operation, ownership of the brand image and thus access to an 'instant' market, and their experience of entering into such contractual arrangements. In circumstances where franchisors also controlled all or a substantial part of supplies their dominance was greater still. There was found to be almost no negotiating ability on the part of single franchisees, though multiple franchisees were found to have a substantially improved bargaining position with consequent flexibility to negotiate terms.

Participants in franchise systems were found to be very interdependent, due to the nature of franchising involving close economic and financial links between the two main parties, together with the reliance of all system members upon the maintenance of a standardized total product and brand image. Thus a franchisor, franchisee and directly-employed managers of either party were seen to be links of a chain, all being dependent on the strength of each link to sustain the whole.

A number of environmental factors were found to be of considerable significance to the growth of franchising systems, including those affecting the availability of suitable sites, adequate capital and prospective franchisees. Whilst some factors were seen to be peculiarly relevant to franchising (such as those affecting the attitudes of potential franchisees towards the franchising method), other factors were found to be comparable to those influencing the development of non-franchised systems (such as planning regulations, attitudes of lending institutions and competitive systems) but to present additional facets relevant to the franchising arrangement and usually affecting a franchisor and his franchisees to a different degree.
The franchisor:single franchisee relationship was found to undergo significant changes during the course of time. The initial dominance by a franchisor, manifested in contractual terms that were weighted in his favour, was seen to be reduced by a combination of factors including the growth in a franchisee's status, an increase in his contribution to the arrangement, the consumption of a major part of the franchisor's initial input, and the more feasible alternatives open to a franchisee. Changes in the relationship between the two parties were seen not to be reflected by modifications to the agreed contractual terms, but in some degree to be acknowledged in practice.

The franchisor:multiple franchisee relationship was assessed as being one between parties of a roughly comparable status. The relationship was seen to undergo no significant change during the course of time as a result of alterations to the status of, or contribution by either party, or of more feasible alternative options subsequently becoming open to them. However, where initial terms between the two parties had been such as to result in a multiple franchisee's substantial development (either in terms of size or departure from the standardized system image or procedures), this was seen to cause a change in the balance of power between them, and to present far-reaching implications for the system as a whole.

In making a comparison of these findings with those in the surveyed literature, a difficulty arose from a lack of published information relating specifically to the British situation which incorporated a detailed and comprehensive coverage of economic, managerial and attitudinal aspects. Where possible, these findings are compared with relevant areas of British studies. Despite differences in the American and British cultural and business environment, it was thought meaningful to compare this researcher's findings with those of American studies and with American hypotheses, excluding any detailed comparison of financial performance, legal aspects and the current status of franchising in the two countries.
No other British study was traced which either examined franchising within a particular sector of economic activity, let alone examined franchising within the hotel and catering sector. Neither was any study found which combined a detailed survey of franchisors, their respective franchisees and an analysis of the contractual and financial terms of their agreements as offered and executed, nor one which assessed the dynamics of the relationship between the two main parties over a period of time.

The most applicable British study as a basis for comparison is that by Stanworth (35) which provides data on catering franchisees and which takes account of the economic effects of franchising upon the two main parties and upon consumers. Stanworth's data relate to three groups of franchisees including those from one catering franchise system. Broad agreement exists in his profile of the latter franchisees with that depicted by this researcher, although certain interesting differences exist, such as a more widespread state of self-employment prior to franchising experienced by Stanworth's respondents, and a less commonly enjoyed previous experience of catering activities than found amongst the franchisees surveyed by this researcher. Though Stanworth's survey of catering franchisees was, in total, larger than in this study, the number of face-to-face interviews carried out by his team was only half that undertaken in this survey (36). The relatively small sample in both studies therefore indicates a need for a more widely based statistical survey than was possible in either case. Stanworth's brief assessment of the economic effects of franchising coincides in most respects with those reached by this researcher (37).

It was considered inappropriate to compare in a detailed manner American findings related to the overall economic significance of fast food franchisors and franchisees or to their individual performance, with the findings of this survey. However the contractual and financial terms seen to exist in the British situation and the management services offered by franchisors were found to be similar to those outlined in the literature surveyed (38).

Attention has been paid in several American studies (39) to the dynamics of the franchise relationship, including brief mention of the particular differences in the relationship over a time span, and that between franchisors and their single or
The findings of this study agree with these assessments, though inadequate experience in the British situation over a long period precludes similar conclusions being reached. The 'recommended best practice' proposed in this study (40) is based upon consideration of the practical findings of this researcher, and agrees with many of separate recommendations put forward in a number of British and American publications (49). An assessment of the economic effects of franchising upon the national economy is a synthesis of views propounded by the major authors on the subject (49).

9.6 SUMMARY COMPARISON OF FOUR TYPES OF CONTRACTUAL ARRANGEMENT

The main common features of the arrangements are summarized in Schedule 9.1. Their main differences are outlined below.

9.6.1 Stage of Development

The stage of development of the four types of contractual arrangement varies extensively. The tied house system has a very long historical background and is a widely prevalent and accepted business arrangement amongst almost all brewers. The catering contract arrangement likewise is a long-established method of operation, practised by some two hundred contractors mainly in a large proportion of on-site employee feeding operations. By comparison, franchising and in particular the hotel management contract arrangement are relatively recently practised business methods and in general terms are of much less current significance within the catering and hotel sectors in which they are used. The total number of franchisors or hotel management contractors is very small, though the franchise systems of a few franchisors are extensive and significant within the market in which they operate. Unlike the other three arrangements, which are restricted to a particular sector of the hotel and catering industry (43), franchising is a business method that is used for the establishment and operation of hotels and for restaurants and 'take-away' outlets, as well as in a broad range of activities outside the hotel and catering industry.
Summary of Main Features Common to Four Types of Contractual Arrangement

1. Involvement of two main parties in a business arrangement in which there is a separation of the ownership from the operation and management of a particular unit, or a separation of the ownership and management of a system in its entirety from that of the ownership, operation and management of its component units.

2. Initial and continuing input of an active or passive nature by both parties.

3. Economic and financial interdependence of the two main parties.

4. Affected to a varying extent by other parties involved in or adjacent to each arrangement.

5. Influenced by general environmental factors of a political, social or of a wider business nature.

6. Governed by a formal written document containing financial and contractual terms and delineating the legal and operational rights and responsibilities, applicable to each party. Also influenced by informal, unwritten conditions normally prevailing in such arrangements.

7. Involving a dynamic relationship between the two parties.

8. Finally dependent upon a mutuality of aims and goodwill* between both parties.

* in general sense not in financial context.
9.62 Role and Contribution of Two Parties

Table 9.5 summarizes the contributions of the two parties to each arrangement and points to their varying degree of 'active' operational or 'passive' financial participation. The separation between the active and passive roles is most obvious in the case of hotel management contracts. The provision or creation of a market for the goods or services being sold or provided by the unit operator (i.e. contractor, tenant or franchisee), is variously undertaken by the operator or by the other party either in total or in part.

The main continuing receipts or benefits obtained by the two parties in return for their input to the arrangement are summarized in Table 9.6. Both tables illustrate the economic and financial interdependence of the two parties, which arises in each of the four arrangements through a different combination of factors.

9.63 Raison d'être of the Arrangements and Objectives of the Two Parties

There are important differences between the four types of contractual arrangement hinging on their raison d'être and on the objectives of the two main parties. In all four arrangements, the aim of the unit operator is to achieve a reward for his endeavours, but in only three of the arrangements does the 'non-operating' party also seek a direct financial return. In the contract catering situation, the client's policy is primarily to purchase a service to benefit categories of people for whom he has responsibility, such as employees, students or patients. Thus the catering contract arrangement is created expressly for this end, and does not involve mutual participation by the two parties in a profit-making activity or in the creation of capital appreciation. In the other three arrangements, those of hotel management contracts, the tied house system and franchising, both parties participate with the primary policy of each achieving a financial return, through the sale of goods and/or services to the public by the operator.
### Table 9.5  Summary of Contribution by Two Parties to Each Contractual Arrangement

<table>
<thead>
<tr>
<th>Contribution Provided</th>
<th>Catering Contract Arrangement</th>
<th>Hotel Management Contract Arrangement</th>
<th>Tied House Arrangement</th>
<th>Franchising Arrangement</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>catering contractor</td>
<td>client</td>
<td>hotel management contractor</td>
<td>client</td>
</tr>
<tr>
<td>Site, building, contents</td>
<td></td>
<td>✔</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Working capital</td>
<td>✔</td>
<td></td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Labour and operational Management</td>
<td>✔</td>
<td></td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Supplies</td>
<td>✔ *</td>
<td>✔ *</td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Concept</td>
<td>✔</td>
<td></td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Managerial and Technical Expertise</td>
<td>✔</td>
<td></td>
<td></td>
<td>✔</td>
</tr>
<tr>
<td>Market</td>
<td>✔</td>
<td></td>
<td></td>
<td>✔</td>
</tr>
</tbody>
</table>

**Key:**
- * usually as agent
- ** sometimes as producer or wholesaler, sometimes as agent, sometimes with no direct involvement
- ( ) limited contribution
Table 9.6

Summary of Continuing Return to Each Party for their Contribution to the Contractual Arrangements

<table>
<thead>
<tr>
<th>Receipts or Benefits Gained</th>
<th>Catering Contract Arrangement</th>
<th>Hotel Management Contract Arrangement</th>
<th>Tied House Arrangement</th>
<th>Franchising Arrangement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Financial Receipts</td>
<td>catering contractor</td>
<td>client</td>
<td>hotel management contractor</td>
<td>client</td>
</tr>
<tr>
<td>Payment linked to sales or supplies</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>Payment linked to profit</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>Fixed payment</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>Net profit (loss) after above deductions</td>
<td>subsidy/net loss</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>Non-financial benefits</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Directly received operational services</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
<tr>
<td>Market Exposure for Branded Product or Concept</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
<td>✔️</td>
</tr>
</tbody>
</table>

Key
* one or other method of payment
** market exposure to branded concept and product where hotel visibly operated in contractor's name.
The divergent means by which this financial return is achieved by the unit operators in each type of arrangement, and by their respective 'non-operating' parties point to significant consequences. In the catering contract arrangement, the contractor's remuneration is usually directly or indirectly based on volume, not on profitability. The nature of the arrangement and prevalence of the practice by clients of subsidizing such catering services results in emphasis by clients on minimizing costs (commensurate with agreed standards) and not normally encouraging the growth of sales, thus resulting in a conflict of underlying objectives of the two parties.

In the hotel management contract arrangement there is a broad concurrence of objectives between contractor and client, though the degree of concurrence over whether to strive for maximizing revenue or profit depends on negotiated fee structures, the agreed duration of the contract and individual trading figures of hotels. Their aims are likely to be closest where the contractor's remuneration is based only on profitability of the managed hotel and where the contract is for a long period, thus causing a mutual desire for the long-term profitability of the hotel.

In the tied house system and franchising there is a significant divergence in aims between the operators of units and the other parties. The former seek to maximize the profitability of their outlets, whilst brewers and franchisors respectively aim to maximize overall sales, thus gaining greater revenue from wholesale margins on supplies or a royalty based on gross revenue. As a policy of non-selective general sales growth in either tenanted public houses or franchised outlets does not necessarily accord with an objective to maximize profitability, there is an underlying conflict between the two parties to each agreement.
Context in which Arrangements Operate

Table 9.7 summarizes the context in which the contractual arrangements are set as well as factors affecting their continuation. It indicates the difference between the position of catering contractors whose services are by and ancillary to their clients' activities, and those of hotel management contractors whose services embrace the operation of a complex major business interest of their clients, with potential for profit and for capital appreciation. The somewhat tenuous position of catering contractors is caused by a combination of factors including the possibility that the services which they provide may be eliminated altogether or replaced by other methods (for example, vending machines in some circumstances).

The summarized alternatives open to the 'non-operational' party to each of the four arrangements (i.e. the party not primarily involved as a unit operator) indicate the variety of options which may be available to the parties. They point to the relatively stronger position of brewers, caused by their ownership of an existing alternative method of distribution through directly-managed outlets, by their ownership of tenanted outlets (and thus ability to change these to direct management), and by additional distributional channels for off-license sales, in comparison with that of franchisors who (if franchisors per se) normally directly own few units and for whom the creation of an alternative distribution channel would be a more difficult, costly and time-consuming task.

Also shown in Table 9.7 is the difference in the effect upon the four types of arrangement caused by other parties within or adjacent to the arrangement. It points to the peculiarly important position of unit managers in the relationship between contractor and client in both the catering contract and hotel management situation. In the former case this is because of his normally frequent proximity to the client and because of the contractor's dependence for the continuation of the contract on the level of satisfaction of client-employees with catering services; and in the latter case because the role of the hotel manager is to manage a complex activity as a viable business proposition, usually being remote from the
<table>
<thead>
<tr>
<th>Table 9.7</th>
<th>Context in Which Four Contractual Arrangements Operate</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Environment</strong></td>
<td><strong>Catering Contract Arrangements</strong></td>
</tr>
<tr>
<td><strong>Activity of Operator</strong></td>
<td>Usually in non-commercial context with 'captive' or 'semi-captive' customers; ancillary activity to client's main business, normally involving a substantial subsidy.</td>
</tr>
<tr>
<td><strong>Alternative Arrangements open to other party</strong></td>
<td>Ranges from a small-scale simple activity during normal working hours to an extensive, complex activity on a 24 hour continuous basis.</td>
</tr>
<tr>
<td><strong>Effect of Other Parties</strong></td>
<td>May use vending machines, direct management of catering activity, or close down catering services altogether.</td>
</tr>
<tr>
<td><strong>Operating performance</strong></td>
<td>Operating performance largely dependent on unit manager, who usually has a close, informal relationship with the client. Success of arrangement judged to some extent by level of client-employee satisfaction with services. Financial arrangement between contractor and supplier has important ramifications.</td>
</tr>
</tbody>
</table>
contractor's supporting services. In the tied house arrangement and franchising a similar tripartite relationship occurs only where a unit manager is employed by a multiple tenant or franchisee.

Due to the standardized nature of franchise systems, and the necessity for maintaining a controlled brand image, the actions of all system participants and their effect upon consumers is of particular importance. Thus the activities of a franchisor, all franchisees within a given system, and of directly-employed managers of either party, are of significance to each other. Such inter-dependence may be mirrored to some extent in the hotel management situation, where an hotel is visibly operated under a brand name. In the tied house arrangement there is normally no such homogenized image of any one brewery system and thus no similar reliance between participants. In this arrangement the actions of other parties are mainly significant in circumstances where tenant pressure groups affect generally obtaining terms between brewers and their tenants, and may influence policies within a given brewery or in the brewing industry in general.

9.65 Mutual Constraints Imposed by the Two Parties
The main constraints placed upon parties to each arrangement are summarized in Table 9.8, which illustrates the difference in emphasis on financial and operating controls. In catering and hotel management contracts the unit operator is primarily subject to financial constraints with only broadly outlined requirements governing operating performance. In the tied house system and franchising arrangements, unit operators are subject to closely defined operating requirements (extending to constraints on other business activities) but not to controls on financial performance. Legal responsibilities accruing to the various parties reveal the potential specific problems engendered by the nature of each type of arrangement.
<table>
<thead>
<tr>
<th>Contractual Constraints contained in</th>
<th>Catering Contract Arrangement</th>
<th>Hotel Management Contract Tied House Arrangement</th>
<th>Franchising Arrangement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unit operator</td>
<td>Catering contractor</td>
<td>Hotel management contractor</td>
<td>Franchise</td>
</tr>
<tr>
<td></td>
<td>broadly outlined operating and advisory obligations; detailed requirements on operating times and selling prices</td>
<td>broadly outlined operating and advisory obligations</td>
<td>tied trade tenant</td>
</tr>
<tr>
<td></td>
<td>Overall financial budgets (in most cases); defined legal responsibilities to third parties (in some agreements)</td>
<td>defined overall financial budgets and results required; defined legal responsibilities to third parties and to the other party to the agreement;</td>
<td>very detailed operating requirements including (usually) the source of supplies, range of products, operating hours (sometimes selling prices (sometimes) and permitted methods.</td>
</tr>
<tr>
<td></td>
<td>Constraints imposed by the environment provided by the other party; constraints due to the subsidy provided by the other party.</td>
<td>constraints imposed by the environment provided by the other party;</td>
<td>Constraints on other party's agreement (site, size of operation)</td>
</tr>
<tr>
<td>Other party</td>
<td>Client</td>
<td>Brewer</td>
<td>Franchisor</td>
</tr>
<tr>
<td></td>
<td>broadly defined obligations relating to the provision of a suitable environment; defined financial obligations relating to continuing subsidy; (in some cases) defined legal obligations in respect of third parties.</td>
<td>broadly outlined requirements relating to the provision of a suitable environment; defined overall initial financial obligations and broadly outlined subsequent financial obligations.</td>
<td>no obligations in respect of environment</td>
</tr>
<tr>
<td></td>
<td>constraints on employing other operators at the given site.</td>
<td>defined legal responsibilities towards third parties and towards operator; (in some agreements) an obligation to provide supplies to best of ability expected, but not formally agreed, services including advice and assistance with management and marketing activities.</td>
<td>comprehensive but not precisely defined obligations to provide advice and assistance with management and marketing activities</td>
</tr>
</tbody>
</table>

Table 9.6 Summary of Main Mutual Constraints Imposed by Each Party Within the Four Contractual Arrangements
9.66 Dynamics of the Two Party Relationship

The difference in the dynamics of the relationship between the two main parties in the four types of arrangement hinges on the nature of the parties involved. Whereas catering contract and hotel management contract arrangements are negotiated between two parties of broadly comparable status, each of whom normally has substantial concurrent interests elsewhere, the tied house and franchising arrangements occur between parties of unequal status, with the business interests of the intending tenant or franchisee usually restricted to the particular business being negotiated (an exception to this occurs in the case of multiple franchisees). The personal involvement of tenants and franchisees in their businesses, and their consequent personal development as entrepreneurs has a most important bearing on their respective relationships with their brewer or franchisor. Such a development does not occur in the catering or hotel management contract arrangement, where no comparable personal involvement of either party takes place; those changes which do occur, centre on the interactions between unit/hotel manager, contractor and client.

Shifts in the balance of power between the two main parties may result from the consumption during the course of time by either party of a major part of the other's initial input to the arrangement, combined with a perceived end to or reduction in continuing input. In the case of catering and hotel management contract arrangements, the implementation of plans results in the client's consumption of a major part of the contractors initial input, but their continued services in operating and managing (and, in the case of hotel contractors, of marketing) the units, is evidence of their continuing contribution to the arrangement. In the case of the tied house arrangement, there is no similar initial 'blue-print' of operation provided by brewers to tenants and thus no consumption of such plans during the course of time. The contribution made by tenants to the arrangement, mainly being their own labour and working capital, remains evident and continuous,
Whilst the input of brewers, being the provision of the premises and supplies, also remains tangible and does not reduce in value. However, in the franchising situation there is consumption by the franchisee during the course of time of the franchisor's initial 'total business package' including the plans, policies, and to some extent (by creating their own loyal customers) the benefits of an 'instant' market of consumers. In some systems, this is concurrent with what franchisees perceive as a lack of, or reduction in, a continuing contribution made by the franchisor to the arrangement, and a tangible increase in input made by the franchisee (in the form of a larger payment to the franchisor based on increased sales as the business becomes established).

9.67 Conclusions

The many factors mentioned in this summary comparison point to the conclusion that of the four types of contractual arrangement, franchising is the activity in greatest need of further assessment. Unlike the catering contract or tied house arrangements which have been widely practised and to some extent studied, the nature and ramifications of franchising and hotel management contracts are not widely understood, being relatively recent phenomena in this country and of current small overall dimensions. But whereas the nature of hotel management contracts is essentially an arrangement involving the purchase and supply of specialist services between two parties of broadly comparable status, one essentially being in an 'active' operating capacity and the other in a 'passive' financial role, whose relationship alters less significantly and upon whom constraints do not relate to their entire business interest, the nature of franchising displays more complicated characteristics.

The peculiar complexity of the franchising arrangement may be attributable to the combination of several factors, including the particular 'mix' of contributions made by each of the two
parties to the arrangement, their differing objectives, the
dynamics of their relationship and the interdependence of all
participants in any one system. In essence, the greater com-
plexity of franchising centres on the involvement of two par-
ties in a business activity in which each seeks with an unack-
nowledged difference in objectives, a continuing financial
return; and in which the relatively weaker party normally
achieves considerable growth in personal and business develop-
ment, using his own capital and owning the distribution outlet, whilst being subject to considerable operational con-
straints relating to that outlet or to his wider business inter-
est, such constraints being necessary for the viability of
the system as a whole.

It is therefore proposed to examine in greater detail the ad-
vantages and disadvantages of franchising to the two main par-
ties, as well as to the consumer and the wider economy, and
to leave for further research any further assessment of the
other three types of contractual arrangement.
CHAPTER 10
ASSESSMENT OF THE ADVANTAGES AND DISADVANTAGES OF FRANCHISING

10.1 INTRODUCTION

10.2 RELEVANT TO THE FRANCHISOR
   10.21 Marketing and Distributional Advantages and Disadvantages
   10.22 Financial Advantages and Disadvantages
   10.23 Purchasing Advantages and Disadvantages
   10.24 Operational and Managerial Advantages and Disadvantages
   10.25 Legal Advantages and Disadvantages

10.3 RELEVANT TO THE FRANCHISEE
   10.31 Marketing and Distributional Advantages and Disadvantages
   10.32 Financial Advantages and Disadvantages
   10.33 Purchasing Advantages and Disadvantages
   10.34 Operational and Managerial Advantages and Disadvantages

10.4 PECULIAR TO THE ARRANGEMENT BETWEEN FRANCHISOR AND MULTIPLE FRANCHISEE

10.5 RELEVANT TO THE CONSUMER

10.6 RELEVANT TO THE NATIONAL ECONOMY AND IN THE GENERAL INTEREST

10.7 CONCLUSIONS AND SUGGESTED 'BEST PRACTICE'
   10.71 Overall Assessment of the Value of Franchising
   10.72 Recommended 'best practice'
      10.721 Testing of concept
      10.722 Adequate disclosure of franchisor background
      10.723 Franchise contract
      10.724 Source of franchisor income and fee structure
      10.725 Franchisor services
      10.726 Franchisor controls
      10.727 Franchisee rights
      10.728 Recognition of franchisee's special status
      10.729 Multiple franchisees.
10.1 INTRODUCTION

In this chapter an assessment is made of the advantages and disadvantages of franchising to the franchisor, the franchisee, the consumer and to the general economy. It is based upon an examination and assessment of the advantages and disadvantages proposed in much of franchising literature (1), and whilst lacking extensive empirical backing, draws upon the findings of this researcher relating to franchisors and franchisees in the British context. Some advantages normally claimed of franchising are either thought to be unrealistic or are not supported by evidence in the British situation. A number of disadvantages are suggested to exist in certain circumstances, attention to which has not been drawn previously in franchising literature. Whilst the incidence and extent of advantages and disadvantages vary with any given franchise system and with the particular stage of its lifecycle, it is proposed that in general, those outlined below are widely applicable.

An examination is made of the functional characteristics of franchising including its marketing and distributional, financial, purchasing, managerial and operational advantages and disadvantages. Consideration is also given to the differences arising in arrangements between a franchisor and single franchisee, and those with a multiple franchisee.

10.2 RELEVANT TO THE FRANCHISOR (2)

10.21 Marketing and Distributional Advantages and Disadvantages

10.211 Advantages

One of the chief advantages of franchising to the franchisor is found to be the relative ease and speed with which market penetration may be achieved through harnessing the capital, energies, time and motivated interest of franchisees to augment
the franchisor's financial and organizational resources. By using franchisees' investment capital to build up the system, the franchisor is able to expand far more quickly than by non-franchised means. By securing franchisees' energies to search for suitable sites or premises for their franchised units, or by attracting owners of existing sites to become franchisees, the franchisor may pre-empt competitors, or obtain a significant saving in time or staff, particularly a franchisor whose site requirements are difficult to meet, or whose needs are for sites which are considerably sought after.

Through harnessing the financially-motivated interest of franchisees to supervise and encourage the speedy and satisfactory implementation of their own units, the franchisor benefits from a reduction in the need for (and cost of) developmental personnel, is able to establish new outlets more quickly and may expand in areas far removed from the existing field of operations or from franchisor headquarters.

The comparative speed and breadth of expansion provides significantly greater market exposure of the franchised product than would otherwise be possible. Increasing benefits accrue to the franchisor from a wider availability of outlets to existing brand-loyal customers, additional exposure of the franchised product to potential customers and to potential franchisees.

Through establishing a network of tied distribution outlets, the franchisor, in the role of supplier, is able to accord the overall volume of supply with demand, to benefit from exclusion of competitors' products from such units, to introduce new products and to gain advantages from economies of scale in production and distribution comparable to such as would result from direct ownership of outlets. Such a role of supplier may apply to food or liquor products, disposable commodities, equipment, fixtures and furniture.
Franchising is seen, therefore, to provide a franchisor with the marketing and distributional advantages which permit the rapid implementation of a product or concept in response to a perceived market demand, and which enable a franchisor with relatively small resources to compete against a larger non-franchised competitor.

Another marketing advantage which has been suggested (3) is that by using the franchising method a franchisor may retain strategic mobility. Because of the reduced extent of the franchisor's investment, it is suggested that he may readily disengage himself from a system that proves unsuccessful. This is probably a valid claim, but such an advantage is likely to be applicable to a franchisor on only one occasion because of the resultant bad image with franchisees, suppliers and consumers.

The claim that franchising provides the franchisor with an opportunity for obtaining accurate marketing feedback (4) needs to be carefully examined. In franchising systems where all or most supplies are tied to the franchisor this permits the type and volume of supplies to match demand in overall terms. However, where such ties are not enforced, and even where they are, it is suggested that in practice few franchisors obtain or act upon information from their franchisees in respect of detailed sales' mixes or precise changes in consumer requirements. Such information is usually derived by a franchisor from his wholly-owned and managed outlets.

10.212 Disadvantages

An important disadvantage of franchising stems from the problem that is found to be encountered by franchisors in enforcing standardization amongst system outlets (5). Whilst the maintenance of a standardized brand image is necessary to ensure a sense of security amongst customers, and whilst
such a policy is in the long-term interests of all participants within the franchise system, this is not necessarily found to be the underlying objective of franchisees, whose main aim is usually to maximize their own profitability. To achieve this franchisees may either stimulate sales by improving the value of particular products or extending the existing range of products or services, or may reduce costs; in either case the products or environment are altered.

As in a standardized but wholly-owned system of hotel and catering outlets a difficult problem exists in enforcing strict compliance with detailed standards governing the activities of possibly numerous employees engaged in a complex operation, which may combine a multiplicity of products and services. But the franchisor's problem is further accentuated by the fact that he has only indirect control over such activities. Whilst he may terminate a franchise agreement for a franchisee's non-compliance with agreed operating standards, the result of such an action may have considerably greater import than the dismissal and subsequent replacement of a unit manager in a wholly-owned outlet. Unless the franchisee is committed either to giving his franchisor first option to purchase, or control over the sale of his franchised outlet, the termination of the arrangement is likely to lead to the loss of a tied distribution outlet, possible emergence of a competitor, and may reflect the franchisor in a harsh light amongst existing or prospective franchisees.

Whilst the nature of franchising, in comparison with a wholly-owned system, offers a rapid means of implementing a new product or concept, it is found to result in a much
slower and more difficult process of subsequently altering
the system to any significant extent whilst maintaining a
cohesive image. Unless there is an appropriate clause within
each franchise agreement enforcing compliance with such
changes as are thought necessary by the franchisor, each
and every franchisee has to be convinced of the direct
benefits that would accrue to him from such alterations,
and where necessary, be persuaded to make the necessary
re-investment and/or lose revenue whilst alterations are
made. Although the need for such changes is likely to
stem from an altered market demand for the system as a
whole, an individual unit may not be affected by the same
characteristics of demand and may not necessarily benefit
from the required alterations. In such circumstances the
franchisor is likely to encounter problems prior and sub-
sequent to enforcing changes to the franchisee's unit,
whether or not an appropriate clause of consent has been
signed by the franchisee, particularly if a substantial
sum is required from the franchisee for re-investment. In
any event, the franchisor is precluded from a simultaneous
alteration to all units or even a phased alteration to out-
lets in specific areas, such as could be achieved under
direct ownership.

Another disadvantage of franchising is the possibility that
maximum exploitation of a given area may not be achieved.
This may be due to the complacency of existing franchisees
with their existing turnover or profitability, and the relative
inability of the franchisor either to change the franchisees' attitude or replace them. Under-exploitation may also arise
in circumstances where, for example, two franchised outlets
of a system are unable to meet demand in a particular area,
such demand being insufficient to support three outlets at
the same level of turnover and profitability. Whereas a third
outlet could be opened in a wholly-owned system, thereby im-
proving the system's overall performance, the introduction of
a third franchised outlet (or of a franchisor-owned outlet)
would reduce the income of the existing franchisees and cause
considerable franchisee unrest.

As mentioned earlier, it seems likely that a lack of market-
ing feedback to the franchisor is a disadvantage, particularly
if all outlets within a system are franchised.

10.22 Financial Advantages and Disadvantages

10.221 Advantages

Mention has already been made of the greatly reduced need on
the part of the franchisor for investment capital to expand
the system arising from the use of franchisees' funds. By
eliminating or reducing his investment in the system as a
whole, and in its fixed assets such as buildings, equipment
e tc. and by spreading risk amongst a number of units, the
franchisor is less exposed to financial failure; should the
system not prove viable the franchisor is not subject to
losses on the sale of assets.

The franchisor obtains a second substantial financial advan-
tage in the contribution made by franchisees to the franchi-
sor's working capital. This is in the form of payments of
franchise fees which allow the franchisor discretion in their
expenditure such as might not be permitted through other fund-
ing arrangements and which working capital may be more speed-
ily and cheaply obtained than through more conventional means.
A reduced demand for working capital for the franchisor is
caus ed by the transference to franchisees of the responsibi-
ity for certain developmental resources.
A continuing advantage to the franchisor is the transference to franchisees of distribution and operating costs of the system. Thus, the franchisor's costs are limited to expenses incurred in setting up and maintaining the necessary organization to administer the franchise system, whilst franchisees are exposed to variable operating costs and to fixed overhead costs of maintaining their distribution outlets, the latter expenditure being irrespective of sales volume.

Franchising offers to the franchisor a continuing source of revenue, calculated normally as a percentage on total turnover or as a premium on supplies, and thus linked to sales growth within each outlet as it becomes established, and to inflation.

By involving a number of other parties (franchisees) in a requirement to obtain investment funds, the franchisor is able indirectly to use additional channels of raising finance, including as well as the franchisees' own savings, their separate approaches to institutional lenders, more inclined to spread their risk amongst a number of borrowers than to lend the equivalent sum to one party (the franchisor).

Whilst diluting the ownership of, and control over the franchise system, franchising offers the advantage in that the franchisor may thereby avoid the necessity for seeking financial participation by parties external to the business, be they shareholders or finance houses, and may thus retain within the system, and possibly exclusively to the franchisor, the capacity to make decisions and ability to affect the central interests of the franchisor.

10.222 Disadvantages

A disadvantage of franchising to the franchisor is found to arise from his inability to ensure a policy of sales maximization in franchised outlets. Whereas in a directly-owned unit the manager may be set goals to fulfill, or threatened
with dismissal, such actions cannot be taken with franchisees. The franchisor must rely on a mutuality of his aim for maximum sales with that of franchisees for maximum profit, and on a lack of complacency on the part of the franchisees, throughout the period of their tenure, with their existing level of revenue or profit.

Other alleged disadvantages of franchising which are more apparent than real (6) include the fact that franchisors obtain a substantially smaller return from franchised units than from wholly-owned units, and that franchisors are unable to build equity in the franchised system as a whole. Both characteristics stem from the fact that the franchisor has no or relatively small capital investment in franchised outlets. He therefore cannot reasonably expect a comparable remuneration with the return on investment in wholly-owned units, and neither can he expect a similar level of capital appreciation from ownership of an intangible concept to that which would accrue from tangible, financial ownership of outlets.

10.23 Purchasing Advantages and Disadvantages

10.231 Advantages

Through the considerably increased demand arising from the total requirements of system members, a franchisor is seen to be able to benefit from purchasing leverage significantly in excess of that available if the system were not franchised. Thus the whole system is likely to benefit from a reduction in purchasing and delivery costs of commodities, which may include food, liquor, disposables, equipment and furniture. The system's purchasing leverage may also result in the ability to order products of a particular quality, size, packaging or design which it would not be economic for a supplier or manufacturer to provide if demand were smaller or less predictable. Similarly, the system's purchasing leverage is also likely to ensure that the distribution of supplies extends to all units of the system, wherever situated geographically, and may result in the further advantage of being able to influence the frequency of deliveries.
All system members are therefore likely to obtain advantages from their combined purchasing leverage, which benefit the profitability of each outlet. Thus a franchisor obtains direct benefits for his directly-owned and operated units within the system, as well as gaining advantage from the consequent general improvement to the system's performance.

10.232 Disadvantages

As in a standardized wholly-owned system, the franchisor must ensure that each newly-implemented unit can be adequately serviced by supplies of an exactly comparable nature, quality, portion size etc. to those in existing outlets. Such a necessity may impose demands upon the franchisor disproportionate to his potential remuneration.

10.24 Operational and Managerial Advantages and Disadvantages

10.241 Advantages

A major benefit to a franchisor from franchising stems from the nature of the franchisee's interest in his franchised outlet. By investing his own capital and/or accepting indebtedness and by exposing himself to risk, a franchisee becomes motivated to achieving operational and financial results that will provide an adequate return on his investment, and will lead to the appreciation of his assets. An added incentive is found to be that, to some extent, the franchisee is investing his personal reputation as an entrepreneur, and therefore is likely to want to provide good service and standards to customers and to prove his operational and financial capabilities. Franchising thus provides a franchisor with a supply of owner-managers, motivated to increasing revenue, to controlling costs, supervising employee behaviour (including controlling dishonest practices) and maintaining overall standards within the unit.
A further advantage to the franchisor is the reduction in turnover of unit managers, this being a consequence of their motivation as owner-managers and of the relatively less easy process for them to sever links with the franchisor (by terminating the agreement and selling their outlet) than for a hired manager to hand in his resignation. A further advantage to franchisors is likely to stem from the personal interest shown by franchisees in their outlets and in their employees, thus creating conditions likely to stabilize staff turnover in franchised units.

The transference to franchisees of operating problems and costs, including those associated with the recruitment, retention and dismissal of employees, is a further substantial advantage to franchisors.

Mention has already been made of the saving in development management resulting from harnessing the energies and interest of franchisees. Similarly there is a reduction in the requirement for area management who, in a wholly-owned and operated system would be needed to supervise and motivate unit managers.

Some writers (7) claim that franchising enables the franchisor to obtain easy acceptance of a franchised unit within a given locality, as a result of the franchisee's own standing in the community prior to becoming a franchisee, and because of his status as an individual, there is anticipation that his unit will be better than merely another standard company outlet. According to evidence from this study, such a claim appears unlikely in the British context (8). Franchisees in general did not establish their units in localities with which they were closely associated. Neither did it appear that the public were normally aware of whether a unit was franchised or wholly-owned and operated, thus obviating any particular expectancy arising from the knowledge of an owner-manager's involvement.
A major disadvantage of franchising is found to be the problem of selecting suitable franchisees who combine all the necessary attributes. Not only must they have access to adequate sites or premises (in some systems) and to the required funds (thereby eliminating some who might otherwise have all the necessary characteristics, for example younger people), but they also require a certain mix of intangible qualities and aspirations, suiting them to a business relationship unlike any other which, in this country, does not enjoy widespread understanding. Thus franchisors have the two-fold problem, firstly of defining what intangible characteristics and aspirations they seek in franchisees, and secondly of assessing whether prospective franchisees initially enjoy such traits and aspire to such aims and whether these are likely to continue during the course of time. The consequences to a franchisor or a franchise system of inadequate definition and assessment of franchisee characteristics are considerably greater than would be similar mistakes in the selection of direct employees. The problem for a franchisor of franchisees lacking entrepreneurial drive has been touched upon already; those with excessive drive are likely to resent the franchisor's constraints and, having benefited from the franchisor's total experience of a particular concept, may well establish themselves as competitors.

Although mention has been made of the advantages to the franchisor resulting from a reduction in the extent of development management and area management needed to supervise and stimulate the implementation and operation of franchised units, the requirement for an organization to support the franchising activity to some extent balances this. Though placing fewer demands on such central resources than would a directly-owned and operated system, the establishment of a franchised system needs support of a different nature. There is a necessity for the franchisor's field representatives to be perceived as advisors and co-ordinators rather than as controllers, and to walk the narrow path of ensuring compliance by franchisees with the system's policies and practices without unduly repressing their entrepreneurial drive. Thus the franchisor needs field management endowed with particular skills.
10.25 Legal Advantages and Disadvantages

10.251 Advantages

In addition to the advantages outlined above, a franchisor usually also derives the benefit of avoiding legal responsibility for all activities occurring within franchised outlets. Thus a franchisor normally has no liability towards employees in franchised outlets, nor towards customers, except (where applicable) for the normal obligations devolving upon a supplier (9). A franchisor also avoids direct responsibility for complying with local regulations, such as the need to ensure that permitted opening hours are respected in franchised outlets.

10.252 Disadvantages

A potential major disadvantage of franchising to franchisors is the attitude of the government and the courts to franchising per se: this has not yet been clarified. Legislation forbidding restrictive trading agreements has recently been extended to services (10), which makes compulsory the registration of any agreement between two or more persons which limits the parties' freedom to supply or obtain services, including restrictions on selling prices, terms or conditions of operation, and areas in which business may be carried out (11). The attitude appears to be that each agreement must be separately considered as to whether it is or is not in the public interest and that restrictions are permitted if they stem exclusively from the franchise agreement (12). No franchisors have yet been before the Restrictive Practices Court, and it seems unlikely that the law will be so interpreted as to strike at the very roots of such proven and established franchise systems as Wimpy International.
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<td>2. Ability to expand in areas remote from headquarters.</td>
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<td></td>
<td>3. Increased market exposure to customers and potential franchisees.</td>
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<td></td>
<td>4. Better alignment of supply with demand, exclusion of competitors' products and economies of production and distribution resulting from tied outlets.</td>
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<td></td>
<td>5. Ability to effectively compete with larger non-franchised system.</td>
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<tr>
<td>Financial</td>
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<td></td>
<td>2. Contribution to franchisor's working capital in the form of franchise fees, paid in advance by franchisees.</td>
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<td>3. Transference of distribution and operating costs and financial exposure to franchisees.</td>
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<td>4. Continuing and broad-based source of revenue adjusted to inflation.</td>
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<td>5. Increased number of avenues to institutional finance.</td>
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<td>6. May avoid necessity to 'go public' thereby diluting control over policy.</td>
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<td>Purchasing</td>
<td>1. Reduction in costs of commodities due to purchasing leverage.</td>
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<td>2. Improved ability to order supplies of particular characteristics required.</td>
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<td>3. Greater control over deliveries because of increased magnitude of orders.</td>
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<td>4. Direct benefit to wholly-owned and operated outlets and indirect benefit from improved performance of system as a whole.</td>
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<tr>
<td>Operational and Managerial</td>
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<td>2. Greater stability of unit owner-managers and employees in the franchised outlets.</td>
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<td>3. Transference to franchisees of operating problems and costs, including those of recruitment, retention and dismissal of employees.</td>
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<td>4. Reduction in franchisor development management and organization.</td>
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<tr>
<td><strong>DISADVANTAGES</strong></td>
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<tr>
<td>Marketing and Distribution</td>
<td>1. Lack of power and flexibility to cohesively alter system once established.</td>
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<td>2. Lack of control over standardized image.</td>
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<td>3. Problem of under-exploitation of some areas.</td>
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<td>4. May not achieve information feedback.</td>
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<td>Financial</td>
<td>1. Lack of power to enforce sales maximization.</td>
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<td></td>
<td>2. Receives a much smaller remuneration than if the system were wholly-owned, and may receive less than that due to franchisee duplicity.</td>
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<td>3. Restricted ability to build equity in total system.</td>
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<tr>
<td>Purchasing</td>
<td>1. Need to establish and control system of standardized supplies to all franchisees.</td>
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<tr>
<td>Operational and Managerial</td>
<td>1. Problem of recruiting franchisees with the necessary tangible and intangible characteristics.</td>
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<td>2. Difficulty of defining, assessing and continuing a concordance of aims of the two parties.</td>
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<td>3. Requirement for organisation and services specifically to support the development and continuation of the franchising activity.</td>
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10.3 RELEVANT TO THE FRANCHISEE (13)

10.31 Marketing and Distributional Advantages and Disadvantages

10.311 Advantages

A major advantage obtained by a franchisee upon joining a franchise system is the immediate access to a marketing concept which normally has been tried and proven successful in a specific environment. Thus the franchisee achieves very substantial benefits from a saving in time and expenditure normally required to plan and implement a system, and gains the advantage of what may be considerable expertise and experience of the franchisor in devising, operating and adjusting the concept. In contrast to an individual entrepreneur, a franchisee upon opening his unit gains access to an 'instant' market of brand-loyal customers and benefits from a general awareness of the system's name and reputation.

Franchisees may also derive substantial advantages from advertising and promotional activities organized by the franchisor prior to, during or subsequent to the opening of franchised units. Such activities are likely to be on a scale far in excess of that achievable by a single entrepreneur, being supported by a continuing wide revenue base from existing franchisees, benefiting from economies of scale and being managed with greater expertise. Similarly franchisees may also benefit from market and technical research initially and subsequently undertaken by the franchisor, such as could not be economically arranged by an individual entrepreneur.

Thus franchising provides a franchisee, who may have no prior experience of a particular market, with the ability to enter such a market and compete effectively with established outlets of other systems or of individuals.
Disadvantages

Franchisees are at a considerable disadvantage in the extent to which they depend on their franchisor's expertise in accurately assessing the viability of their franchise system. This is particularly so in a newly established system, when there is little evidence to support the franchisor's predictions. Similarly, franchisees usually place great reliance on their franchisor's endorsement, prior to implementation of a given unit, of its future viability.

A second disadvantage to franchisees is their complete dependence, in a new system, on their franchisor attaining a critical size within a given period in order that the system achieves a market presence and obtains economies of scale. In comparison with independent entrepreneurs the reliance placed by franchisees on the continuing viability of their franchisor, though varying with the type of product, experience of the franchisee and extent of local consumer loyalty to a particular unit, is a disadvantage.

Whilst franchising offers immediate benefits to a franchisee arising from public awareness and acceptance of a given system, it is also found to bring attendant disadvantages stemming from public rejection of the system. A franchisee is thus potentially exposed to consumer reactions in response to the mal-practices of other participants within the franchise, including other franchisees and directly-employed unit managers of the franchisor or franchisees. A franchisee's success is therefore dependent in large measure on the ability of his franchisor to maintain adherence to the system's policies and standards by all system members.

Marketing activities undertaken by the franchisor, including the formulation of the concept, advertising and promotional activities, and market research often significantly vary in applicability, extent and effect with the particular stage of the franchisor's development, with the rate of development
of franchised outlets at a given time, and with the particular geographical situation of franchisees. Benefits from such services may not be broadly comparable to all franchisees within one system, and may not broadly accord with payments made by a given franchisee to his franchisor.

Whilst franchisees, like individual entrepreneurs, are necessarily restricted in their selection of suitable sites or premises by a need for the combination of certain factors to ensure future feasibility of the unit, they tend to be further restricted in their choice of location by franchisor development policy or by the existing distribution pattern of franchised outlets. Franchisees may therefore be channelled by the franchisor to or away from certain areas or may be severely restricted in choice of location in a mature system of considerable dimensions. Furthermore, unless protected by an appropriate clause in his franchise contract, a franchisee may be unable to protect the exclusivity of his catchment area, once his outlet is operating, from the encroachment by other franchisees or franchisor-owned outlets in the same system.

10.32 Financial Advantages and Disadvantages

10.321 Advantages

An important advantage of franchising to franchisees is seen to be a reduction in working capital needed to establish a unit. This is due to the saving in time and costs otherwise needed to plan, test and implement a concept and may also result from extended credit offered by the franchisor on supplies. There may also be a marginal reduction in investment capital required of the franchisee in circumstances where, for example, shopfitting services or items of equipment are obtained at competitive prices through or directly from the franchisor, though such a benefit does not appear to be as substantial as indicated in much of the franchising literature. In some systems, franchisors contribute to a franchisee's investment in the form of a long-term loan.
Franchisees obtain a major advantage stemming from their entry to an 'instant' market and from the supporting expertise of the franchisor, in that their units appear to become viable in a significantly shorter time than if they were independent, unbranded outlets. The quicker move into profitability and the proven nature of the concept reduce the franchisee's exposure to risk, which is also lessened by the tendency of franchisors to go to considerable lengths to protect their franchised outlets from failure, thus safe-guarding the image of the system in the eyes of both customers and other franchisees.

By joining in a relationship with a franchisor of proven reputation, franchisees are likely to gain easier access to development capital from banks and other lenders whose tendency is not to provide funds to individuals with no proven success and possibly no previous relevant business experience.

A further advantage to franchisees would seem to arise where demand from prospective franchisees outstrips the supply of potential sites (either because the system is already widely established or site requirements are difficult to fulfill). In these circumstances the saleable value of a franchisee's unit is likely to be increased over and above that justified solely by its trading position.

10.322 Disadvantages

The necessity of making an initial payment to the franchisor - of a franchise fee - brings a two-fold disadvantage to the franchisee: that of having to make an advance payment for a franchisor's concept and services before receiving any benefit from them or being able to assess their value in the particular set of circumstances; and that of investing in a purchase of intangible benefits which are not 'bankable'. Where the franchise fees are very substantial, as in the case of hotel franchises, this is a more significant disadvantage.
The requirement for franchisees to make a continuing payment to their franchisor is of proportionately greater disadvantage to those franchisees involved in a medium to long-term arrangement. For whilst the benefits and services obtained by franchisees in the initial stages of operation are likely to present exceptional value for money (taking into account the initially low sales volume in a new outlet and thus low payment to the franchisor), the situation is reversed after a period of time. As the franchisee gains experience of the particular concept and as an entrepreneur, he derives fewer benefits from the franchisor whilst continuing to make a similar or increased payment (the volume of sales being likely to increase as the unit becomes established, and gross turnover being likely to rise with inflation).

By being subject to constraints imposed by the franchisor to maintain a standardized image for the good of the system as a whole, franchisees may be prevented from pursuing a policy which, in their respective particular circumstances, would lead to profit maximization in their units. Restrictions precluding sales maximization (for example by preventing franchisees from meeting evident local demand for additional services or products) or constraints on lowering costs within the franchised unit, may thus be disadvantageous to an individual franchisee, at least in the short term and may also be against his long term interest.

Franchising also appears to give rise to particular problems for franchisees when a decision is made by the franchisor that the system is in need of significant changes requiring substantial re-investment and/or resulting in the loss of revenue whilst alterations are made. Whilst such changes may be of benefit to the system as a whole, they may not necessarily be cost-effective to an individual franchisee, and if the franchisor is able to enforce such re-investment it may not be at a time to suit the franchisee's particular financial circumstances.
If the franchise agreement contains restrictions upon the sale of a franchised unit (such as permitting the franchisor to have first option to purchase or allowing him to approve the prospective buyer) this may restrict the franchisee's ability to obtain a realistic selling price for his outlet, and thus prevent his capacity to build equity in his business.

Advantages

Franchising literature suggests that franchisees obtain substantial benefits from competitively priced costs of supplies (including food, liquor, disposable items, equipment and furnishings) either provided directly by the franchisor or through stipulated or suggested suppliers. Problems in making a comparison of quality and (in the case of consumables) of portion sizes prevent any conclusion being reached as to whether this claim is generally true in British franchise systems.

However, franchisees would seem to be benefiting from access to products which are specifically produced, portioned, packaged or purchased for their system, and which would not be readily available in such form to smaller purchasers with a less assured demand. Reliability of delivery is also a significant advantage to franchisees enabling a reduction in the amount of stock held and thus of working capital. In times of industrial disputes which might put at risk the supplies ordered by an individual entrepreneur, the purchasing muscle of the franchisor may be sufficient to ensure continuity of supply from the usual sources, or the franchisor may organize alternative supplies to all units in order to protect the brand name.

Lastly, franchisees appear to obtain significant benefits from a reduction in time and costs expended in activities related to purchasing. Thus a need to evaluate new product lines to select certain fresh supplies on a regular basis or to spend time in portion control is often eliminated by transferring it to the franchisor.
10.332 Disadvantages

Franchisees whose supplies are tied completely or substantially to a franchisor or to his nominated suppliers may be compelled to pay uncompetitive prices or to purchase goods of a lesser quality than desired. Constraints imposed by a franchisor similarly may prevent franchisees from flexibility in purchasing, thereby losing the opportunity to benefit from seasonal variations, special reductions etc. and possibly militating against the growth of local goodwill from local suppliers. Stipulations may also result in franchisees being forced to carry a larger range of stock (thus tying up more capital) than if they were free to select their own menu and own suppliers.

10.34 Operational and Managerial Advantages and Disadvantages

10.341 Advantages

A major benefit to franchisees is the provision by their franchisor of a total 'blue-print' of operation, incorporating plans, designs and inventory requirements for the unit, as well as defined policies, procedures and products. A franchisee thus obtains a very significant advantage over an independent entrepreneur in that the total operation has been designed, tested and modified in the light of experience, prior to his involvement in that system. Where the unit to be operated is of considerable size and complexity, such as an hotel, the information provided by the franchisor on, for example, the inventory required or systems to be installed, and supervision by the franchisor of the construction, is of very considerable value to a franchisee. In most systems franchisees also gain the advantage of their franchisor's help in selecting or assessing a suitable site or premises; this may be a critical factor for the success of their unit.

Another important advantage for franchisees is the initial training provided by franchisors, encompassing technical aspects of operation and sometimes supervisory aspects, and being either formal or informal, at a training centre or 'on the job'. Advice and assistance on operational and managerial aspects prior to, during and subsequent to the opening of a
franchised unit are of significant benefit to franchisees, especially those without former relevant experience of the particular market or of entrepreneurship.

Indications are that initially, though not necessarily over an extended period, franchisees benefit from a feeling of security engendered by their ability to shelter under their franchisor's 'umbrella' of experience and support, and by their membership of a group. Simultaneously it appears that they derive satisfaction from what they perceive to be independence of action, free from employee status.

10.342 Disadvantages

A significant disadvantage to franchisees is the need to comply with operating constraints or policies (such as particular promotional policies) of the franchisor, which, in the view of franchisees in general or of a given franchisee, may be unnecessarily restrictive or inapplicable to certain situations. Such constraints or policies may be against the best interests of an individual unit.

An important contribution to the franchise arrangement is the support offered by a franchisor to his franchisees including back-up services and a well-known brand image. However, such benefits are difficult to quantify or qualify, and thus franchisees suffer the disadvantage of normally being unable either to assess accurately or enforce their franchisor's performance of such matters.

Another disadvantage of franchising arises in the limitations usually imposed by franchisors on their franchisees' business interests. Restraints may be imposed on franchisees preventing them from becoming involved in any activity other than their particular franchised interest, or may restrict them from expanding their number of units which they wish to operate within their franchise system.
Schedule 10.2 Summary of Main Advantages and Disadvantages of Franchising to the Franchisee

ADVANTAGES

Marketing and Distributional

1. Proven marketing concept with 'instant' brand loyal customers.
2. Advertising and promotional activities beyond the resources of a single entrepreneur.
3. Access to market and technical research by franchisor.
4. Ability to enter market and effectively compete with established outlets of other systems or individuals.

Financial

1. Reduction in working capital needed to establish unit.
2. Possible reduction in investment capital.
3. Quicker achievement of unit viability and return on capital.
4. Reduction in exposure to risk.
5. Easier access to development capital.
6. Salesable value of outlet may be increased due to demand from prospective franchisees outstripping supply of potential sites.

Purchasing

1. Direct cost of supplies may be reduced.
2. Access to products not available to single entrepreneur.
3. Greater dependability on delivery of supplies.
4. Reduction in indirect purchasing costs.

Operational and Managerial

1. 'Plug-in' for implementing the concept including site assessment, plans, designs, inventory requirements, policies, details of procedures and products.
2. Initial and subsequent training, advice and assistance tailored to established needs of system.
3. Ability to establish own 'independent' business without necessarily having prior experience as entrepreneur.
4. Creates feelings of security from ability to shelter under franchisor's umbrella, and from membership of a group combined with satisfaction derived from freedom from employee status.

DISADVANTAGES

Marketing and Distributional

1. Dependence on accuracy of franchisor's predictions for the viability of the system and for any given unit.
2. In newly established system, dependence on franchisor reaching a critical size within a given period; continued reliance on franchisor's and system's viability.
3. Exposure to effects of malpractices by fellow members of the system upon existing or potential brand-loyal consumers.
4. Marketing activities, including advertising, promotions and market research may significantly vary in extent and effect with the life cycle of the franchisor and geographical location of the franchise.
5. May be restricted freedom to select operating area, or to protect area exclusivity once unit is established.

Financial

1. Advance payment of franchise fee is prior to receiving, being able to value accurately or enforce any benefits or services. Such intangible assets are 'barkable'.
2. Continuing payment to franchisor based on sales not profitability.
3. Imposed constraints may reduce profit-maximization.
4. Enforced re-investment may be neither cost effective nor relate to the financial circumstances of a given franchise.
5. Constraints on sale of unit may limit ability to build equity.

Purchasing

1. Where supplies are tied to franchisor they may not be at a competitive price or of the quality desired by franchisee.
2. Restrictions in purchasing flexibility.

Operational and Managerial

1. Operating constraints or need to comply with franchisor policy may be onerous and not in the best interests of an individual unit.
2. Difficulty of assessing and enforcing franchisor's agreed or prior indicated level of support and obligations.
3. Limitations imposed by franchisor on franchisee's existing or subsequently desired business interests (within or outside system).
4. Conflict arising from the unequal growth in characteristics of status, consumption of input to the arrangement and differing aims and expectations of the two parties.
Lastly, conflict stemming from the dynamics of the franchise relationship seems to be a significant disadvantage in some cases. The unequal growth in status of the two parties, the consumption by the franchisee of a large part of the franchisor's input to the arrangement, and the diversity of underlying aims and expectations of the two parties may lead to an unsatisfactory partnership.

10.4 PECULIAR TO THE ARRANGEMENT BETWEEN FRANCHISOR AND MULTIPLE FRANCHISEE (14)

10.41 Advantages to the Two Parties
The main advantage to the franchisor from entering into an agreement with a multiple franchisee centres on the greater ease of market penetration and increased market exposure over and above that provided by single franchisees. Particular benefits accrue to the franchisor from a multiple franchisee who is based in an area geographically remote from the franchisor's existing field of operation. In such cases the multiple franchisee is likely to bring benefits of local knowledge, locally-based development resources and local esteem.

Another advantage which is not necessarily provided by single franchisees is that multiple franchisees are often able to offer suitable sites to the franchisor to which they already have legal title, or through their existing contacts may quickly locate sites in desired areas. In some instances the prestige and potential of multiple franchisees' sites are such that they have a profound effect upon the whole franchise system.

Broadly similar financial and purchasing advantages accrue to the franchisor from arrangements with both single and multiple franchisees, but there is likely to be a further reduction in the franchisor's need for development management and for area management on a continuing basis.
Another advantage to the franchisor may be that by absorbing a substantial multiple franchisee into a given franchise system, the franchisor thereby eliminates a potential competitor. The advantages to the multiple franchisee of entering into a franchising arrangement are broadly comparable to those enjoyed by single franchisees in respect of marketing and distributional, financial and purchasing functions. Due to the extent of the multiple franchisee's own organizational resources, fewer operational advantages are gained than in the case of a single franchisee.

10.42 Disadvantages to Both Parties

The major disadvantage to the franchisor resulting from this arrangement is seen to be an accentuated problem of maintaining control over the system's brand image. This may stem from the involvement of another party - the franchisee's unit manager - over whom the franchisor has no direct control, or from the multiple franchisee's subsequent departure from the standard system, permission for which deviation was initially conceded during the course of negotiations.

A second substantial disadvantage to the franchisor contrasting with the arrangement with single franchisees, is that the unit managers of multiple franchisees do not have the motivation stemming from their ownership of the business, and thus are unlikely to strive to a similar extent, for the best possible financial and operating performance in their units.

As in the case of single franchisees, the franchisor suffers the disadvantage, prior to entering into an agreement, of having to assess whether the multiple franchisee has short and long-term objectives and expectations that accord or are compatible with those of the franchisor. Whilst the characteristics of the multiple franchisee are unlikely to alter as substantially as those of a single franchisee, his status and influence within the franchise system may increase (depending on whether restrictions have been placed on his growth and on the extent that deviations from the standard system have been permitted).
Summary of Advantages and Disadvantages Peculiar to the Relationship Between Franchisor and Multiple Franchisee

Advantages to the Franchisor

1. Accentuated advantages of market penetration and market exposure, particularly in areas geographically removed from the franchisor.

2. Easier access to suitable sites.

3. Broadly similar financial and purchasing advantages to those arising from arrangements with single franchisees.

4. Further reduction in need for franchisor development and area management.

5. Absorption of potential competitors into system.

Disadvantages to the Franchisor

1. Creates accentuated problem of control over system's brand image through involvement of a third party - the unit manager, and through initially negotiated deviations from the system conceded to the franchisee.

2. Does not provide access to motivated unit managers and thereby does not gain resultant benefits of improved unit performance and stability of operating management.

3. Difficulty of assessing whether objectives and expectations accord or are compatible, and of evaluating the multiple franchisee's future status and effect within the system.

4. Offers similar financial, purchasing and marketing disadvantages to those stemming from arrangements with single franchisees.

Advantages and Disadvantages to Multiple Franchisee

1. Broadly comparable advantages to those relating to marketing and distributional, financial and purchasing aspects for single franchisees.

2. Fewer operational advantages than those gained by single franchisees.

3. Comparable disadvantages in marketing, distributional, financial and purchasing aspects as those for single franchisees.

4. Disadvantages resulting from divergent policies and objectives.
The disadvantages of franchising to the multiple franchisee are by and large similar to those experienced by single franchisees, except in two respects: fewer limitations are likely to be imposed on the multiple franchisee's other concurrent or future business interests; and conflict which may develop between the two parties is less likely to arise from the dynamics of the relationship but rather from the divergent policies and objectives of the two parties, which may be implicit or explicit.

10.5 RELEVANT TO THE CONSUMER (15)

The following suggested advantages and disadvantages of franchising to the consumer are based on a theoretical assessment of the situation as seen in Britain and consideration of relevant propositions made in franchising literature (16).

10.51 Advantages

By providing an opportunity for small entrepreneurs to compete effectively with established units or systems, franchising allows a wider choice of goods and services to be offered in the market place.

Customers are also likely to benefit from a reduction in selling prices, resulting from three factors: greater competitiveness; economies of scale in production and distribution; and a more accurate alignment of production with demand, due to the tied nature of distribution outlets.

The advantages of branded, standardized systems are evidently preferred by a proportion of the population, who seek security in patronizing outlets with whose product or concept they are familiar (by previous direct experience or through patronage of other units of that system) or of which they are aware (because of wide public knowledge of the brand name and image). The ability to formulate a distinct picture of the product, type of service, eating environment and price, prior to patronizing a given outlet is therefore a considerable advantage to such consumers. By enabling widespread distribution of system units, franchising offers an increasingly mobile public (in domestic and international terms) the opportunity for greater security.
In outlets operated by single franchisees, their personal and financial involvement as owner-managers is likely to result in a better product, service and environment being offered to customers than that offered by disinterested employee-managers. The existence of the back-up services of the franchisor may enable the franchisee to spend a greater proportion of his time in directly satisfying his consumers' needs, and less on supporting activities.

The relative speed and ease with which market penetration can be achieved through the franchising method permits a rapid introduction in new systems of the benefits of technological development such as better food products, improved methods of service, better equipment etc. Such advantages therefore may be made available to a wider public more quickly than through slower developing wholly-integrated systems or through independently owned outlets.

Because a franchised unit is subject to a number of controls exercised by a franchisor, and because it is part of a large network, a customer is likely more easily to obtain redress for an unsatisfactory product. A franchisee may wish to prevent a disputed matter being drawn to the attention of his franchisor (thereby possibly putting his franchise agreement at risk), and may therefore prefer speedily to resolve a significant complaint in favour of the customer. In addition, the ability of a dissatisfied customer to take a complaint to 'head office' is likely to be advantageous, particularly where the 'head office' is anxious to maintain an overall good image of the system.

10.52 Disadvantages

Though franchising has been shown to lead to ease of market entry, thus increasing competition and challenging large, established systems, it may also be instrumental in leading to the demise of existing small, independent businesses which do not have access to such benefits of size and expertise as do franchised units. Where this occurs franchised systems are replacing independent outlets with semi-independent ones and introducing a standardized product and price structure instead of a variety of products and prices, thereby restricting the range of choice open to consumers.
It has been noted that franchising may result in a reduction in the cost of supplies, but this can be offset by additional expenditure incurred by the need to maintain standardized products, or by the necessity for an organization to support the franchise system. Thus franchising does not necessarily bring a more competitively priced product to consumers than would independent or wholly-owned outlets.

Customer security arising from the existence of standardized outlets has already been mentioned as a significant advantage. Also indicated previously is a major problem of franchisors to control their system members and maintain a standardized product and image. The advantage of customer security is turned to disadvantage if expectations of the product etc. do not accord with reality, thus causing dissatisfaction with a particular outlet and destroying a customer's future security within that system.

Whilst franchising permits the rapid introduction of a new concept, product, techniques or equipment, once a system is established there are greater problems in meeting changes in market demand than if all outlets were wholly owned or completely independent. Thus franchising may delay the subsequent introduction of improvements to a product or system, and inhibit the satisfaction of consumers' demands.

10.6 RELEVANT TO THE NATIONAL ECONOMY AND IN THE GENERAL INTEREST (17)

An assessment of the advantages and disadvantages of franchising is made in the context of a free market economy, and bearing in mind the broad objectives of serving the interest of consumers whilst optimally using resources. Little empirical research has been carried out to support or confound the claimed advantages and disadvantages in franchising literature and none at all relating to the British situation. Such research was beyond the time or resources available for this study. The following advantages and disadvantages are put forward after a close examination of the relevant literature and a theoretical assessment of their applicability to the current British scene.
Schedule 10.4

Summary of Advantages and Disadvantages of Franchising to the Consumer

Advantages

1. Permits wider choice of goods and services to be offered in the market place by enabling effective competition with established systems.

2. May result in the transmission to customers of a reduction in price arising from economies of scale in production and distribution.

3. Provides wider opportunity for customer security, particularly to the travelling public.

4. Likely to result in higher standards of products and service maintained by owner-managers.

5. Creates means of quick, widespread innovation of benefits from technological development eg. improved equipment, methods of service and food products.

6. Improves likelihood of redress should product be unsatisfactory.

Disadvantages

1. May result in restriction of choice to consumers because of inflexibility of prices and products within a given system.

2. Customers may not benefit from cost reductions, because of the balancing expenditure required to sustain the system.

3. Difficulty of controlling franchisees' compliance with standard image may destroy customer security in branded product.

4. Ability to accord with changes in market demand or to introduce improvements for the benefit of customers may be restricted.
Advantages

An important ingredient of a free market economy is the existence of plurality in the market place. Franchising, as a proven viable alternative to vertically integrated organizations, appears to reduce economic concentration. However, suggestions have been made that franchising only decreases concentration in the short term, whilst leading to a reversal of this characteristic in the long term (18). Two trends in the U.S.A. point to the latter claim: the tendency for a number of franchisors, once a given system has reached the required size and maturity, to purchase and retain under their ownership a significant proportion of formerly franchised outlets; and the proliferation of purchases of existing franchise systems by conglomerate organizations. The very limited extent of franchising in Britain provides inadequate experience by which to assess whether franchising offers a short or long-term means of reducing economic concentration in this country, but on balance the evidence would seem to point to the beneficial rather than detrimental influence of franchising in this respect.

By facilitating the introduction to the market of a new product or concept and by providing a relatively easy means of extending the geographical penetration of existing products and concepts, franchising offers a significant advantage especially where there is a short life expectancy of the popularity or applicability of a particular product-line.

As in a completely integrated distribution system which includes units of production and tied outlets, franchising aids the broad matching of production to demand, and leads to economies of scale in production and distribution, and in purchasing and marketing. Franchising offers the further advantage of being likely to lead to a nearer optimal utilization of the resources of investment, unit management and labour, due to the personal and financial interest of single franchisees as owner-managers.
Claims have also been made (19) that franchising substantially reduces the rate of failure in small businesses, and thus helps to conserve the assets of such businesses as well as lessening economic disruption and resultant unemployment. Whilst there is no conclusive evidence to support such an hypothesis (20), the existence of the franchisor's vested interest in the success of each and every outlet within a system, combined with the proven nature of the product or concept being franchised, together suggest that franchised outlets are less likely to fail than independently-owned outlets.

It has been established in the U.S.A. that franchising does aid individuals to become self-employed businessmen who would otherwise not have been self-employed (21). In much of franchising literature the concept of self-employment is equated with independence and is regarded as a desirable objective in itself. However the notion of 'independence' is both relative and subjective and is not necessarily an advantage. A more valid claim for franchising is that it helps to create small businesses and self-employed businessmen most of whom perceive themselves to be independent, and who are likely to use their resources more efficiently than if they were not franchised (22). Such an advantage is significant in this country at a time when there is governmental and public interest in, and concern for the improvement of the position of small businesses within the economy (23).

Franchising not only assists in the transformation of individuals from employee-status to that of being self-employed, but also provides a means for them to enter a new sector of business activity with relatively little risk. Franchising thus would seem to be a useful tool for the redeployment of those members of the workforce declared redundant from their original occupation or trade. It is further suggested that franchising has potential as a means of social engineering to advance the interests of those who are disadvantaged by the lack of education or by race, such as immigrants to this
country. Whilst franchising has not been successful in this respect in the U.S.A. (24) it does appear to have been a useful method of business entry for a number of immigrants in Britain (25). One factor militating against this, and resulting in the exclusion of certain groups of potential franchisees, such as younger people, is the requirement for capital investment.

A characteristic of franchising both in this country and in the U.S.A. is its particular suitability as a means of fulfilling demand and creating employment in a wide range of service industries. Franchising therefore seems to be an appropriate business method for the British economy, where the significance of the tertiary sector is increasing (26) and where there is a relatively high level of unemployment.

In addition franchising is seen to offer considerable advantages to those wishing to export products or services, particularly to countries in which there is antagonism to foreign ownership of outlets, or where there are significantly different laws, business customs or markets which can best be dealt with by locally-based 'partners' (27).

Lastly, franchising has been claimed to increase overall investment, employment and consumer expenditure. Some doubt has been thrown on whether the first two contentions are valid, whether franchising merely leads to earlier investment and employment than would otherwise apply, and shifts their form and locus. The increased efficiency of franchised outlets attributable to the proven nature of the system, to the support of franchisors and to the involvement of owner-managers, suggests that the overall levels of investment and employment may actually be reduced (28). The suggestion that franchising creates additional consumer expenditure seems valid because of the greater attention normally paid by franchisors to marketing (including more aggressive sales and promotional activities) than that by individual unit owners. However, whether consumer expenditure in franchised outlets raises the overall level of expenditure, or merely re-channels it from non-franchised outlets or from different markets, has not been established. On balance, however, it would seem that
the obvious dynamism of franchising in the American economy has spurred overall growth and progress, and is likely to offer similar advantages in this country.

10.62 Disadvantages

Although it has been suggested that franchising increases competitiveness in the market place by enabling the growth of competitive systems, there is a counter effect resulting from inflexibility of pricing and standardization of product inherent in franchise systems. This dual aspect has been and remains the cause of dilemma in the U.S.A. On the one hand franchising has been labelled as collusive and anti-competitive; on the other, proponents of the franchising method suggest that if it were replaced by completely integrated distribution systems, the result would be an even less competitive environment. Legal decisions in the U.S.A. reflect the differing attitudes on whether the controls and co-operation in franchising arrangements are pro or anti-competitive, and whether they are for or against the public interest (29). It has been suggested that in trademark licensor-retailer franchising, including hotel and catering systems, the need for strict control over the quality of products and service is essential to the trademark and that such controls may therefore be regarded separately from controls in other forms of franchising, their net result being to protect the consumer by ensuring compliance with trademark law (30).

The other disadvantage which is attributed to franchising, stems from the fiduciary nature of the arrangement, the lack of negotiating flexibility of the weaker party and the difficulty of defining, in precise qualitative and quantitative terms, the short-term and continuing services and benefits to be performed or given by the dominant party. It is claimed that at best this may lead to unsatisfying relationships and at worst, may attract individuals or companies as franchisors whose intentions towards franchisees and the general public are unethical. Whilst this hazard is encountered in franchising, it is one that is applicable to other contractual arrangements which involve intangible services rendered by one party to another, and/or which are of a fiduciary nature, and is therefore not an indictment of franchising per se.
Schedule 10.5

Summary of Advantages and Disadvantages of Franchising to the National Economy and in the General Interest

Advantages

1. Creates plurality in the market place with attendant advantages to consumers arising from competition.

2. Allows ease of market entry to new products or concepts, ie. product extension, and ease of geographical penetration of existing products, ie. spatial extension.

3. Enables the improved use of resources by better reconciling production with demand, by obtaining economies of scale, by improving the use of investment, management and labour, and assisting in the stability of system units.

4. Assists in the creation of small businesses and small businessmen.

5. Broadens opportunities for individuals wishing to alter their status (from employees to being self-employed) or desiring to alter their fields of business. Is a method of advancing the interests of socially disadvantaged sections of the population, and may be a means of re-deploying redundant workers.

6. Fulfills demand and creates employment in the tertiary sector of the economy.

7. Is useful means of exporting visible or invisible products and services.

8. May increase investment, employment and consumer expenditure.

Disadvantages

1. Leads to growth in the number of tied outlets controlled by fewer producers or service-sponsors and thus increases concentration.

2. May result in the closure of non-implementation of non-standardized outlets offering individual products, services and price structures, thereby being anti-competitive.

3. The fiduciary nature of the arrangement and the difficulty of precisely defining the initial and continuing contribution to be made by the dominant party, may lead at best to unsatisfying relationships, and at worst may attract unethical franchisors.
10.7 CONCLUSIONS AND SUGGESTED 'BEST PRACTICE'

10.71 Overall Assessment of the Value of Franchising

After weighing up the advantages and disadvantages for participants in franchising systems, the conclusion is reached that the initial benefits to the franchisor and to the franchisee are substantial and synergistic. Their mutual participation thus increases market penetration, financial leverage and economies of scale in purchasing and expenditure which are considerably greater than the sum of their two separate endeavours. The disadvantages for the franchisor and the franchisee, stemming from the need to maintain a standardized image and the subjugation of the good of any one part of the system to that of the whole, are more apparent during the continuation of their relationship. But it is suggested that whilst these should not be ignored or trivialized when assessing the franchising method, they may be reduced by a carefully planned and implemented franchise arrangement, so that in overall terms the advantages of franchising considerably outweigh the disadvantages.

It is more difficult to assess whether in overall terms franchising arrangements with multiple franchisees are broadly beneficial to both parties. It seems that such arrangements must be carefully assessed on their individual merits, taking into consideration both the short and long-term advantages and disadvantages, and the likely effect of such arrangements upon other system members.

Though not backed by empirical findings, it seems that on balance franchising offers considerably advantages to consumers, producers and investors in a free market economy, which substantially outweigh the disadvantages.

10.72 Recommended 'Best Practice'

To suggest 'best practice' in respect of all aspects of franchise operation would be beyond the scope of this study, as it would require very comprehensive and detailed recommendations applicable to different types of franchises, situations
and organizations. However, the following suggestions are put forward in the light of the findings of this study, as being likely in most situations to maximize the advantages and minimize the disadvantages of franchising to franchisors and franchisees. However, in the final analysis the success of a franchising relationship depends upon a mutuality of aims and pooled goodwill of the two parties, rather than upon lengthy and detailed franchise agreements and closely defined conventions.

10.721 Testing of concept.

The concept being franchised should be adequately market-tested in a number of outlets over a representative period prior to its being offered to franchisees, thereby enabling a franchisor to be fully cognisant of all operating problems and able to produce an accurate assessment of a given outlet's viability.

The ownership and operation of outlets on a continuing basis by a franchisor is also necessary in order that the franchisor may be aware at first hand of changes in market demand, be able to test new products or ideas, and be able to demonstrate to existing franchisees the feasibility of implementing such innovations.

10.722 Adequate disclosure of franchisor background

So that prospective franchisees may come to an informed decision as to whether to enter into a franchise relationship with a given franchisor, details should be furnished by the franchisor not only on the background of the franchise company and its directors, but also on the current number of outlets, extent of franchisor organizational resources to support the system, future plans for the system and predicted trading figures for franchised outlets. The names of several existing franchisees should be given as 'referees' for the franchisor, and copies of the franchise contract should be available for persual at leisure. Franchisees should be advised to consult a solicitor and/or accountant.
10.723 Franchise contract

So that franchisees are fully aware of the precise rights and obligations of both parties, franchise contracts should be written in a readily understandable form (keeping legal terminology to a minimum) and should clearly set out the respective rights and duties of the franchisor and franchisee, with as equal a distribution as possible between the two parties. All terms within the contract should be frank, fair and enforceable.

Clauses permitting termination for non-compliance with obligations or because of financial insolvency, should be equally applicable to either party. Where an operating manual is expressly included as part of the franchise contract, a minor violation of one or more of its conditions should not be sufficient to justify the termination of a franchise. It is suggested that the duration of the agreement should be of a sufficiently long period, say a minimum of five years, to permit the franchisee to formulate a medium-term policy and to avoid management by crisis.

10.724 Source of franchisor income and fee structure

Full disclosure should be made by the franchisor as to the source of his remuneration, which should stem from a combination of an initial franchise fee together with a continuing royalty or premium on food or other supplies. Undisclosed sources of income to the franchisor such as discounts from suppliers or a retained premium on equipment which franchisees are directed to buy from or through the franchisor, are advisable. If the purchase of such equipment is tied to the franchisor, a full statement of its cost to the franchisee should be accompanied by current market prices of comparable equipment, and an indication of any differences in quality, performance etc.

The establishment of a fee structure which equitably reimburses both the franchisor and franchisee requires fine judgement. Three criteria need to be satisfied. First, the structure of fees should broadly accord with the dynamics of the franchise relationship. Thus a substantial payment should be required
of the franchisee at a time when the franchisor's contribution is most evident and most appreciated by the franchisee, i.e. when he is given the blue print of the franchise operation and implements his outlet with the advice and assistance of the franchisor. Once the franchisee has consumed this initial input by the franchisor and has established himself, his need for support lessens and his attitude towards paying the franchisor a continuing sum (either as a royalty or premium on supplies) is likely to be less enthusiastic. Hence the continuing payment should be kept at a relatively low level.

Secondly, although it is advocated that initial fees should be substantial (not only because of the above reasons, but also because the franchisor needs to be assured of the franchisee's substantial commitment) and that a continuing fee be relatively low, the franchisor should guard against giving the impression that his main interest is for a short term arrangement to gain maximum 'front-end' fees, rather than for a long-term continuing relationship. Initial fees should therefore be commensurate with the benefits offered.

The third criterion is that the fee structure should encourage a concordance of aim between the two parties. In circumstances where the franchisor's remuneration is linked to the franchisee's gross revenue, but the franchisees' financial reward arises from his profit, there is an underlying conflict. It is therefore suggested that the franchisor's remuneration should be based on the franchisee's profitability rather than, as is usually the case, on his sales turnover.

The decision of which method of continuing remuneration is more suitable is influenced by a number of aspects, including whether the franchisor wishes and is able to undertake the role of supplier or wholesaler, whether he desires to maintain
central control over products, and whether it is more practicable for him to monitor franchisees' takings (thus checking on the amount of royalty due) or to check that franchisees do not obtain supplies from other than the stipulated source (thus ensuring that there is no avoidance of paying premiums to the franchisor). A further point that should be taken into consideration is the attitude of franchisees towards making a continuing payment; in circumstances where a royalty is payable, franchisees (as they make out a lump sum payment at the end of each month, or whatever period is agreed) tend to question whether the value of their franchisor's services is commensurate with such a payment. Alternatively, those whose continuing payment to their franchisor is through a premium on supplies, tend to compare the cost of their food products (or other supplies) with that obtaining in the market place, and if the product is not unique, are apt to chafe against the tie on supplies and the higher price charged by the franchisor.

10.725 Franchisor Services

To counteract the feeling amongst established franchisees (once they have consumed a significant part of their franchisor's input) that their continuing payment to the franchisor is not balanced by equivalent support, the franchisor should endeavour to supply continuing tangible benefits and services, including national and local advertising, sales promotion, market and technical research and development and training facilities. Where such benefits can be quantified (as for example, with hotel reservations and referrals transmitted by the franchisor to the franchisee or with a predictable increase in sales volume following a television advertisement for the franchised product) franchisees are less likely to question whether they are receiving value for money from their franchisor.
Other supporting services such as advice and assistance with book-keeping, tax returns, payroll preparation, auditing and stock-taking may be offered by franchisors. It is suggested that whilst such services, as part of the franchise package, may be appreciated initially by franchisees, they are likely in the long-term to question whether the franchisor is offering a benefit or invoking a means of control, and to feel that such intervention in their business demonstrates their lack of true independence and indicates a role comparable to that of directly employed managers. Such services should therefore be optional and charged at cost.

10.726 Franchisor controls

These should be reduced to the minimum necessary to protect a given system's brand image and trademark for two reasons: to avoid potential legal actions brought against the franchisor for restraining the trade of his franchisees; and to allow a degree of freedom of action to franchisees, whose quest for independence or semi-independence should not be too obviously thwarted by constraints. Careful consideration should be given to the necessity for tying franchisees on the supply of food, liquor, disposables, equipment, etc. and to whether there is a need for influencing selling prices, and controlling the hours of business and other operating conditions imposed on franchisees.

Whilst it is recommended that controls should not be greater than necessary, such as are deemed valid should be strictly maintained for the good of all participants within a system. It is suggested that not all franchisees are fully cognizant of the nature of their interdependence with other members of their system and of the extent to which their actions (whether to improve their franchised product by offering better value for money, or whether to improve their short-term profitability by reducing costs) may adversely affect others and vice versa. Three ways are proposed of promoting compliance with controls and adherence to changes in franchisor policy: by contractual means, by demonstration and by pressure from other system members.
The reasons for the necessity of compliance with franchisor controls and the extent of such control should be clearly set out in franchise contracts, and should be backed by periodic visits from field supervisors with special training for their task of co-ordinating the activities of self-employed unit owners. It is suggested that to ensure the maintenance of the required levels of hygiene and decor in franchised outlets, a clause should be contained in franchise contracts requiring such re-investment at stated intervals and proposing a means of seeking an independent opinion should the franchisor and franchisee disagree over the timing or need for re-equipment or redecoration.

The second method of achieving franchisee compliance with controls or with required changes to the concept is for the franchisor to demonstrate, in his directly operated outlets, the efficacy of so doing. This is particularly appropriate where the franchisor requires substantial alterations to be made to the system's product or image in order to accord with changes in market demand, or where an entirely new alternative concept is being introduced as a means of replacing a system whose useful life is coming to an end.

It is suggested that a third means of gaining franchisee compliance is through pressure exerted by his peers at franchisee meetings. Group condemnation of a franchisee's unwillingness to conform may be more effective than remonstration by a franchisor.

10.727 Franchisee Rights

It is suggested that when a franchisee is granted the right to operate in a particular unit, he should also be given exclusivity of a defined area, thus protecting the viability of his outlet from incursions by other franchisees or directly-operated units of the same system.

The practice of some franchisors of leasing out premises to franchisees, or of purchase from and lease-back to franchisee-owners is advantageous for the continuity of the franchise system and for the franchisor, but it places franchisees in a vulnerable position for they are dependent upon the contin-
uation of both a franchise agreement and a lease and are unable to build equity in their business. Such a practice is not in the interests of franchisees.

Whilst it is suggested that franchisors should vet prospective purchasers of a franchised outlet, in order to maintain standards of the system, the practice by some franchisors of themselves having first option to purchase a franchised unit should be discouraged, unless an independent valuer is appointed. Furthermore, a franchisor should not be able to stop assignment or sale of a franchised outlet, without providing a valid reason for so doing.

10.728 Recognition of Franchisee's Special Status

The extent of standardization within a franchise system depends upon the type of outlet concerned (being a hotel, restaurant, or 'take-away' unit) and on the market level at which it aims. However, it is suggested that even where strict standardization of the product and environment is required, there should be left some area of discretion for the franchisee, so that his perception of his status as an independent or semi-independent entrepreneur may be maintained. Such discretion could be channelled, for instance, to offering a special dish of the day selected from a bank of recipes approved by the franchisor, or to choosing certain fixtures and fabrics providing that they accord with the overall theme of the franchise system.

Recognition should be accorded by the franchisor to the importance of franchisees as substantial investors (of their capital and labour) in the franchise system, and as channels for marketing feedback. It is suggested that the recognition of franchisee representatives, together with the organization of meetings in which all system members can participate, is a means of satisfying both requirements as well as creating an esprit de corps. The franchisor is provided with information; franchisees benefit through the satisfaction of their need to affect and be seen to affect franchisor policy in matters pertinent to all system members, such as pricing, purchasing and advertising policy and product development. The role of franchisee representative and/or the ability to influence the
franchisor may also serve to accommodate those franchisees who are no longer dependent to any significant extent upon franchisor support and who have a need to demonstrate their newly-acquired, independent status by other means. A further aid to maintaining franchisee morale and increasing motivation is the distribution of some form of regular bulletin to franchisees, giving news of the system, of franchisor policies and personnel, and of the franchisees themselves. Such a publication may also be used as a vehicle for organizing intra-franchise competitions to boost sales or profitability and to reduce complacency amongst franchisees.

10.729 Multiple franchisees

An arrangement between a franchisor and a multiple franchisee needs to be carefully assessed as to the advantages and disadvantages likely to accrue to both parties and to the system as a whole. It is suggested that if significant departures from the standardized system image are conceded to one or more multiple franchisees, in a system where both single and multiple franchisees operate, such special terms may be the seeds of future problems amongst system members which will far outweigh the immediate advantages derived from such arrangements.

A number of multiple franchisees have grown to that status through gradual expansion from the initial ownership of only one unit. Whilst the latitude for such expansion may be beneficial to both the franchisor and franchisees, it is suggested that inadequate attention is normally paid to the significance of the first step by a franchisee from a sole role as owner-operator to that of a combined role of owner-operator and employer of a paid manager in a second unit. In circumstances where a franchisee has achieved excellent results in a single outlet, he is likely to be granted permission to open a second. However, the additional role is likely to demand specific qualities that may not necessarily exist within the franchisee and, for example, the inability of a franchisee to control his unit manager may have far reaching results upon all system members. It is therefore suggested
that the implications of allowing even just two outlets per franchisee should be properly considered and that a different type of training and advice from the franchisor organisation is required in those circumstances.
CHAPTER 11

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CHAPTER 11

OUTLINE OF GENERAL TRENDS IN BRITAIN AND WITHIN THE HOTEL AND CATERING INDUSTRY AND THE APPLICABILITY OF FRANCHISING

This chapter cannot attempt to be a comprehensive and detailed review of all major economic, business and consumer trends in Britain, nor indeed of all such trends within the hotel and catering industry. It is intended to give only a broad indication of those current developments and tendencies which are likely to affect actual or potential franchisors and franchisees, and therefore the future of franchising in the British hotel and catering industry.

11.1 GENERAL BUSINESS CLIMATE WITHIN BRITAIN

The general climate in which business functions in Britain is subject to many factors too diverse and complex to be given detailed consideration in this study. Certain aspects, however, are outlined below, which appear to be of particular relevance to the future of franchising in general terms (not specifically related to hotel and catering activities).

11.11 Economic Concentration and its Antidotes

During the last two decades there has been a trend towards economic concentration within Britain. Large numbers of small companies and individually-owned units have been taken over by, or merged with larger companies, sometimes to the extent of causing a potentially monopolistic situation within a particular industry or sphere of business activity. In recent years, however, there has developed a growing awareness that 'big' is not necessarily 'beautiful', and a questioning of the validity in all circumstances of growth as a necessary and desirable objective. Awareness has been shown by the public, by economic commentators and by the government, of the problems of small businesses and some attempts made to facilitate their survival and to create conditions to encourage the development of other such businesses. Their existence is generally viewed both as a means of avoiding a monopolistic situation and of maintaining buyer:seller relationships on a scale that allows a personal service to be rendered and received.
11.12 Fiscal Policies and Availability of Finance
Corporate expansion and re-investment has been retarded in this country in recent years by fiscal policies and by the general financial climate. Various taxation measures have militated against the accumulation of cash flow to be used as internally generated capital funds, and the scarcity and/or cost of external finance has had a depressant effect. It has been claimed that such circumstances preclude the creation and subsequent expansion of businesses on a scale and of a potentially similar success to that, for instance, of a Marks and Spencer. The actual or claimed inadequacies of traditionally accepted methods of raising finance may lead to the wider search for, and use of other methods of obtaining funds for development and re-investment.

11.13 Government Intervention in the Private Sector
There is an increasing tendency for government to intrude into the normal commercial and contractual practices of private enterprise, with the aim being to protect employees, consumers and the national economy, whilst usually making more complicated and exacting the role of the producer/supplier-employer. In recent years examples of such intervention include a considerable amount of legislation regulating employment practices, forbidding discrimination on the grounds of sex or race amongst actual or potential employees or customers, controlling the pricing policies of larger companies, and requiring a considerable amount of the trader's or company's time as unpaid tax collectors for the Government. This situation may influence businessmen to seek ways of avoiding the responsibilities resulting from being large-scale employers or sellers to the public, and to restrict their direct interests to a level at which they escape government attention or minimize the extent of their required statutory co-operation.

11.14 Level of Unemployment
The level of unemployment in Britain is currently higher than normal, and though likely to be reduced in the short term is unlikely to be significantly lowered in the long term because of increasing automation. Those employees who have been or will be made redundant can be viewed as potential material for alternative occupations to those which they previously enjoyed, and potentially available to join in new forms of business arrangements, such as franchising.
The pre-requisite for such persons to own or have access to funds for investment is particularly likely to be met by those who were formerly top executives, in Her Majesty's forces, or ex-colonial or ex-diplomatic services, who normally receive a substantial severance payment. Recent employment legislation, making compulsory the payment of substantial redundancy compensation to all employees (after a qualifying period) will further extend the range and number of people able to command at least some funds for initial investment.

11.15 Appeal of Self-Employment

During the 1970s a number of factors have served to accentuate the appeal of self-employment to those who have customarily been employees. Successive restraints on salaries imposed on the public sector by the Government during recent years have contributed to this outlook, particularly amongst those employees such as middle management against whom such restraint has had the most effect, by significantly eroding pay differentials between them and those employees for whom they are responsible.

There has also been a trend towards greater formal worker-participation in deciding company policies, and an increase in trade union power which has had the effect of influencing the activities of many businesses and reducing the authority of the management. Together these factors have eroded the discretion and status of middle management, and consequently their motivations.

The high level of direct personal taxation on earned income has also been instrumental in affecting the outlook of employees, amongst whom there seems to be a wider appreciation of the benefits of tax avoidance, and in some instances of tax evasion, both of which can be more easily implemented if the individual is self-employed.

Apart from the direct financial benefits, there appears to be a more widespread search for an improvement to the quality of life, expressed as a desire for self-fulfillment. It would
seem therefore that there is a need for a means by which the financial reward of individuals may be seen to correlate more closely with their working effort, and by which they may gratify their urge to achieve self-esteem.

11.16 Applicability of Franchising

A review has previously been made of the characteristics of franchising and an assessment made of its net advantages to the national economy, the consumer and to the franchisor and franchisees. Set against the background of the current business climate in Britain, it would appear with some reservations (1) to be a particularly applicable method of distribution and of doing business. The synergistic benefits arising from the mutual interests and activities of a franchisor and his franchisees enable easier market entry and a more effective means of combating competition - thus providing one answer to the trend towards economic concentration, and an alternative means of raising developmental funds at a time when more traditional financing methods may be inadequate.

By operating a franchising system as opposed to a wholly-owned and operated system, an entrepreneur-franchisor may avoid some of the problems arising from increased legislation and government intervention in commercial practices. A franchisor may thus avoid direct responsibility for costs and problems arising from new employment legislation (except in respect of the normally relatively small proportion of directly-employed personnel), may avoid the government-imposed restrictions on selling prices (because of the small, net size of the franchisor's direct interests) and may substantially reduce the amount of time required by bureaucracy in such matters for example: as compiling Value Added Tax returns.

Franchising offers further advantages as a particularly appropriate method of business operation for service industries, which are both labour-intensive and a growing sector within the economy. Not only does franchising offer a mechanism for the creation of new jobs in this sector, but it also appears to reduce the likelihood of failure of such businesses and offers a means of disseminating business skills. Thus it would seem to present a mechanism not only for reducing unem-
ployment, but also for the efficient re-deployment of human and financial resources from one business activity to another, and from one geographical region to another. It may further offer the opportunity of social manipulation to benefit disadvantaged sections of the population.

There are, however, two obstacles which militate against the use of franchising as a mechanism for re-deploying redundant workers or for employing those who are otherwise disadvantaged. The first is the attitude of redundant workers towards changing their type of occupation and towards the franchising arrangement per se. The second is the need for capital which is likely to exclude certain sections of the population such as young people, some immigrants, and others caught in the poverty trap.

Despite some uncertainty about attitudes of those who are potential franchisees, shifts in the general attitude towards self-employment seem likely to create an atmosphere conducive to the growth of franchising. For those suited to a semi-independent status, franchising offers obvious advantages of a long-term nature. For those of a truly independent inclination, franchising provides a transitional mechanism by which employees may become entrepreneurs in their own right after a short to medium-term 'apprenticeship', their place in a given franchise system being taken by new franchisees. Providing that both franchisors and franchisees are fully cognisant of the characteristics of franchising, it is suggested that such a method offers considerable net advantages in the current business climate in this country.

11.2 SOCIAL CHANGES AND ALTERATION IN CONSUMER PROFILE
A number of social changes are perceptible which affect the general profile of consumers and which have particular ramifications for the hotel and catering industry.
11.21 Life-Style of Population

There has been a marked increase in the number of married women seeking paid employment, due to factors such as the reduction in the average number of children per family, increasing pressure on the family budget because of inflation and wage restraint, and a move for the greater emancipation of women. This has had the two-fold result of raising disposable income available to many families, and creating a need to replace the former unpaid services of the wife by the purchasing of goods and services from outside the home. Though partly attributable to current economic difficulties experienced in this country, such a trend is likely to continue and accelerate, as it has done in the U.S.A.

There is also a long-term trend (partly attributable to automation, to a larger potential work force and to other social pressures) towards a reduction in the average working week. This will bring greater opportunities for leisure to a wider section of the population, and is likely to stimulate the requirement for associated goods and services.

In relation to the hotel and catering industry, the advent of the working wife creates conditions where a broader section of the community seeks replacement catering services, particularly those of a speedy, refuelling nature such as 'take-away' products or those from fast food restaurants. The trend towards increasing leisure time is similarly likely to increase demand for hotel, catering and ancillary services, though the particular market level which will be affected is dependent on the extent to which disposable income matches disposable time.

11.22 Distribution of Wealth

In recent years there has been a trend towards the re-distribution of wealth, particularly of disposable income amongst different age and socio-economic groups in this country. The increased
importance of the purchasing power of the young has affected a very wide range of producers and suppliers, as has (to a lesser degree) the transference of purchasing capacity to socio-economic groups C2 and D.

A general characteristic of both groups is a preference for less formality, whilst the young also tend to have greater disposable time and a higher degree of mobility than other sections of the community.

Combined with other factors (2), the impact of these new consumers of catering services has had far-reaching consequences. In general they have shown a preference for, or ready acceptance of a reduction in the complexity of food products and of food service, and a desire for a more informal environment. Thus more simple, standardized dishes are now widely offered; self service or part self-service is practised in markets where previously waiter or waitress service was expected; 'fun food', snacks and 'take-away' products are gaining in popularity; environmental themes are more widely used in the catering situation.

Changes in consumer profile have also had a considerable impact (in combination with other factors) upon the provision of hotel accommodation. There has been considerable growth in the demand for self-service holiday accommodation, a move away from full-pension terms in hotels, a trend towards replacing traditional-type hotel-restaurants with a less formal eating environment, and a reduction or elimination of a number of services which previously were provided by hotels.

11.23 Changes in the Consumer Profile
Widespread car ownership, giving increased mobility to a large proportion of the population has also had an effect on consumers, many of whom need to be assured in advance of the reliability of the goods and services which, in an unfamiliar environment, they are considering purchasing.
A further change in the consumer profile stems from the current moves towards greater consumer protectionism. Those who purchase goods and services are more than ever likely to be aware of whether these have been adequately described, whether they represent value for money, and are more likely to attempt to obtain redress if the answer to both is negative.

The implications of the above trends for the hotel and catering industry are that there is likely to be an increasing number of consumers who desire security when faced with selecting a product or service, and who may prefer to patronize establishments which, by dint of their standardized product and established reputation, facilitate an assessment being made of whether the product accords with its description and is as expected, and provide a greater likelihood of redress should the need arise. Thus it follows that standardized systems, with wide-spread geographical representation, are likely to have increasing appeal to consumers.

The advent of relatively cheap travel has introduced a broad spectrum of the indigenous population of this country to foreign cultures, products and customs. Widespread exposure to television programmes and advertising has similarly expanded the horizons of many people. Added to this the growing numbers of in-coming tourists to Britain, as well as the increasing national and racial diversity of the resident population, has broadened demand for different types of goods and services.

Such a trend towards internationalization and specialization of demand has had a number of effects upon the hotel and catering industry. Of relevance in the context of this chapter is the resultant market for 'ethnic' food and speciality restaurants, some of which have already proliferated (such as Indian and Chinese restaurants and 'take-away' outlets), and others which seem likely to have a considerable future impact (such as American hamburger bars).
11.24 **Applicability of Franchising**

The social trends outlined above and the consequent changes in consumer profile suggest that in overall terms the demand for hotel, catering and associated services is likely to increase, though substantial shifts will continue in the proportionate demand between different sectors and markets. In combination with other factors these changes result from a general requirement for less formality, a willingness to accept fewer services, and an increased appreciation or acceptance of standardization and specialization of goods and services.

Reference has already been made to the particular (though not exclusive) applicability of franchising to the sale of a highly standardized product or service. A second characteristic of franchising is that it involves a network of standardized outlets. In Britain franchising in the hotel and catering industry has been almost exclusively confined to the fast food restaurant sector - an area of activity which normally combines both the above attributes - and in the U.S.A. growth in fast food franchising has been spectacular. Franchising seems to be a highly suitable mechanism for providing this type of 'refuelling' catering services of a standardized nature, and for providing accommodation (with or without ancillary services), to a mobile public in need of customer security in a standardized network of outlets.

Through the dissemination of a brand image and an implied quality control, franchising offers to the public a yardstick with which to evaluate and compare the purchased product or service with that held out by the producer or supplier. The franchisor's interest in protecting the system's image further suggests a greater likelihood of redress to complaining customers than in the case of a small, independent outlet. In both respects, franchising offers advantages to a public increasingly concerned with consumerism.
Whilst franchising has not enjoyed any significant penetration in the 'up-market' restaurant sector or in hotels in this country, there would seem to be no significant bar to its use in such markets. In the U.S.A., the franchising method has been successfully used in establishing or enlarging chains of hotels which, though not in a luxury category, have been in a medium to high price range. The necessity for clearly defined and adhered to standards within a franchise system does not infer that such standards must relate to a low-priced product. It is suggested that franchising is also a suitable mechanism for meeting demand for, for example, hotel and catering services other than of a 'refuelling' or basic nature, such as 'ethnic' restaurants.

11.3 PARTICULAR TRENDS WITHIN THE HOTEL AND CATERING INDUSTRY

As mentioned above, this section cannot hope, in the space and time available, to provide a detailed examination of current changes and trends within such a diverse industry as that encompassing hotels, catering and associated outlets. Brief mention is made only of such trends as are thought to be of direct relevance to this study.

- 11.31 Rising Costs and Pressures on Profitability

Most businesses in the industry have been affected by significant increases in the cost of sales. Such increases have been mainly attributable to a general rise in world and domestic prices of raw and manufactured products which in turn have been partly influenced by political and sectional disputes and by current or anticipated future world shortages. Thus the costs of food, drink, equipment, utilities and services have all risen very considerably in recent years. The cost of labour has also increased, in part because of inflation, and in part because of recently imposed employment legislation. In many instances such inflated costs of sales have
not been passed on to consumers, either because of government restrictions on pricing or because of an anticipated natural resistance by consumers to raised selling prices.

In addition, many hotel and catering businesses have been faced with recent legislation or a more rigid enforcement of existing regulations, necessitating expenditure on fire precautions, the working environment for staff, and general hygiene.

Thus most firms in the industry have been affected by a squeeze on profit margins and/or the need for capital expenditure. Many have attempted to rectify the situation by reducing their operational costs, by maximizing the use of their existing resources, or by increasing sales.

11.32 Changes in Catering Techniques

Partly in an effort to reduce labour and (in some cases) food costs, partly as a result of technical innovation, and partly because of changing consumer requirements, there has been a trend amongst caterers to use new products and new techniques. Some of these new products, such as new proteins, have recently been introduced as a means of reducing food costs and of extending the limited world supply of nutrients. In the main, however, the major trend has been for caterers to use convenience foods to an increasing extent as a method of substantially lowering their labour costs and overcoming shortages of preparatory or cooking skills. Such convenience foods encompass three main types of products: simple food items that have been processed and require little preparation and finishing (such as frozen fruit and vegetables); composite dishes or products that have been prepared by the supplier (such as frozen entrees or desserts, or dehydrated sauce mixes); and pre-prepared foodstuffs (such as peeled potatoes or portioned fresh meat).

The use of the first two types of convenience food has further been encouraged by advances in catering equipment, which in particular, have made possible the speedy regeneration of frozen or chilled dishes. Improved design, reliability and
versatility of such cooking and finishing equipment as microwave ovens, forced-air convection ovens and pressure cookers for steaming or frying, have made a considerable impact on caterers, as have new methods of cooking and storage, such as cook/freeze and cook/chill systems, made upon suppliers and those caterers themselves undertaking large scale preparation and storage of foodstuffs.

The net effect of these new products, techniques and equipment has been a trend towards the separation of production from food service, either geographically by using commissaries and subsequent distribution, or temporally by undertaking on-site batch cooking and storage for later use. They have also resulted in a greater standardization and specialization of menu items.

11.33 Deterrents to the Construction of New Hotels.

Since the Hotel Development Incentives Scheme which, by creating favourable financial conditions, encouraged considerable expansion to the existing hotel stock, there has been very little new hotel construction in this country. This is attributable to various factors including substantially increased costs of building materials and labour, the high cost of land, an institutional reluctance to provide capital at normal rates, and (in many areas) a limited availability of suitable sites. Planning restrictions and requirements by local authorities, particularly the requirement for extensive car parking facilities to accompany any hotel development, have made impracticable the construction of new hotels in most town centres or city areas.

To counter the problem of building costs there has been a tendency (in line with general trends) for hotel building to be on a systems basis, and for a greater use of pre-fabricated units such as bedrooms and bathrooms. There has also been a move in motels and some hotels to reduce costs and the overall space requirement by minimizing public rooms, and by eliminating the 'frills' normally associated with accommodation of the particular market level at which they are aiming.
11.34 Enlightened Business Practice
There has been a trend for those involved in hotel and catering activities to hire, seek or develop professional expertise for specialist functions of their businesses. This has stemmed from their need to reduce operational costs, to maximize the utilisation of their resources and to boost sales. The enlightened business practices of the market leaders, and the demonstrated benefits gained from their use, has also been of influence.

The larger groups have been able to afford their own specialist advisors, specialized departments (such as marketing or purchasing) and special equipment (such as, in the case of hotel companies, reservation systems, and access to computers). Smaller groups or individuals have not been able to do likewise, and there has thus been a trend towards group co-operation amongst such businesses, and towards the creation of links for specific purposes. A number of marketing consortia have been established, some also offering purchasing and advisory services to members. Some hoteliers have formed sales and referral links with larger companies or representative sales groups.

11.35 Applicability of Franchising
The trends which have been outlined suggest that there is an increasing vulnerability of individuals and small companies to pressures on their profitability, and a greater awareness of the need to achieve economies, to maximize the use of resources and to turn to specialist expertise. As franchising offers to individuals the economies of scale and specialist advice and assistance normally only available to much larger businesses, it is, in this respect, a suitable alternative to the forms of group co-operation mentioned above. In addition the proven nature of the concept and product offered by a good franchise system, and the support provided by the franchisor, suggest the greater likelihood of success in the face of adverse economic conditions.
The moves towards the separation of production from food service, by the use of new catering products, techniques and equipment also provides a suitable environment for franchising. Being particularly applicable to activities where the component tasks may be readily described and taught to those with few or no directly relevant prior skills, franchising lends itself to a situation where there is a reduction at service outlets of on-site catering skills. Trends in the industry towards standardization and specialization are similarly compatible with the nature of franchising.

Franchising also seems to be an applicable method for those encountering the above-mentioned problems of hotel building. The provision by a franchisor of a 'blue-print' for construction and implementation is likely to reduce time (and thus costs) of implementation. The standardized nature of franchising systems is particularly, though not exclusively, applicable to hotels where there is a standardized environment (i.e. building and contents) such as is more likely to result from the new constructional techniques.
CHAPTER 12

SUGGESTED GROWTH AND DEVELOPMENT OF FRANCHISING
AND ITS IMPLICATIONS

12.1 INTRODUCTION

12.2 POSSIBLE DETERRENT OR STIMULATING FACTORS AND ASSESSMENT OF THEIR IMPACT

12.3 GROWTH OF FRANCHISING WITHIN SECTORS OF THE HOTEL AND CATERING INDUSTRY

12.31 Restaurants, Cafes, Snack Bars and 'Take-Away' Outlets

12.32 Hotels and Other Residential Establishments

12.33 Other Hotel, Catering and Associated Activities

12.4 IMPLICATIONS FOR THE INDUSTRY, ITS SUPPLIERS AND CONSUMERS

12.5 SUGGESTED FURTHER RESEARCH
12.1 A detailed forecast of the growth and development of franchising is precluded by the lack of current official statistics and general paucity of information on franchising in Britain, and by the potential effect of several variables which defy accurate prediction. However, based upon the findings of this study, a number of suggestions are made indicating broad trends and implications for those engaged in the hotel and catering industry and for its suppliers and consumers.

In the previous two chapters it has been proposed that franchising offers net advantages over and above its disadvantages to the franchisor, franchisee, consumer and to the general public interest, and that it is an applicable business method in the context of current economic and social trends. However, the growth and development of franchising is dependent upon three important factors: continuing legal approbation of the method; public acceptance of the concept and consequent supply of suitable franchisees and of development funds; and the availability of suitable sites for expansion.

12.2 POSSIBLE DETERRENT OR STIMULATING FACTORS AND ASSESSMENT OF THEIR IMPACT

A vital issue affecting the growth or decline of franchising is the, as yet, unclarified legal attitude to the trading restrictions inherent in such arrangements (1). Should the recently implemented Restrictive Trade Practices (Services) Order be interpreted so that restrictions imposed by one party upon another were seen not to stem directly from the granting of the franchise, and thus be proclaimed illegal, such an interpretation would fundamentally affect the existence of franchising in this country. It is anticipated that with an increasing understanding of the concept resulting from a more balanced treatment of the subject by academics and observers, and from
the establishment of a soundly-based trade association of franchisors (2), an interpretation of the Order will not be detrimental to those franchise systems whose agreements contain only such restrictions as are necessary to protect their trademark and brand image, and thus the consumer.

A second important factor affecting the growth of franchising in this country is the degree of public acceptance of the concept, and the extent to which recent, more informed exposure of the nature and ramifications of properly-implemented franchise systems can overcome the previously, widely-held public attitude of mistrust of the method. It is suggested that the recent formation of the British Franchise Association, and more favourable comments on franchising in the British press (3) are likely to have a gradual snowballing effect on public opinion, resulting in a growing number of applicants wishing to become franchisees in a wide range of businesses, including hotel and catering activities and a greater availability of funds, both to franchisees and franchisors, from institutional lenders cognizant of the true nature of franchising.

An insufficiency of suitable sites for the development of franchised units has been proposed as a potential deterrent to the growth of franchising in this country (4). Whilst this may be true to some extent for certain types of business activity (such as hotels) or for systems requiring the satisfaction of particular conditions (such as restaurants aiming at trunk road traffic, or fish and chip shops - for which a special permit is required for the premises from local planning authorities), it is not thought to be a more widely applicable deterrent. In any case it ignores the possibility of 'empirical franchising' (5), that is taking over, for example, existing hotels, roadside restaurants or fish and chip shops, and moulding them to the image of the given franchise system.
A factor likely to stimulate the growth of franchising in Britain is the increased use of this business method in other countries with which close trading or cultural ties exist. The spectacular growth in the use of franchising per se and in the number and type of franchise systems in the U.S.A. and an increase in franchising in Western Europe (6) is expected to lead to a greater awareness by British businessmen and British consumers of its potential significance and overall advantages. In addition, the evident interest shown by some well-known foreign companies with extensive interests, in entering the British market as franchisors, is likely to draw increasing attention to the business method and to lead to greater competition between franchised and non-franchised systems in this country, as well as between franchised systems.

Taking into account the foregoing factors, it is suggested that franchising will grow significantly, in this country, both in business sectors where it is already prevalent and in new areas. However it is thought unlikely that it will attain a size and importance comparable to that achieved in the U.S.A., due to the generally conservative attitude in this country to franchising, arising from instances of unfortunate previous British and American experience, and to differences in fiscal policies between the two countries. Furthermore it is suggested that there is an important difference in the entrepreneurial attitudes of the inhabitants of the two countries: Americans tending to esteem highly the 'little man making good' and to value material acquisition
attained by the expenditure of personal energy, whilst there is a tendency in Britain to esteem more highly successes of a non-entrepreneurial nature and to regard with more respect the acquisition of resources which have not been gained through physical labour.

12.3 GROWTH OF FRANCHISING WITHIN SECTORS OF THE HOTEL AND CATERING INDUSTRY

Whilst franchising is at present restricted almost entirely to the fast food sector of the industry, its potential applicability to other market segments and to other business sectors of the industry must be considered. A brief outline follows of the suggested development of franchising within different types of hotel and catering activity and of its implications.

12.31 Restaurants, Cafes, Snack Bars and 'Take-Away' Outlets

Franchising is already an established method within the fast food sector, although in only a handful of systems is it used to any extent. It is predominantly established in outlets selling hamburgers, fried chicken, ice cream and in restaurants with restricted menus centring on grilled or griddled items.

Mention has previously been made of the expansionary plans of existing fast food franchisors, and of the recent arrival in this country of foreign franchisors of considerable significance, whose development of franchised outlets is likely to be extensive once they have tested the British market. In addition it is suggested that the generally increased use of franchising in Britain, and its demonstrated advantages, is likely to influence existing non-franchised companies to use franchising as an alternative method of expansion or diversification; and is also likely to stimulate the implementation of new systems using franchising as the exclusive or main means of development.
Bearing in mind the very wide variety of menus in American fast food restaurants which have been successfully franchised, and also taking into account the slightly less catholic taste of the British public, it is suggested that franchising in this country may be successfully used in the following types of restaurants, though the potential viability of franchising in each system is obviously a matter for detailed consideration in the given circumstances (7): restaurants or 'take-away' units selling pasta dishes including pizza, spaghetti etc., fish and chips, pancakes, 'health food', vegetarian or delicatessen dishes, casseroles and other 'country' fare, sandwiches and snacks, pastry and bakery products, Indian, Chinese and other 'ethnic' foods with fast food characteristics.

In addition it is contended that franchising is a method that may be used in restaurants not included in the fast food definition i.e. those offering a more leisurely environment and service and selling more expensive food, such restaurants at present sometimes being let on a concessionary basis to specialist operators. Providing that high standards of service, product and environment are defined and monitored within an overall framework of the system's image, it is suggested that franchising may be used in the more expensive 'ethnic' restaurants offering food, with or without entertainment, of a special national character and in restaurants selling steak, seafood etc.

12.32 Hotels and Other Residential Establishments
As yet franchising has made almost no impact upon this sector. The few hotels in Britain which were examined in this survey had, with two exceptions, more than one hundred rooms and offered accommodation of a relatively expensive type; no existing franchised hotels could be traced which were of relatively small dimensions and which aimed at the lower end of the accommodation market. Of those hotels which were franchised, only one was owned by a single franchisee (the others being the property of a multiple franchisee or operated by incentive managers), and this sole example has recently ceased to be the subject of a franchise agreement and instead is now under management contract.
It is suggested that no significant growth is likely in the numbers of franchised, newly-built hotels aiming at the medium to top end of the market. Difficulties in finding suitable sites for construction, together with unfavourable tax treatment (in comparison with that existing in the U.S.A. during the rapid expansion of hotel franchising) point to a lack of development of such hotels (whether franchised or not). The alternatives to franchising (such as joining a consortium, sales agency or hiring a management contractor) combined with the existing attitude to, and lack of experience of franchising in the hotel sector, further suggest that those hotels which are developed are unlikely to include a significant number under franchise.

However, there appears to be potential for the implementation of franchise systems amongst existing hotels which require marketing, managerial and purchasing advice and assistance, whose needs cannot be met by consortia or management contractors, and which conform (or can be altered to conform) to the standards and image of the intending franchisor. One large hotel company has developed a franchise policy for such hotels with more than fifty bedrooms, thereby hoping to augment its wholly-owned and managed hotel interests to achieve a more balanced pattern of distribution, whilst avoiding capital expenditure.

Another large company with hotel interests similarly considered to be feasible, and initiated, the establishment of a franchise system of guest houses, altered from existing, going concerns. This policy was terminated because of external factors unrelated to the project itself, and it is suggested that there remains an opportunity for implementing a similar scheme in relation to guest houses or relatively small hotels.

The economics of operating costly, newly built hotels which offer a traditional range of services etc, have been proposed as one reason for the lack of growth of franchising in such outlets. But it is suggested that there is an opportunity for the implementation of franchise systems of newly-constructed economy-class hotels with limited services, or of hostels or self-catering accommodation, aimed for instance at the younger sections of the population (8).
Other Hotel, Catering and Associated Activities

Predictions about the development of franchising in other sectors of the industry or in other related activities can only be a matter of conjecture, there being no current evidence of any franchising (as defined in this study) within public houses, clubs or contract catering. Such development seems unlikely where similar, alternative contractual arrangements exist, as in public houses and contract catering, though one author has suggested that these sectors offer an opportunity for franchising (.9). The essential standardization of franchising also seems inapplicable to the type of club which offers to members a highly individual total product of food, drink, accommodation (in some cases), service and environment. However, there may be potential for franchised systems in 'Working Mens' Clubs' or those offering to members entertainment and catering facilities of a more standardized nature.

Similarly, the development of franchising within other areas of hotel and catering activity, such as banqueting and conference management, is open to speculation. In the U.S.A. there are a large number of franchise systems which do not involve ownership by the franchisee of the premises where the service is performed, but which require him to own special equipment and to use the franchisor's specialized systems for the provision of services. This form of franchising activity could be applicable to banqueting, catering for special functions, or conference management. Such a system would include provision by the franchisor of training to franchisees, a 'blue-print' for different occasions of operational requirements and inventory, and purchasing and marketing assistance. There has been a slight indication that hoteliers wish to hire, and others are willing to provide, expertise in such matters (10), though not on a franchised basis.
12.4 MAIN IMPLICATIONS FOR THE INDUSTRY, ITS SUPPLIERS AND CONSUMERS

The difficulty of making any precise forecast of the growth of franchising in hotel and catering activities precludes other than a broad indication being given of its likely impact on manpower within the industry, on its suppliers of goods, or of its potential, competitiveness for available sites, development capital and consumers' disposable income.

It is suggested that within the next decade there is unlikely to be overall growth in the number of hotel and catering outlets, although changes in demand will cause growth in some market sectors or locations and decline in others. The expected increase in franchised outlets and systems will therefore occur at the expense of non-franchised units and systems, and will lead to an increased proportion of hotel and catering outlets being of a standardized nature.

Reference has already been made to the likelihood that franchising brings about the more efficient use of resources, including labour. Whilst this is likely to reduce the overall number of those employed in the industry, a compensating trend is that franchised outlets tend to cater for a larger volume of trade than those which they replace. Thus no significant change is envisaged in the overall number of people employed in hotel and catering activities. However, because franchising is particularly applicable to fast food operation requiring easily-learned preparation, production and serving techniques, it is suggested that there will be a reduction in the proportion of highly skilled workers in the industry. At the same time, the training programmes of franchisors will raise the basic levels of skills and knowledge of those employees, formerly designated as unskilled or semi-skilled.

Whilst franchising is thought likely to appeal to a wide range of individuals within (and outside) the industry, employed in an operational and managerial capacity, it is suggested that it may have particular appeal to junior and middle management at a time when governmental and other forces are affecting their job satisfaction.
Resulting from an increased proportion of those working within the industry being either franchisees or franchisees' employees, it is further suggested that there is likely to be a reduction in the general level of staff turnover, due to the financial and personal commitment of the former, and their likely treatment of the latter.

Though unlikely to alter radically the existing heterogeneous demand by thousands of individual establishments for a very wide range of products from many different suppliers, an increase in the number and size of franchise systems will create more companies with substantial purchasing leverage, and with closely defined requirements for consumables and non-consumables, and possibly with a need for a national or widespread distributional competency on the part of selected suppliers. A number of franchisors are likely to establish their own channels of supply for most or some products, through creation of new, or backward integration with existing manufacturers and suppliers. Suppliers are therefore likely to be affected by competition with other suppliers to secure contracts with franchise companies, or by competition created by such companies in their role as manufacturers or suppliers.

Growth in the number of franchised outlets and systems is likely to create pressures on the property market and to increase the value of available, suitable sites or premises, thus affecting non-franchised outlets desiring to establish themselves. Similarly, an increase in franchising could affect the allocation of development funds, and by dint of an established reputation of franchised systems, may secure finance which would otherwise have been allocated to non-franchised systems.

Whilst the development of franchised units will be at the expense of existing, individually-owned outlets, these will be, in the main, outlets which are inefficient or which have not kept pace with changes in consumer demands. An increase in franchising does not herald an era of complete standardization and lack of choice. It is suggested that efficient, individualized outlets will still retain a place in the market as a contrast to such units, and that the lack of choice
will be to some extent offset by an increase in the number of franchise systems offering diverse products and environmental themes.

Growth in the number of franchised outlets is likely to lead to a greater sales volume and turnover in real terms, and a larger proportion of consumer disposable income expended within the industry, due to the likely larger size of franchised outlets (than those they replace), and to the generally more extensive marketing practices and more aggressive selling techniques of franchisors than independent businessmen, and to changes in life-style of the population resulting in a move towards the more frequent use of such outlets.

12.5 SUGGESTED FURTHER RESEARCH
Throughout this study reference has been made to the lack of published information on the contractual arrangements examined, particularly in respect of franchising and hotel management contracts. Hence there is wide scope for a variety of studies to provide greater understanding of certain aspects, to suggest optimal ways of organizing resources and to provide clearer indications of the present significance and potential growth of such arrangements of British and foreign companies in this country and of British companies overseas. Some specific avenues for further research are suggested below.

An important area requiring further clarification is the definition of the demographic, financial and behavioural characteristics of franchisees, and the operating and financial characteristics of franchisors, which give rise to an optimal performance within franchisees' units and within the system as a whole. A further examination is needed of the contribution made by multiple franchisees, to establish whether they bring overall benefits or disbenefits to a franchise system.

There is a need to determine typical life-cycles both of the systems themselves and of the relationships between franchisor and franchisees, and to suggest how best to accommodate patterns of growth, maturity, decline and re-generation.
A number of the advantages and disadvantages of franchising that have been suggested in this study in relation to the national economy, consumers and participants in franchising, need to be tested on a wide scale and over a substantial time-span, so that such an assessment can be backed by empirical findings.

An investigation is also needed to clarify the short, medium and long-term effect on both parties of the different methods of remuneration and, in the case of hotel management contracts, of the precise ramifications of different fee structures in given circumstances.
Appendix A

Main Periodicals and Newspapers Consulted in Survey

Business Ideas Letters (privately circulated)
Caterer and Hotelkeeper
Catering Times
Cornell Hotel and Restaurant Administration Quarterly
European Journal of Marketing
Fast Food
Financial Times
Harvard Business Review
HCIMA Journal
HCIMA Review
Hospitality
Industrial and Welfare Catering
International Journal of Physical Distribution
Institutions/Volume Feeding
Journal of Marketing
Journal of Retailing
Journal of Small Business Management
Management Today
Marketing
Retail and Distribution Management
Service World International
Sunday Times
Times
Appendix B

Companies Requested for Company Reports and Accounts

Adda International Limited
Allied Hotels, Scotland (Aberdeen Hotel Co. Ltd.)
Bass Charrington Ltd.
British Transport Hotels
C. G. (Hotels)
Centre Hotels (Cranston) Ltd.
Courage Ltd.
Cunard Hotels Ltd.
De Vere Hotels and Restaurants Ltd.
BMI Ltd.
Grand Metropolitan Ltd.
Greenall Whitley and Co. Ltd.
Hallway Hotels Overseas Ltd.
Imperial London Hotels Ltd.
Ladbroke Group
Leisure and General Holdings Ltd.
Lex Hotels Ltd.
J. Lyons and Co. Ltd.
Mount Charlotte Investments Ltd.
Myddleton Hotels Ltd.
Norfolk Capital Hotels Ltd.
North British Trust Hotels Ltd.
M. F. North Ltd.
Queens Moat Houses Ltd.
Rank Organization
Rowton Hotels Ltd.
Saxon Inns Motor Hotels Ltd.
Scottish and Newcastle Breweries Ltd.
Scottish Highland Hotels
Reo Stakis Organization Ltd.
Trust Houses Forte Ltd.
Vaux Breweries Ltd.
Whitbread and Co. Ltd.
S & M Winton Group
Appendix C

'Informed' Individuals Consulted During Survey excluding those participating in the four types of contractual arrangement.

<table>
<thead>
<tr>
<th>Name</th>
<th>Designation/Organization</th>
</tr>
</thead>
<tbody>
<tr>
<td>P. Bertram</td>
<td>Partner, Cornwell, Greene, Bertram, Smith</td>
</tr>
<tr>
<td>G. Campbell-Smith</td>
<td>Consultant, Service Development and Operations Ltd.</td>
</tr>
<tr>
<td>D. Chow</td>
<td>Consultant, Nielsen Consultants Ltd.</td>
</tr>
<tr>
<td>R. Coombes</td>
<td>British Home Stores</td>
</tr>
<tr>
<td>* I. Cooper</td>
<td>Druce and Co., Property Agents</td>
</tr>
<tr>
<td>* P. Copp</td>
<td>Director, Horwath and Horwath (UK) Ltd.</td>
</tr>
<tr>
<td>R. Cornwell</td>
<td>Partner, Cornwell, Greene, Bertram, Smith</td>
</tr>
<tr>
<td>E. Davies</td>
<td>Director, Horwath and Horwath (UK) Ltd.</td>
</tr>
<tr>
<td>* Mr. Delap</td>
<td>Office of Fair Trading, London</td>
</tr>
<tr>
<td>R. Doswell</td>
<td>International Labour Office</td>
</tr>
<tr>
<td>* R. H. Down</td>
<td>Catering Advisor and Inspector, British Airports Authority</td>
</tr>
<tr>
<td>* Col. Dumas</td>
<td>Cork, Gulley, property agents</td>
</tr>
<tr>
<td>* M. S. Fielding</td>
<td>Department of Transport, Motorway Service Areas</td>
</tr>
<tr>
<td>R. Fraser</td>
<td>Director, Richard Ellis property agents</td>
</tr>
<tr>
<td>J. Fuller</td>
<td>Head of Department of Catering and Hotel Management, Oxford Polytechnic</td>
</tr>
<tr>
<td>H. Guest</td>
<td>Head of Civil Service Catering Organization (CISCO).</td>
</tr>
<tr>
<td>* A. K. T. Hopper</td>
<td>Director, Pannell, Kerr, Forster</td>
</tr>
<tr>
<td>M. Mendelschn</td>
<td>Solicitor</td>
</tr>
<tr>
<td>* J. Nairn</td>
<td>Christie and Co., property agents</td>
</tr>
<tr>
<td>G. Parkinson</td>
<td>Director, Horwath and Hörwath (UK) Ltd.</td>
</tr>
<tr>
<td>M. Quest</td>
<td>Editor, Catering Times</td>
</tr>
<tr>
<td>* W. G. Richards</td>
<td>English Tourist Board</td>
</tr>
<tr>
<td>P. Smith</td>
<td>Industrial and Commercial Finance Corporation Ltd (ICFC)</td>
</tr>
<tr>
<td>S. Spiegel</td>
<td>Lecturer, Middlesex Polytechnic</td>
</tr>
<tr>
<td>J. Stanworth</td>
<td>Senior Lecturer, Central Polytechnic of London</td>
</tr>
<tr>
<td>A. Sutton</td>
<td>Features Editor, Caterer and Hotelkeeper</td>
</tr>
<tr>
<td>R. J. Wood</td>
<td>Operations Director, Associated Restaurants Ltd.</td>
</tr>
<tr>
<td>M. Woodmansey</td>
<td>Research Fellow, Central Polytechnic of London</td>
</tr>
</tbody>
</table>

Note: Interviews were personally conducted on a face-to-face basis, except those marked thus *, which were carried out during a lengthy telephone conversation.
Appendix C /cont'd...

List of Respondents Interviewed During Survey
ie: Those Engaged in Contractual Arrangements

### Catering Contractors

<table>
<thead>
<tr>
<th>Name of Company</th>
<th>Respondent, Designation</th>
</tr>
</thead>
<tbody>
<tr>
<td>ARA Services, Feltham, Middlesex</td>
<td>P. Thornton, President (Europe)</td>
</tr>
<tr>
<td>Bateman Catering Organization Ltd. London</td>
<td>R. P. Lichtensteiger, Managing Director</td>
</tr>
<tr>
<td>Grandmet International Site Services London</td>
<td>G. Lewis, Chief Executive</td>
</tr>
<tr>
<td>Four Square Catering and Vending Slough, Bucks.</td>
<td>C. Milne, Catering Product Manager</td>
</tr>
<tr>
<td>Gardner Merchant Food Services Ltd. Croydon, Surrey</td>
<td>L. Totman, Director of Administration</td>
</tr>
<tr>
<td>Midland Catering Ltd., Birmingham</td>
<td>A. W. Walford, Managing Director</td>
</tr>
<tr>
<td>Rebate Services (Catering Centres) Ltd. Leicester</td>
<td>A. Moore, Director and General Manager</td>
</tr>
<tr>
<td>Stuart Cabeldu Catering Ltd. London</td>
<td>H. Potter, General Manager, Commercial</td>
</tr>
<tr>
<td>Sutcliffe Catering Group Ltd. London</td>
<td>J. K. R. Graveney, Chief Executive</td>
</tr>
<tr>
<td>Taylorplan Catering Richmond, Surrey</td>
<td>R. Powell, Regional Controller</td>
</tr>
<tr>
<td>Three Counties Catering Co. Ltd. Sutton Coldfield, West Midlands</td>
<td>R. D. Creek, Director</td>
</tr>
</tbody>
</table>

### Clients of Catering Contractors

<table>
<thead>
<tr>
<th>Name of Company</th>
<th>Respondent, Designation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Automobile Association Basingstoke, Hants</td>
<td>G. K. Yeates, Catering Co-ordinator</td>
</tr>
<tr>
<td>Canterbury College of Technology Kent</td>
<td>F. Howitt, Principal</td>
</tr>
<tr>
<td>Chrysler (UK) Ltd. Coventry</td>
<td>W. Muir, Company Employee Services Manager</td>
</tr>
<tr>
<td>Dennis Motors Ltd. Guildford, Surrey</td>
<td>D. Watt, Mrs. Personnel and Training Officer</td>
</tr>
<tr>
<td>English Abrasives Ltd. London</td>
<td>K. R. Dagg, Assistant Company Secretary</td>
</tr>
<tr>
<td>Equity and Law Life Assurance, London</td>
<td>D. Whittingham, Assistant Secretary</td>
</tr>
</tbody>
</table>
### Name of Company
- Fiat (England) Ltd.
- Brentford, Middlesex
- Harrods Ltd.
- London
- IBM
- Cosham, Portsmouth
- Ilford Films Ltd.
- Brentwood, Essex
- Independent Television News
- London
- International Computers Ltd.
- London
- Lesney Products
- London
- Rapid Metal Developments
- Birmingham
- Roussel Laboratories Ltd.
- Wembley, Middlesex
- Sun Alliance Insurance Group
- London
- Wickman Ltd.
- Coventry
- Arnold E. Williams
- Birmingham

### Hotel Management Contractors

<table>
<thead>
<tr>
<th>Name of Company</th>
<th>Respondent, Designation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Brent Walker Ltd.</td>
<td>N. Byrne</td>
</tr>
<tr>
<td>London</td>
<td>Construction Director</td>
</tr>
<tr>
<td>Commonwealth Holiday Inns of Canada, London</td>
<td>E. J. Rieck</td>
</tr>
<tr>
<td>European Hotel Corporation (UK) Ltd. Ascot, Berks</td>
<td>General Manager, European Operations</td>
</tr>
<tr>
<td>Grand Metropolitan Ltd.</td>
<td>M. Brooker</td>
</tr>
<tr>
<td>London</td>
<td>Development Director</td>
</tr>
<tr>
<td>Hallway Hotels Overseas Ltd., London</td>
<td>G. Lewis</td>
</tr>
<tr>
<td>Hilton International</td>
<td>Chief Executive, Industrial and Hotel Division</td>
</tr>
<tr>
<td>London</td>
<td>W. A. Lipscombe</td>
</tr>
<tr>
<td>Hotel Management International</td>
<td>General Manager</td>
</tr>
<tr>
<td>Longford, Middlesex</td>
<td>L. G. Blouet</td>
</tr>
<tr>
<td>Intercontinental Hotels (UK) Ltd.</td>
<td>Division Director, U.K.</td>
</tr>
<tr>
<td>London</td>
<td>P. W. Van der Vlieet, Resident Manager</td>
</tr>
<tr>
<td></td>
<td>P. Phillips</td>
</tr>
<tr>
<td></td>
<td>Managing Director</td>
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<tr>
<td></td>
<td>G. Jeffrey</td>
</tr>
<tr>
<td></td>
<td>General Manager</td>
</tr>
</tbody>
</table>
Name of Company
Landmark International Hotels Ltd.
London
Norfolk Capital Hotels,
London
* Novotel (UK) Ltd.,
Radlett, Herts
Pendennis Hotels Ltd.,
Saundersfoot, Pembrokeshire
Trust Houses Forte Ltd.

Respondent, Designation
J. Skinner, Chairman
R. G. Hainsworth, Managing Director
D. James
Managing Director
P. Charles
General Manager, potential contractor
I. Bell
Chairman
R. Forte, Director of Personnel
J. Logie, Assistant Managing Director,
International Hotels Division

Clients of Hotel Management Contractors
Name of Company
Blackpool Borough Council
Blackpool
European Hotel Corporation (UK) Ltd.
Ascot, Berks
Holiday Inns U.K. Inc.
Harlington, Hayes.
Houlder Bros.
London
Ladbroke Dragonara Hotels
London
Lex Hotels Ltd.
London
Morgan Grenfell Finance Ltd.
London
Philip and Son Ltd.
Dartmouth, Devon
Saxon Inns Motor Hotels Ltd.
London
Westmoreland Investments Ltd.,
London

Respondent, Designation
D. Wardman, Treasurer
M. Brooker
Development Director
J. Corson
Deputy Managing Director
C. Dodge, Director
D. Barnett, Operations Director
(former client)
P. Makin, Divisional Director
D. Keys, Director
P. Pensabene
Chairman
J. W. Maddern
Director
B. Davies
Finance Director
Breweries

Name of Company

Ind Coope Ltd.,
London

Bass Marketing Services Ltd.,
Burton-on-Trent

Charrington and Co. Ltd.,
London

Courage Eastern Ltd.,
London

Greenall Whitley and Co. Ltd.,
Warrington

Mansfield Brewery Co. Ltd.,
Mansfield

Newcastle Breweries
Newcastle

Daniel Thwaites and Co. Ltd.,
Blackburn

Truman Taverns
Grand Metropolitan Ltd. London

Vaux Breweries Ltd.,
Sunderland

Chef and Brewer,
Grand Metropolitan Ltd., London

Whitbread (London)
London

Respondent, Designation

G.T.R. Hayter,
Regional Estate Manager

W. A. Mason, Licensed House
Director

R. Smith, Licensed House Advisor

R. Stewart, Divisional Sales
Director, Central Region

N. White, Senior Retail Trade
Director

L. Prescott, Group Licensee
Selection Manager

R. Chadburn, Chairman

R. Umbers, Director of Sales

N. Thompson, Tenancy Manager

J. Steven, Assistant Tenancy Manager

Mr. Cronshaw, Tied Trade Manager
Mr. Stevens, Senior Tied Trade
Representative

A. Christie, District Sales
Manager

I. Alderson, General Manager
Tied Trade

M. J. Wallace, Regional Director,
Watney Innkeepers South

M. Tabor, Tenanted Trade Director

Tenants

C. Belcher
J. J. Brincat-Smith
P. Brooks
F. H. Colbridge
M. Connelly
A. Finch
J. Goodfellow
D. Hawkes
L. Heath
R. E. Jackson-Cox
W. Jefferies
J. Keeton
T. F. Lowther
P. O'Connor, Mrs.

Bookham, Surrey

Preston, Lancs

Derby

Lowestoft, Norfolk

London (South)

Tarbock, Nr. Liverpool

Wide Open, Nr. Newcastle

Middlesborough

London (South)

Bromsgrove, West Midlands

Hove, Sussex

Newbold, Cheshire

Silksworth, Nr. Sunderland

London (North)
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<th>Franchisors</th>
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<tr>
<td>F. S. Patterson</td>
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<td>P. J. Pescod</td>
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<td>W. H. Piper</td>
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<td>T. G. Pritchard</td>
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<td>G. J. Salmon</td>
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<td>L. Saunders</td>
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<td>H. A. Short</td>
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<td>P. Spavin</td>
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<td>J. Thompson</td>
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<td>A. Woodward</td>
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<tr>
<td>Ferry Hill, Co. Durham</td>
<td>J. Selzer, Ms. Operations Manager</td>
<td></td>
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<td>Lewes, Sussex</td>
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<tr>
<td>Wednesbury, West Midlands</td>
<td>N. I. Mandell Franchising Director</td>
<td></td>
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<tr>
<td>St. Paul’s Cray, Kent</td>
<td></td>
<td></td>
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<tr>
<td>Merrow, Surrey</td>
<td></td>
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<tr>
<td>London (North)</td>
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<tr>
<td>Effingham, Surrey</td>
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<tr>
<td>Addlestone, Surrey</td>
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</tr>
<tr>
<td>Cronton, Nr. Liverpool</td>
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<td></td>
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<tr>
<td>Bury, Lancs.</td>
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<tr>
<td>Franchisors</td>
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</tr>
<tr>
<td>J. Lyons and Co. Ltd.</td>
<td>J. Corson Deputy Managing Director</td>
<td></td>
</tr>
<tr>
<td>London (former intending franchisor)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pizza Express,</td>
<td></td>
<td></td>
</tr>
<tr>
<td>London</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Queens Moat Houses Ltd.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Romford, Essex</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sandwich Supermarkets</td>
<td></td>
<td></td>
</tr>
<tr>
<td>London (former franchisor)</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Name of Company
Seafarer Restaurants Ltd.,
Romford, Essex (former franchisor)
TraveLodge International, Inc.,
El Cajon, California,
Trust Houses Forte Ltd.,
London

Name of Company
Wimpy International
London

Respondent, Designation
M. Morton
Managing Director
R. Manfred
President & Chief Executive Officer
R. Forte, Director of Personnel
D. Durban, Director and Group Secretary
M. Reed, Franchise Manager (Hotels)
P. D. Merry, General Manager, Franchise Operations (Popular Catering)
D. Acheson, ex Managing Director
W. Sharman, Director of External Affairs
E. J. Fisher, Marketing Director

Franchisees

<table>
<thead>
<tr>
<th>Name/Organisation</th>
<th>Respondent, Designation (if applicable)</th>
<th>Location of Unit(s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>N. Ali</td>
<td></td>
<td>West London</td>
</tr>
<tr>
<td>P. J. Bannon-Bourke</td>
<td></td>
<td>Epsom, Surrey</td>
</tr>
<tr>
<td>Banquets of Oxford</td>
<td></td>
<td>National</td>
</tr>
<tr>
<td>F. Bolam (sub franchisee)</td>
<td>G. Silver, Managing Director</td>
<td>Dorking, Surrey</td>
</tr>
<tr>
<td>Commonwealth Holiday Inns of Canada</td>
<td>E. J. Rieck General Manager</td>
<td>National</td>
</tr>
<tr>
<td>B. Defriend (management licensee)</td>
<td></td>
<td>Central London</td>
</tr>
<tr>
<td>EMI Hotels &amp; Restaurants Limited</td>
<td></td>
<td>London</td>
</tr>
<tr>
<td>Empire Catering Co. Ltd.</td>
<td></td>
<td>National</td>
</tr>
<tr>
<td>N. Fitzgerald, Ms. (management licensee)</td>
<td></td>
<td>Central London</td>
</tr>
<tr>
<td>L. Frankel</td>
<td></td>
<td>North London</td>
</tr>
<tr>
<td>H. Godfrey</td>
<td></td>
<td>Kingston, Surrey</td>
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<tr>
<td>J. Goulding, Mrs.</td>
<td></td>
<td>Guildford, Surrey</td>
</tr>
<tr>
<td>S. Greene</td>
<td></td>
<td>London</td>
</tr>
<tr>
<td>P. Huguet</td>
<td></td>
<td>West London</td>
</tr>
<tr>
<td>A. V. Jones</td>
<td></td>
<td>Stretton-en-Fosse, Glos.</td>
</tr>
<tr>
<td>Kefco Sales Ltd.</td>
<td>I. B. Trott, Managing Director</td>
<td>Maidenhead, Berks and South East</td>
</tr>
<tr>
<td>Name/Organization</td>
<td>Respondent, Designation</td>
<td>Location of Unit(s)</td>
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</tr>
<tr>
<td>S. Landau</td>
<td></td>
<td>North London</td>
</tr>
<tr>
<td>A. F. Lean</td>
<td></td>
<td>Yeovil, Somerset.</td>
</tr>
<tr>
<td>J. Leckstein</td>
<td></td>
<td>North London</td>
</tr>
<tr>
<td>S. Less</td>
<td></td>
<td>Greater London area</td>
</tr>
<tr>
<td>P. Lewis</td>
<td></td>
<td>Reading, Berks</td>
</tr>
<tr>
<td>K. Mackay (management licensee)</td>
<td></td>
<td>Privett, Hants.</td>
</tr>
<tr>
<td>Marsden Caterers</td>
<td>R. Marsden, Company Secretary</td>
<td>Sheffield, Yorks.</td>
</tr>
<tr>
<td>K. Niyazoglu</td>
<td></td>
<td>East London</td>
</tr>
<tr>
<td>Old Kentucky Restaurants</td>
<td>W. Landau, Managing Director</td>
<td>Central London</td>
</tr>
<tr>
<td>P. Palmer (incentive manager)</td>
<td></td>
<td>Ilford Essex</td>
</tr>
<tr>
<td>F. Poole</td>
<td></td>
<td>South East London</td>
</tr>
<tr>
<td>Q. Inns Ltd.</td>
<td>A.H.K. Edwards, Managing Director</td>
<td>Farnham, Surrey and South Coast</td>
</tr>
<tr>
<td>S. Raguz (incentive manager)</td>
<td></td>
<td>Droitwich Spa, Worcs.</td>
</tr>
<tr>
<td>* S. Remp</td>
<td></td>
<td>Aberdeen, Scotland</td>
</tr>
<tr>
<td>J. M. Richardson Mrs.</td>
<td></td>
<td>East Hornden, Essex</td>
</tr>
<tr>
<td>(management licensee)</td>
<td></td>
<td>West London</td>
</tr>
<tr>
<td>A. Rocca, Mrs. (prospective franchisee)</td>
<td></td>
<td>Ross on Wye, Herefordshire</td>
</tr>
<tr>
<td>P. Rynehart (incentive manager)</td>
<td></td>
<td>West London</td>
</tr>
<tr>
<td>D. Secretan (ex franchisee)</td>
<td></td>
<td>Long Melford, Suffolk</td>
</tr>
<tr>
<td>M. Signorini (incentive manager)</td>
<td></td>
<td>West London</td>
</tr>
<tr>
<td>R. Silvestri</td>
<td></td>
<td>Glasgow, Scotland</td>
</tr>
<tr>
<td>Reo Stakis (intending franchisee)</td>
<td>J. F. Loughray, Managing Director</td>
<td>North West London</td>
</tr>
<tr>
<td>A. A. Taylor (prospective franchisee)</td>
<td></td>
<td>Edinburgh, Scotland</td>
</tr>
<tr>
<td>United Biscuits Ltd.</td>
<td>I. B. Richardson, Director, Catering Division</td>
<td>Canterbury Kent</td>
</tr>
<tr>
<td>A. Walker</td>
<td>F. Huggins, General Manager</td>
<td>Central London</td>
</tr>
</tbody>
</table>

Note: All interviews were carried out on a face to face basis except those marked thus *, which were conducted during a lengthy telephone conversation.
## Parties Involved in Other Arrangements

<table>
<thead>
<tr>
<th>Name/Organisation</th>
<th>Respondent, Designation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Centrelink Hotels</td>
<td>Giles Jackman, General Manager</td>
</tr>
<tr>
<td>(a marketing and purchasing</td>
<td>Managing Director</td>
</tr>
<tr>
<td>consortium)</td>
<td>(subscriber to Centrelink)</td>
</tr>
<tr>
<td>W. G. Crossman</td>
<td></td>
</tr>
<tr>
<td>The Crown and Mitre Hotel,</td>
<td>Managing Director</td>
</tr>
<tr>
<td>Carlisle, Cumbria.</td>
<td>(subscriber to Centrelink)</td>
</tr>
<tr>
<td>T. E. Harrison</td>
<td></td>
</tr>
<tr>
<td>Palm Court Hotel,</td>
<td>Managing Director</td>
</tr>
<tr>
<td>Torquay, Devon</td>
<td>(subscriber to Centrelink).</td>
</tr>
</tbody>
</table>
APPENDIX D

QUESTIONNAIRE TO CONTRACTORS : HOTEL MANAGEMENT/CATERING

Date of interview
Name of interviewee
Title

Section A: Profile of Contractor

1. Name of company.
2. Public/private.
3. Date of incorporation.
4. Name of system(s) operated.
5. Name of parent company.
6. Name of subsidiary/associated companies.
7. Address of head office/applicable regional office.
8. Registered address.
9. Names of top executives, major shareholders.
10. Main business occupation of contractor.
11. Main business occupation of parent/subsidiary/associated companies.
12. Location of outlets.
13. Total number of outlets within system.
14. Proportion/number of managed/wholly owned and operated/franchised outlets.
15. Brief history of company development (including date of initiation of system(s), date of 1st management/catering contract, maximum number contracts ever held, current number).
16. Anticipated future development (growth in contracts/direct ownership and operation, system or product diversification, changes in market location).
   (a) entire system
   (b) management/catering contracts.
18. Pre-tax profit (loss) for 1974/75 and 1975/76.
   (a) entire system
   (b) management/catering contracts.
19. Number of directly-employed employees.
   (a) in entire system
   (b) in management/catering contracts
   (a) in outlets
   (b) in supporting organisation
21. Revenue attributable to contracts in 1974/75 and 1975/76
Section B: Profile of Clients, Data on Clients' Outlets

22. Number of clients.
23. Business occupation of clients (typical examples, note any pre­
dominant occupation).
24. Location of clients' businesses.
25. Status of clients: (private individuals/public companies/private
companies/institutional lenders etc.).
26. Classification (single or multiple ownership of outlets being
managed).
27. Proportion/number of clients known concurrently to employ other
contractors.
28. Proportion/number of clients known to directly own and operate
similar outlets.
29. Proportion/number of clients' units taken under contract when
already operational/initiated by contractor.
30. Perceived reason for, and expected duration of contract (eg.
planned action of long-term nature/'bridging' device of short­
term nature/'rescue' operation/ad hoc action).
31. Classification of managed units (hotels/employee feeding faci­
lities/other - specify).
32. Type of clients' customers (hotel guests/students/patients/employ­
ees).
33. Geographical location of managed units (overseas/GB/region).
34. Market location (city/suburban/rural/industrial/other).
35. Indication of grading of units (if hotels whether de luxe/1st
class etc; if catering units give an indication of type and qual­
ity of product offered).
36. Size of outlets (number of rooms/potential or actual customers) -
average or range.
37. Hours that outlets are operational.
38. 'Average' length of business relationship with clients.
39. Duration of 'average' contract, outline terms for renewal.

Section C: Contractor's Input to Arrangements

40. Is a feasibility study undertaken/advice given on location of
outlet.
41. Is advice and assistance available on technical matters such as
construction, design, decor, equipment, stock inventory.
42. Is such advice and assistance part of main contract or subject
to a separate arrangement.
43. Is advice and assistance available on systems and procedures,
standards, operational and financial control.
44. Is an operating manual provided.
45. Are staff recruited and trained by contractor. To what levels
does this apply (senior/middle management/supervisors/other
employees).
46. How long in advance of opening the outlet are such staff installed.
47. Do you consider that the staff employed by you are of significantly better calibre than those whom your client could directly employ.
48. How are you reimbursed for staff selection and training.
49. What pre-opening support is offered (training/sales promotion/advertising etc.). For how long does this last.
50. How are you reimbursed for the above support.
51. Are visits made by your representative(s) to clients' outlets (how frequently, by whom, for what purpose).
52. What is the span of control of such representatives.
53. Is information offered to clients on operating and financial norms of such outlets.
54. Do you normally/ever make a financial investment in your clients' outlets. If yes, is this investment in fixed assets/working capital, and what is the normal extent of such investment.
55. Indicate the extent, frequency and mode of financial reporting by you to your clients.
56. What marketing support is offered to clients (market research/advertising/sales promotion/reservation system etc.).
57. How are you reimbursed for this.
58. Are clients' outlets normally branded in the name of your system (indicate whether there is general recognition by guests/customers/employees of the outlets' managed status).
59. Is advice and assistance available on purchasing requirements, sources of supply.
60. Do you normally undertake the role of supplier of such commodities. Outline type of commodity supplied, and indicate whether other purchases must be obtained through suppliers nominated by you.
61. How are you reimbursed for this (is a discount credited by your suppliers/wholesalers/retailers, and is this retained by you in total or part).

Section D: Client's Input to Arrangement

62. Indicate the type and range of fee structures agreed between you and your clients. Give a detailed breakdown of the most common arrangements (establish precisely what payments are included and what excluded from calculations).
63. Do clients normally make any other payments to you. If so, what are they.
64. What is the arrangement regarding timing of such payments.
65. To what extent are your clients exposed to financial risk (or subsidies).
66. Do your clients normally themselves locate suitable land/property etc.
67. Do your clients normally provide/have title to land, buildings, fixtures and fittings, equipment, stock, working capital.
68. What other resources do clients normally provide (e.g. lighting, heating, drainage, telephones, lifts, water).
69. Are employees usually employed in the name of the client or of the contractor.
Section E: Imposed Controls

70. Who determines operating policies and standards of performance. What is the limit of your authority in this respect.

71. Who sets budgets, operating costs and selling prices. What is the limit of your authority in this respect.

72. How do your clients monitor your performance.

73. Do clients have right of access to the managed outlet, to its books of account, and to the relevant records within your head/regional office.

74. To what extent do clients come in contact with the unit manager. do they seek to intervene between you and the manager.

75. Do you stipulate that clients must purchase supplies from you/nominated/approved suppliers. Does the unit manager retain any purchasing discretion.

76. What arrangement is made for the replacement and renewal of fixtures and fittings, furniture, equipment, and for redecoration of the units.

77. Indicate the arrangements normally made in respect of insurance; (establish whether client or contractor is responsible for named categories of cover).

78. Is it normally the responsibility of your clients to ensure compliance with local regulations and laws.

79. What arrangements are made for arbitration.

80. Do you have first option to purchase the unit, fixtures and fittings etc.

Section F: Operating Data on Managed Units

81. Give an indication of the 'average' or range of the number of staff employed in the managed units.

82. What is the 'average' or range of gross turnover per managed unit in 1974/75 and 1975/76.

83. What is the 'average' or range of pre-tax profit (loss) per managed unit in 1974/75 and 1975/76.

Section G: Attitude towards Management/Catering Contracts

84. Why did your company start undertaking management/catering contracts.

85. Is this a long-term commitment or an ad hoc measure.

86. Are you satisfied with your company's capacity to undertake additional management/catering contracts. How is this capacity determined, and what is the maximum expansion per annum which you feel to be feasible.

87. Is there an adequate supply of clients with suitable units/sites and funds for construction of units.

88. What type of client is preferable to you (see questions 25, 26).

89. From what type of client and in what geographical area do you perceive future growth.
90. Does your company enjoy a successful relationship with clients.

91. What, if any, are the main problem areas with them or with the managed outlets.

92. Do you experience any particular difficulties with units located overseas.

93. What factors are likely to affect the future of management/catering contracts:
   (a) in Britain
   (b) overseas.

94. How do you view existing legislation and regulations as affecting your managed interests.

Note: During/at the end of the interview, the following should be requested:
   a copy of the management/catering contract;
   a copy of any other contracts such as technical services agreements;
   any promotional literature provided by the contractor;
   a list of clients' names (for further interviews) or named individuals to be contacted for questioning.
APPENDIX E

QUESTIONNAIRE TO CLIENTS OF CONTRACTORS : MANAGEMENT/CATERING

Date of interview
Name of interviewee
Title
Name of Contractor

Section A: Profile of Client, Data on Client's Unit(s)
1. Name of client company.
2. Public/private.
3. Date of incorporation.
4. Name of system under which unit(s) operated.
5. Name of subsidiary/associated companies.
6. Address of head office/applicable regional office.
7. Registered address.
8. Names of top executives, major shareholders.
10. Brief description of size of company, location of units, market sector, etc.
11. Number and location of units operated for client by contractor.
12. Name and address of unit being the main subject of this interview.
13. Type of 'customers' for whom services are being provided (eg. hotel guests/employees/patients/students).
14. Classification of location of unit (eg. city/suburban/rural/industrial/other).
15. Approximate grading of unit/services provided (eg. de luxe/1st class or silver service catering/cafeteria).
16. Size of unit (if hotel - number of rooms; if catering - potential or actual number of customers served).
17. Hours that unit(s) is/are operational.
18. Are other management/catering contractors concurrently employed by you.
19. Do you concurrently own and operate other outlets similar in activity to that/those being operated by the contractor.
20. Is the employment of a contractor an intended long-term arrangement/short-term 'bridging' or 'rescue' measure.
21. (For catering contractors only) What is your policy towards the provision of catering services (ie. why do you provide them).
22. (For catering contractors only) What is your policy in respect of subsidizing such services. How much subsidy do you pay.
23. (For hotel management contractors only) Is your ownership of an hotel a planned/ad hoc state.
24. Did the contractor take over management of the unit prior to its implementation/as a going concern.
25. For how long have you had a business relationship with your contractor.

26. What is the duration of the management/catering contract. How is this renewable.

Section B: Contractor's Input to Arrangement

27. Did the contractor undertake a feasibility study for the proposed unit/recommend others so to do.

28. Was technical expertise available from the contractor/recommended experts on construction, design, decor, equipment and stock inventory.

29. Was this technical advice and assistance included within the management/catering contract, or the subject of a separate agreement.

30. Was advice and assistance available on systems, procedures and standards.

31. Did the contractor suggest and install financial and operating controls, produce budgets.

32. What is the extent, frequency and mode of financial reporting undertaken by your contractor.

33. Did the contractor recruit and train staff for your unit. Were they transferred from other units of the contractor or specifically recruited to your unit (establish to which categories of staff these responses apply).

34. Were staff installed prior to the opening of the unit. What levels of staff were these, and how long in advance were they posted.

35. What pre-opening support was provided by your contractor in respect of training/sales promotion/advertising etc.).

36. How did you reimburse your contractor for such support.

37. Does/do your unit(s) receive visits from representatives of your contractor (how frequently, by whom, for what purpose).

38. Is information provided by your contractor on operating and financial norms of units similar to yours.

39. Has your contractor any financial interest in your unit. If yes, is this in fixed assets/working capital, and what is the amount of investment.

40. What marketing support is provided by your contractor (market research/advertising/sales promotion/reservation system/point of sale merchandise).

41. If not provided by your contractor, are such services available to you through agents nominated or recommended by your contractor.

42. Is an additional payment made by you for such services or are they included within the management/catering fee.

43. Is/are your outlet(s) branded in the name of your contractor, and are your 'customers' aware of the managed status of the outlet(s)
44. Did your contractor supply initial purchases (indicate if equipment, food etc.).

45. Does your contractor act as supplier of all/most/some of your purchasing requirements. Are nominated or approved suppliers proposed by your contractor.

46. Does your contractor receive an additional payment for such services. If possible give an indication of the amount involved.

Section C: Client's Input to Arrangement

47. What type of fee structure governs this arrangement (fixed/incentive etc. - obtain precise details of included and excluded costs).

48. Indicate the approximate overall fees paid to your contractor in 1974/75 and 1975/76.

49. What, if any, additional fees were payable to your contractor. (state type and approximate amount).

50. When do fees become payable.

51. To what extent does this arrangement expose you to financial risk/payment of subsidies.

52. Do you own/have title to the land, buildings, fixtures and fittings, equipment, stock, working capital.

53. Do you provide for the use of your contractor, lighting, heating, drainage, telephone, lifts, water.

54. Are employees in the managed outlet(s) employed in your name/that of your contractor. Who is responsible for potential claims by employees (give details of any allocated responsibilities between the two parties).

Section D: Imposed Controls

55. What limit do you place on the authority of your contractor in respect of determining operating policies, standards of performance.

56. What limit do you place on the authority of your contractor in respect of setting budgets, incurring operating costs and determining selling prices.

57. How do you monitor the performance of your contractor.

58. Do you have right of access to your outlet(s), to the books of account, and to the relevant records kept at your contractor's head/regional office.

59. To what extent do you come in contact with the manager of the outlet (eg. frequency of meeting, action instigated etc.).

60. Whose responsibility is it to ensure compliance with local regulations and laws.

61. What is the arrangement for the replacement and renewal of equipment, fixtures and fittings, furniture and for redecoration of outlet(s).
62. (For catering contractors only) Whose responsibility is it to maintain the catering premises and equipment in a proper state of hygiene.

63. Indicate the arrangement made for insurance of premises, equipment, stock, employees, third parties such as 'customers' etc.

64. Are you permitted to sell or assign your outlet without prior permission from your contractor.

65. In case of dispute, is an arbitrator named in the contract.

Section E: Attitude towards Management/Catering Contract Arrangements

66. Why did you employ an hotel management/catering contractor.

67. Why did you employ this particular contractor.

68. How many previous contractors have you employed.

69. What led to your terminating their contracts.

70. Are you satisfied with the performance of the unit manager.

71. Are you satisfied with the contractor's overall performance.

72. Do you enjoy a successful relationship with your contractor.

73. What, if any, are the main problem areas in this arrangement.

74. Do you consider that the contractor gives priority to his wholly-owned and managed interests.

75. Do you intend to operate your unit(s) yourself in the short/medium/long term.

76. Are you considering changing to another contractor.

77. What factors are likely to affect the future of management/catering contract arrangements.

78. How do you view existing legislation and regulations as affecting your outlets under management, or your contractual arrangement.

Note: During the interview the following should be requested:

a copy of the management/catering contract;

other promotional material provided by the contractor.
APPENDIX F

QUESTIONNAIRE TO FRANCHISORS/BREWERIES

Date of interview
Name of interviewee
Job Title

Section A: Profile of Franchisor/Brewery

1. Name of Franchisor/brewery.
2. Public/private company.
3. Date of incorporation.
4. Name of system(s) operated.
5. Name of parent company.
6. Name of subsidiary/associated companies.
7. Address of head office/applicable regional office.
8. Registered address.
9. Name of top executives, major shareholders.
10. Main business occupation of franchisor/brewery.
11. Main business occupations of parent/subsidiary/associated companies.
12. Location of outlets.
13. Number of outlets within system(s).
14. Proportion/number of franchised: company-owned and operated outlets/tenanted: directly managed public houses.
15. Brief history of company development (including initiation of system(s) in which franchising occurs and date of commencement of franchising per se/or history of brewery growth, amalgamations etc.).
16. Anticipated future development (growth in franchising: direct ownership and operation/tenancies: direct management: system or product diversification, changes in market location etc.).
   (a) from franchised/tenanted outlets.
   (b) from all franchisor/brewery activities.
18. Pre-tax profit (loss) for 1974/75 and 1975/76.
   (a) from franchised/tenanted activities.
   (b) from all activities of franchisor/brewery
19. Capital invested at 1976 book value in
   (a) franchised/tenanted outlets
   (b) all outlets within system
20. Number of directly-employed employees of franchisor/brewery.
Section B: Profile of Company's Franchisees/Tenants

21. Number of franchisees/tenants.
22. Location of franchised/tenanted outlets.
23. Classification of franchisees
   (a) single/owner-operator (up to 5 units).
   (b) multiple/franchisees with more than 5 units.
24. Nationality (predominant, range).
25. Age ('average', range).
26. Sex, marital status (predominant).
27. Involvement of franchisee's/tenant's family ('average').
28. Socio-economic grouping (predominant, range).
29. Educational qualifications ('average').
31. Prior knowledge of specific locality (on 'average').
32. 'Average' length of business relationship with franchisees/tenants.
33. Duration of franchise/tenancy agreement. How and when renewable.
34. How are franchisees/tenants located (advertisement, broker, personal contacts).
35. Outline screening process.
36. Indicate franchisee/tenant turnover (ie. wastage of personnel).

Section C: Franchisor's/Brewery's Input to Arrangement

37. Is a feasibility study undertaken/advice given on location of outlet.
38. Is advice and assistance available on construction, decor, equipment, stock inventory. Describe typical extent of your involvement.
39. Is advice and assistance available on systems, procedures and standards. Give examples of your involvement.
40. Is an operating manual provided.
41. Is training available for franchisees/tenants and/or their employees.
42. Describe training provided (whether formal/informal, on-the-job/ at special training centre/nominated outlet, free/charged for).
43. Is opening support provided, by whom and for how long. Describe typical support given by you.
44. Are visits paid by a representative of franchisor/brewery (state frequency, by whom and for what purpose).
45. What is the span of control of such representatives.
46. Is information provided to franchisees/tenants on operating and financial norms within the system.
47. Is assistance offered with control and accounting system imple­mentation and supervision. Indicate the extent of such assistance.

48. Is financial assistance offered to all/any franchisees/tenants on short/medium/long term basis. If so, indicate the amounts normally involved. Are you willing to act as guarantor.

49. What type of advertising support is offered (national/local, out­line type of advertising normally undertaken).

50. Is there a charge made for such services. If so, how much, and is it standard to all franchisees.

51. Are special promotions organized for system participants, and point of sale merchandise provided.

52. Is this a free benefit/charged at cost/subject to a mark-up.

53. Do you offer advice and assistance to franchisees/tenants on sources of supplies of consumables, equipment etc.

54. Do franchisees/tenants obtain any personal benefits attributable to your purchasing leverage (eg. cheaper medical insurance, holidays, personal shopping facilities etc.).

55. Is an educational programme available to franchisees/tenants, such as refresher courses, seminars organized by you.

56. What formal or informal channels of communication exist for franchisees/tenants to communicate with you or with each other (eg. company magazine, franchisee/tenant association).

Section D: Franchisee's/Tenant's Input to Arrangement

57. How much initial capital investment is required of your franchi­sees/tenants (indicate 'average' or range) for land and buildings, contents including stock, franchise fee (if applicable).

58. Are such funds usually provided by franchisees/tenants themselves, or by third parties (banks, loan houses, friends etc.).

59. When does the franchise fee become payable.

60. What form of continuing payment is made, and how much is this (royalty/rent/mark-up on supplies/other).

61. Is a standard payment made by all your franchisees/tenants, or does this vary according to projected/actual volume of sales, or negotiating strength.

62. Do your franchisees normally provide/locate potential sites or buildings.

63. Is local market feedback provided by your franchisees/tenants on customer demands, uptake of products etc.

64. Do franchised/tenanted outlets act as pilot units for new pro­ducts or methods.

65. Are other franchisees/tenants or your directly-employed employ­ees trained by your franchisees/tenants.
Section E: Imposed Controls

66. Are your franchisees/tenants subject to control on all/most/some supplies of food/beverages/disposables/equipment/other items sold.

67. Are the costs of these supplies controlled by you.

68. Do your franchisees/tenants have complete/some/no discretion on the choice of products/services offered.

69. Do you control the selling prices of all/some/no products sold by them.

70. Do you stipulate opening times.

71. Are operating methods used in franchised/tenanted outlets laid down in detail by you.

72. Do your franchisees have area exclusivity.

73. May they increase the number of outlets which they operate within your system.

74. May they operate outlets other than within your system, or undertake other business interests.

75. Do you exercise control over your franchisees'/tenants' personal behaviour.

76. Does a minimum amount of supplies have to be ordered by your franchisees/tenants.

77. Do your franchisees have the right to sell or assign their outlets without your permission.

78. Must franchisees be governed by your decision concerning location.

79. Must franchisees/tenants respect your decisions concerning construction, design, furnishing and equipping their outlets.

80. Are they constrained to utilize the architects, designers, shopfitters etc. recommended by you.

81. Is it obligatory for franchisees/tenants and/or their employees to undergo training organized by you.

82. Must they comply in all respects with the operating manual provided by you.

83. Is it obligatory to respect your accounting procedures. Do you require sight of their audited accounts.

84. Must franchisees/tenants comply with special promotions organized by you.

85. What stipulations are made by you concerning insurance by your franchisees/tenants against third party liability/other liability.

86. What control do you exercise over the timing and quality of replacements and renewals in franchised/tenanted outlets.

87. Is an arbitrator named in your agreements with franchisees/tenants.
Section F: Operating Data on Franchised Units

88. What opening times (days, hours) are kept.
89. State the number of staff per franchised/tenanted outlet ('average' or range).
90. What are the annual gross takings per franchised/tenanted outlet ('average' or range).
91. Indicate the following percentage costs on turnover expected in your franchised/tenanted outlets: food costs, labour costs, rent and rates, other overheads.
92. Indicate the annual pre-tax profit (loss) per franchised/tenanted outlet ('average' or range).
93. What is the 'average' spend per customer per franchised/tenanted unit.

Section G: Attitude Towards Franchising/Tied Tenancy Arrangement

94. Why did your company begin franchising/initiate tied trade tenancies.
95. Is this a long-term commitment/short term/ad hoc measure.
96. Is there a sufficient supply of potential franchisees/tenants of an overall suitable calibre for your purpose.
97. Does your company enjoy, on the whole, a successful relationship with your franchisees/tenants.
98. Do you consider that your franchised/tenanted outlets are competently and satisfactorily operated.
99. What, if any, are the main problem areas with franchisees/tenants, or in franchised/tenanted outlets.
100. Do you regard franchisees/tenants as independent businessmen and women.
101. Do you have a preference for single or multiple franchisees.
102. Are there any specific problems arising from relationships with multiple franchisees.
103. What factors are likely to affect the future of franchising tied trade tenancies.
104. How do you view existing or potential legislation as affecting your franchised/tenanted interests.

Note: during the course of/at the end of the interview, the following should be requested:

- a list of franchisees'/tenants' names from which to select interviewees OR suggestions for future interviewees.
- a copy of the franchise/tenancy agreement.
- any promotional literature aimed at franchisees/tenants.
APPENDIX G

QUESTIONNAIRE TO FRANCHISEES/TENANTS

Date of interview
Name of interviewee
Title (if applicable)
Name of company with whom a contract is made

Section A: Profile of Franchisee/Tenant

2. If a company, the registered name.
4. Date of incorporation.
5. Name of system of which respondent is a member.
6. Address of unit(s) being the main subject of interview.
7. Number of units under franchise/tenancy within above system.
8. Location of units within above system.
9. Other units under franchise/tenancy outside above system.
10. Other business interests.
11. Duration of business relationship with above franchisor/brewery.
12. Duration of current contract (i.e. excluding renewals).
13. Duration as franchisee/tenant per se.
14. Nationality. (If not UK born, how long in this country).
15. Age.
16. Sex, marital status.
17. Is there a family background of being franchisees/tenants.
18. Involvement of family in franchisee's/tenant's unit (state approximate hours).
22. Prior experience as owner of business/manager/supervisor.
23. Prior knowledge of specific locality in which outlet(s) situated.
24. Describe application procedure.
Section B: Franchisor's/Brewery's Input to Arrangement

26. Did franchisor/brewery recommend consulting a third party prior to signing the contract (e.g. lawyer, accountant, bank manager).

27. Were trading figures revealed to you prior to signing the contract, indicating the norms of the outlet in question, or of an average outlet within the system.

28. (For franchisee only). Did your franchisor undertake a detailed assessment of the feasibility of one or more sites on your behalf.

29. (For franchisee only). Did your franchisor advise on construction, decor, furnishing, equipment, stock inventory.

30. Was advice and assistance given on systems, procedures and standards.

31. Were you given an operating manual/other written information to aid operation.

32. Was training offered or provided to you and/or your employees.

33. Outline type of training, duration, and state whether this was free.

34. Was opening support provided by your franchisor/brewery.

35. Outline type of support, who gave it, duration.

36. Are visits made to your unit(s) by representatives of your franchisor/brewery. How frequent are these, by whom made, and for what purpose.

37. Are you provided with information on operating and financial norms within the system to which you belong.

38. Is assistance available with control and accounting procedures, and/or with auditing.

39. Have you received any financial assistance from your franchisor/brewery (other than the fixed assets of land and premises), in respect of a loan, credit on supplies, introduction to finance from a third party.

40. Is marketing support provided by your franchisor/brewery (including market research, product research, advertising, sales promotion).

41. Is this a separate cost to you.

42. Do you receive point of sale merchandise from your franchisor/brewery. Is this free/charged at cost/subject to a mark-up.

43. Is advice and assistance offered with initial/subsequent purchasing.

44. Have you gained any personal benefits from being associated with a larger company (such as cheaper medical insurance, holidays, competitive personal shopping facilities).

45. Is there opportunity for you to attend educational courses/seminars etc. organized by your franchisor/brewery.

46. Are there formal/informal means of communicating with your franchisor/brewery and/or with other franchisees/tenants.
Section C: Franchisee's/Tenant's Input to Arrangement

47. What was your initial investment in
   (a) land and buildings
   (b) equipment
   (c) stock and working capital
   (d) franchise fee.

48. Was this from your own savings/loaned by a bank/loaned by the
   franchisor/brewery/other.

49. When did you make payment to your franchisor/brewery.

50. What continuing payments do you make to your franchisor/brewery,
   eg. royalty/rent/mark-up on supplies/other.

51. When do you make such payments.

52. Indicate the mark-up which you consider that your franchisor/
   brewery is making on supplies.

53. What subsequent investment have you made in your unit (eg. on
   building, equipment, increased stock etc.).

54. Did you locate yourself, or previously own the site/building for
   your franchised outlet.

55. Do you report back to your franchisor/brewery on market demand.

56. Has your unit been used as a pilot outlet for new products or
   methods.

57. Have you trained other franchisees/tenants or direct employees
   of your franchisor/brewery on behalf of your franchisor/brewery.

Section D: Imposed Controls

58. Which, if any, of the following sources of supplies are controlled
   by your franchisor/brewery:
   (a) food
   (b) liquor
   (c) disposable items
   (d) equipment
   (e) other items sold

59. Does your franchisor/brewery control the purchase price of (a)/
   (b) etc. above.

60. Does your franchisor/brewery control the selling price of (a),
   (b), (c), (e) above.

61. Do you have to order a minimum amount of supplies from or through
   your franchisor/brewery.

62. Do you have discretion on all/some/none of the products which you
   may sell from your unit.

63. Does your franchisor/brewery stipulate operating times for your
   unit.
64. Must you respect in considerable detail the operating policies/systems/procedures of your franchisor/brewery.

65. Do you have area exclusivity laid down by your franchisor. How is this defined.

66. Are you permitted, within the same system, to increase the number of units that you may operate.

67. Are you permitted to take on units of other systems under your management (i.e. become a master franchisee/tenant).

68. Are you permitted to concurrently undertake other business interests.

69. Does your franchisor/brewery stipulate controls over your personal conduct.

70. Are you permitted to sell or assign your franchised outlet/transfer your interest in the tied tenancy.

71. Are you obliged to comply with franchisor/brewery advice in respect of construction or alteration to the building, decor, equipment etc.

72. Are you obliged to use franchisor/brewery - recommended specialists such as architects, engineers, shopfitters etc.

73. Is it obligatory for you/your employees to undergo training provided by your franchisor/brewery or by designated agents.

74. Must you observe your franchisor's/brewery's standardized accounting procedures and controls.

75. Must you participate in a stipulated number of special promotions organized by your franchisor/brewery.

76. What stipulations are made in respect of insurance cover (which party is responsible for what cover).

77. What stipulations are made in respect of redecoration or renewal of equipment in your outlet.

78. In case of dispute, is an arbitrator named in your contract.

Section E: Operating Data on Franchised/Tenanted Unit

79. What opening times do you normally keep (days, hours).

80. How many staff do you employ, on a year-round 'average'. Does this include members of your family or your own time.

81. What were your annual gross takings in 1974/75 and 1975/76 per one franchised unit and/or all your franchised units within the system.

82. What percentage costs on turnover do you have in your unit(s) including food costs, labour costs, rent and rates, other overheads.

83. What was your pre-tax profit (loss) in 1974/75 and 1975/76 in one unit and/or all your franchised units within the system. (Determine whether this is before or after a 'salary' has been paid to respondent and family, if applicable, and whether depreciation has been charged, and a return on capital investment calculated).

84. What is the average spend per customer in your unit.
Section F: Attitude towards franchising/tenancy arrangement

85. What led you to take up franchising/enter into a tied trade tenancy.

86. Why did you decide to become involved in hotel/catering/public houses.

87. What motivated you to choose your particular franchisor/brewery.

88. Is this a long-term arrangement or an interim measure for you.

89. Has the franchise/tenancy arrangement lived up to your expectations in terms of economic reward, and job satisfaction.

90. Did your franchisor/brewery 'oversell' the possibilities of your unit.

91. Do you enjoy a satisfactory relationship with your franchisor/ brewery.

92. Does your franchisor/brewery fulfill the obligations set out in the agreement/undertake their responsibilities originally held out during initial discussions with you.

93. What, if any, are your main problems with your franchisor/brewery.

94. Do you regard yourself as an independent businessman/woman.

95. Do you find any of your franchisor's/brewery's controls onerous and without adequate justification.

96. Do you consider that your franchise/tenancy agreement is fair.

97. Are you satisfied with your franchisor's/brewery's public image.

98. What, if any, changes would you like to make to your franchisor's/ brewery's system.

99. Do you consider that franchisor-/brewery-owned outlets receive preferential treatment.

100. What factors are likely to affect the future of franchising/tied trade tenancies.

101. How do you view existing or potential legislation as affecting your franchised/tenanted interests.

Note: During the interview the following should be requested:

a copy of the franchise/tenancy agreement;
any promotional literature provided by the franchisor/brewery;
sight of audited accounts.
Two Main Fee Structures of Catering Contractors

Fixed Fee System

This is a method of payment which has been used during the early development of contract catering, and is still employed by some contractors. An overall fixed cost is quoted by the contractor to the client, being the total sum payable by the client to the contractor to reimburse operating costs including consumables and labour and the contractor's profit. No fixed retainer is made. Usually the fixed fee is calculated and tendered as a specific cost per potential customer (i.e. usually the client's employees). The client normally provides, free to the contractor, the use of premises and equipment, and services such as heating, lighting, water etc. During the 1950s the majority of contractors moved away from the fixed cost system, and turned to using the 'cost plus' system. This was mainly due to rising food and labour costs combined with clients resistance to increasing selling prices to their employees, thus putting the contractors' margins under pressure.

'Cost Plus' System

As in the fixed fee system, the client normally provides premises, fixed equipment and services free of charge. In addition the client undertakes to reimburse the contractor for all properly incurred expenses including labour costs and related charges, supplies of consumables and sundry other items such as laundry, stationery etc. The 'plus' element is a guaranteed management fee payable to the contractor, which is calculated in various ways.

Comparison of Two Systems

The protagonists of each system make claims for the relative advantages to clients and contractors of one system as opposed to the other. Those who advocate fixed cost catering claim that a guaranteed overall cost (frequently being a subsidy by clients on their employees' feeding) benefits clients by stabilizing budgets. They also claim that the
contractor puts his own profit at risk and therefore manages the catering operation with greater care and expertise. Fixed cost contractors state that cost plus catering enables contractors to pass on to clients the results of poor buying and inadequate control whilst retaining their own management fee irrespective of performance. They also claim that in cost plus catering there is no incentive for the unit manager to use his initiative in competitive purchasing or in producing good operating results.

Protagonists of cost plus catering emphasize that despite the theory of unrestricted transmission of costs to clients, in practice they have to work within a budget and costs are normally carefully scrutinized by clients. They claim that any benefits from better purchasing or good management are passed on to clients. Commenting on fixed cost catering, the advocates of the cost plus system state that in practice (particularly in times of inflation) the fixed fee must either include built-in safeguards or be subject to constant re-negotiation - neither of which elements benefit the client. They also claim that the system of fixing an overall limit on costs may encourage reduction in quality or portion size and payment of lower wages to staff.

In comparing the two systems, what is material is that in practice both are normally subject to an overall fixed budget which may be extended by negotiation or special arrangement, in response to external factors beyond the contractor's control. In both systems a degree of trust is necessary between the two parties. If the client questions the contractor's integrity and amount of remuneration being received, in the case of fixed cost catering he must monitor the quality of product, size of portions and consider what proportion of the total fee is the contractor's profit. In cost plus catering he must monitor expenditure and standards and may question what alternative revenue is being received by the contractor as discounts from suppliers.
APPENDIX I

DESCRIPTION OF TYPE OF CLIENT FOR HOTEL MANAGEMENT CONTRACTORS: CURRENT AND POTENTIAL

The following examples of actual and potential client-types were given by contractors and other interested parties. Their most likely main reasons for the arrangement and the expected duration of the relationship are also suggested. Some clients may be classified under more than one heading.

1. Clients from developing countries, particularly from the Middle East and North Africa, interested in planned joint development and the long-term separation of ownership and management. Examples of such clients were: governments, government agencies, consortia of foreign businessmen, participating British businessmen and very wealthy individuals.

2. Clients from companies desiring to complement their business interests in related fields such as leisure complexes, marinas, tourist transportation etc. within Britain and overseas. Clients wishing to complement their corporate facilities through the provision of residential accommodation for employees or trainees in Britain and overseas. The duration of such relationship being likely to vary.

3. Clients from a variety of companies with 'inherited' ad hoc interests in hotels, including British and foreign companies. The length of agreement would usually depend on the adequacy or otherwise of the hotel's financial performance, and the company's policy towards retention of non-mainstream interests.

4. Developing hotel companies, interested in a short-term arrangement to gain expertise from the importation of a contractor's services. Other hotel companies with widely dispersed units or distant regional or head offices, in the process of increasing their penetration of an area or prior to selling off their interests altogether, and requiring 'bridging' operational and marketing resources. Clients from developing countries (as outlined above in 1) interested in gaining staff training, marketing benefits and operational expertise on a short-term basis.
5. Local government authorities, interested in maintaining or developing hotel facilities for the general benefit of a locality, as in new towns and areas of re-development; such arrangements occurring in circumstances where hotel operators proved unwilling to undertake ownership or a lease; the duration depending upon the demonstrable viability of the hotel (and consequent potential interest of a buyer).

6. Banks, insurance companies, mortgagees and those acting as receivers for hotel properties, interested in recouping their investment or obtaining repayment to creditors, and involving a short to medium-term arrangement to establish the hotel as a viable proposition (or at least to improve its potential sales value) before selling.

7. Individuals with various personal reasons for short or long-term arrangements, including proprietors suffering from ill-health or old age and those disinclined to maintain close personal supervision over their hotel's operation. Individuals who desired to own, but not to manage a hotel property, for reasons of prestige or as a supporting facility for their business and personal life-style, such as film and stage stars and others prominent in the public eye. Individuals interested in the ownership but not the management of hotels for tax purposes such as the ability to set off losses on the hotel against gains derived from other interests; or to provide roll-over capital gains benefits; or to constitute a facility for free living and/or entertaining.
APPENDIX J Terms Defined Within Management Contracts

Main Financial: Gross Revenue, gross income, sales, gross operating income, operating expenses, outgoings
Gross operating profit
Adjusted gross operating profit
Net operating profit, net profit, profit
Cash flow
Pre-opening expenses
Annual budgets, annual plans
Capital
Equity share capital

Time: Fiscal year, account period, account day
Pre-opening period
Completion of hotel
Opening date
Operating Term, operating period, operating years

Services: Technical assistance services
Group services

Parties: Hotel owner, proprietor
Operator, manager
Operator's subsidiaries, affiliates, parent company
Operator's other hotels (wholly owned, franchised or associated)
Other interested parties (named in each agreement)

Inanimate Objects: Site
Building, premises, hotel
Furniture, furnishings and equipment

Legal and Other Financial:
Legal Requirements
Insurance requirements
Capital improvements
Concessions
Ground lease
Mortgage
Compositions, permitted encumbrances
Compensation
Perpetuity
Uniform system of accounting

Source: Management contracts examined by researcher.
### Illustration of Effects of Different Fee Structures in Hotel Management Contracts

based on a fictitious 300 room hotel

<table>
<thead>
<tr>
<th>Description</th>
<th>£</th>
<th>%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Income</td>
<td>3,000,000</td>
<td>100.0</td>
</tr>
<tr>
<td>less Cost of Sales</td>
<td>1,500,000</td>
<td>50.0</td>
</tr>
<tr>
<td>Gross Operating Income</td>
<td>1,500,000</td>
<td>50.0</td>
</tr>
<tr>
<td>less Operating Overheads</td>
<td>600,000</td>
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</tr>
<tr>
<td>House Profit</td>
<td>900,000</td>
<td>30.0</td>
</tr>
<tr>
<td>add Store Rentals</td>
<td>100,000</td>
<td>3.3</td>
</tr>
<tr>
<td>Gross Operating Profit</td>
<td>1,000,000</td>
<td>33.3</td>
</tr>
<tr>
<td>less Other Deductions</td>
<td>£200,000</td>
<td></td>
</tr>
<tr>
<td>Debt Service</td>
<td>500,000</td>
<td>23.3</td>
</tr>
<tr>
<td>Net Income</td>
<td>300,000</td>
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#### Fee Structures

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<th>A</th>
<th>B</th>
<th>C</th>
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</thead>
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<tr>
<td>Share of Gross Revenue</td>
<td>3%</td>
<td>nil</td>
<td>3%</td>
</tr>
<tr>
<td>Share of Gross Operating Profit</td>
<td>12½%</td>
<td>25%</td>
<td>nil</td>
</tr>
<tr>
<td>Share of Net income</td>
<td>nil</td>
<td>nil</td>
<td>50%</td>
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<tr>
<td>Total Fees Payable</td>
<td>£215,000</td>
<td>£250,000</td>
<td>£240,000</td>
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Source: based on privately circulated document, Bib. ref (160).
### Appendix L Management Fee Structures:

#### Examples in Survey of Basic Fees Plus Incentive Fees

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<th>% gross revenue plus %GOP</th>
<th>Special Provisions</th>
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<tr>
<td>2</td>
<td>12</td>
</tr>
<tr>
<td>2½</td>
<td>10</td>
</tr>
<tr>
<td>3</td>
<td>10</td>
</tr>
<tr>
<td>3</td>
<td>13</td>
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<td>25</td>
</tr>
<tr>
<td>3½</td>
<td>9½</td>
</tr>
<tr>
<td>4</td>
<td>25</td>
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<td>10</td>
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<table>
<thead>
<tr>
<th>% gross revenue plus %N P</th>
<th>plus % N P</th>
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<tr>
<td>2</td>
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<tr>
<th>% gross revenue plus %N P</th>
<th>Special Provisions</th>
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<td>2</td>
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<td>2½</td>
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<td>10</td>
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<td>3</td>
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<table>
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<th>Fixed fees</th>
<th>plus %GOP</th>
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<tbody>
<tr>
<td>£2,500</td>
<td>10</td>
</tr>
<tr>
<td>£8,000</td>
<td>10</td>
</tr>
<tr>
<td>£30,000 - 60,000</td>
<td>7½ to 10</td>
</tr>
<tr>
<td>£30,000 - 200,000</td>
<td>25</td>
</tr>
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</table>

Key: GOP = gross operating profit  
N P = Net profit.
Appendix M  Summary of Pre-opening Services
Offered within Contractors' Agreements

Varying between advice, assistance and stipulation to owners and
owners' advisors in respect of:

Site selection
Architecture
Interior design including furnishings and fittings
Equipment including furniture, bathroom, specialized
    hotel and operating equipment.
Kitchen, laundry and other specialized areas.
Mechanical, electrical and plumbing facilities including
    heating, ventilation, air conditioning, lifts,
    phones and other communications
Graphic and other design
Landscaping
Other ancillary facilities eg. leisure and sports

Such services including:
in the Preliminary Stage

submission of overall requirements, standards, concepts,
recommendation of special advisors such as architects, designers,
    quantity surveyors, engineers.
preparation of advisors' briefs
negotiation of advisors' contracts
assistance in production of preliminary plans, specifications and layouts.
review and approval (jointly with other parties) of final
    plans, specifications and layouts.
submission of detailed requirements for specialized hotel
    equipment and operating supplies
preparation of estimated budgets for purchase of above items
recommendation of sources of supply for above purchases
review of bids from suppliers regarding specialized hotel
    equipment and operating supplies in terms of comparative
    costs and specifications
placement of orders of above supplies and responsibility
    for delivery in total
preparation of a programme of work
periodic on-site monitoring of progress of builders, subcontractor and advisors
project management (full time)
submission of progress reports and statements of expenditure
assistance with scheduling deliveries
advice regarding appropriate insurance cover

In the immediate pre-opening stage
planning of operating procedures in all departments
installation of accounting and control systems
recruitment and training of hotel staff
organization of pre-opening advertising and promotion
planning of opening festivities
preparation of budgets and financial projections (immediate pre-opening and post-opening)
determination of post-opening tariffs and charges

Note: not all services were offered by all contractors

Source: management agreements, technical services agreements
Appendix N

Summary of Clauses Relating to Marketing Services
included within management contracts

Sales outlets: in defined geographic, national or regional areas
in defined units eg. contractor's sales agencies or
based within other hotels in the chain
by number of agents or representatives including
those on hotel's payroll, or within contractor's
group services (stating whether executives or
other employees)
via subsidiary or associated companies (units and
agents)
via arrangements with travel agencies, tour operators,
business houses, and government tourist depart­
ments (units and agencies)

Sales Promotion: via local, national or international advertising
via single or joint advertising schemes
using defined advertising material
through package deals to the general public or
specific groups
through specified third party, owner or contractor
channels
by acceptance of discounts, commissions, credit cards
by proferring sample visits to hotel

Reservation Methods: through chain or group referrals
through contractor's centralized reservation system
whether computerized or manual

Markets: single or group bookings
convention and business seminars
personal

Market Research: Research and development of appropriate business

Public Relations: Handling of customer complaints
Marketing Policy: with regard to:
- comparable status to other hotels within the group or chain
- chain promotion
- reservation and referral systems
- reporting procedures
- discounts and commissions
- credit card acceptability

Note: no one contract contained reference to all headings

Source: management agreements examined by researcher
CHAPTER 1

1. Formerly the Department of Hotel and Catering Management

2. Bib.ref. (33). Minimum List Headings 884 (hotels and other residential), 885 (Restaurants, cafes and snack bars etc.), 886 (Public Houses), 887 (Clubs), 888 (Catering Contractors).

3. For example, "take-away" outlets were included within the recent study on eating out, implemented by the Hotels and Catering EDC; bib. refs (96) Vol. II No. 2 pp 89 - 102 and (150).

4. The term 'marketing' is used throughout this study to signify the activity of aligning a product (goods and/or services) with market demand, thus encompassing the assessment of demand and its satisfaction through production, distribution and sales. Market research, distribution, advertising and sales promotion are therefore aspects of marketing.

5. Reference was made not only to the club sector as defined within section 887 of the Standard Industrial Classification, but also to clubs whose predominant activity was other than the provision of accommodation and/or food and drink to members, but in which the sale of food and drink constituted a significant ancillary activity.

6. See bibliography for list of works consulted in the study.

7. See Appendix A for list of main periodicals and newspapers scanned, and refer to bibliography for the main works that were consulted.

8. See Appendix B for list of companies requested for copies of their reports and accounts.

9. See Appendix C containing a list of 'informed individuals' consulted during the survey.

10. See chapters 5, 6, 7 and 8 for details of sample, size and criteria for selection of interviewees.

11. See Appendices D, E, F, G.

12. Whilst it was realized that greater benefit would have been derived from receiving a copy of such documents prior to the interviews with contractors, brewers or franchisors (thereby rendering unnecessary some of the questions concerning standard contractual or financial terms, and providing more information on which to base other questions), it was deemed unlikely that such documents would be released unless the respondent's confidence in the researcher's integrity were first assured. The assumption seems to have been valid as the majority of respondents at first were disinclined to part with their standard contracts, and had to be reassured that they would be treated in complete confidence.
CHAPTER 2

1. Eyster Bib. ref. (65) was not published in the U.S.A. until 1977, and Ozanne and Hunt, Bib. ref. (159) was unobtainable for more than a year. In addition a further useful work by Stanworth Bib. ref. (186) was not completed until this study was almost finished.

2. No number was specified, but allusions in the text suggest that some ninety respondents formed the universe of this study.

3. Including the study by Curry, Bib. ref. (48), reviewed above.

4. Ozanne and Hunt, reviewed above, Bib. ref. (159)

CHAPTER 3

1. However, in Thompson, Bib. ref. (197), p.xvi, it is pointed out that no market system is ever completely free because of explicit and implicit restraints such as the law of contract, or ownership integration.

2. Curry, Bib. ref. (48) p.10.

3. Thompson, Bib. ref. (197) p.12.

4. As quoted in Conference Board, Bib. ref. (40) p.4.

5. No information was directly obtainable from the International Franchise Association. This definition, attributed to the I.F.A. is given in Mendelsohn, Bib. ref. (135) p.6.

6. Conference Board, Bib. ref. (40) p.3.

7. The author notes that this does not imply a guaranteed area exclusivity as essential to a franchise.


16. In this study reference is made only to tenanted on-licensed premises.

17. For example in the Times, Bib. ref. (66) in which no distinction is made between franchising, concessions, distributorships and pyramid/multi-level selling and Sunday Times Bib. ref. (139) in which franchising and pyramid selling are not distinguished.

18. At a NESDA conference Bib. ref. (154), paper by Scottish Advocate Mathieson, A.M. on "The Legal Aspects of Joint Ventures and Licensing Agreements".

19. A number of American franchise systems use the terms "licensor, licensee, and license" to describe participants in, and the agreement of a franchise arrangement; e.g. McDonalds.
20. Conference Board, Bib. ref (40) p.5 and Curry, bib.ref. (48) p.11. 
21. See Para 3.22. 
22. Mendelsohn, Bib. ref (135) p.4. 
24. See Paras. 3.32 and 3.33. 
26. See for example Thompson, Bib. ref (198) pp. 8 and 9. 
27. No British statistics of franchising have been compiled. 
28. U.S. Dept. of Commerce, Bib. ref (209) states that in 1975 the franchise sales from automobile and truck dealers, automotive products and services and gasoline stations were approximately 76% of all franchise sales; estimates for 1977 are put at approximately 80%. 
29. Izraeli, Bib. ref (107) pp. 29 and 67 and see later para 3.64. 
30. Kursh, Bib. ref (115) pp. 30 and 247; examples in USA: Mr. Softee and Snap on Tools; in UK: Home Tune franchise, see Sunday Times 1 Feb 1976. 
31. Izraeli, Bib. ref (107) p.43. 
34. Including a number of people approached by the researcher during the course of this study. 
35. Except in some area, regional or territorial franchising, see Para. 3.72. 
36. In the U.S.A., examples of such systems are franchises for sale of hearing aids and advice to wearers, or for sponsorship of teenage beauty competitions, see Kursh, Bib. ref (115) p.225. 
37. See above para 3.52. 
39. See Izraeli, Bib. ref (107), Chapter 6 for detailed discussion on group trading in food distribution in Britain. 
40. Eglin and White, Bib. ref (59). 
41. Hall, Bib. ref (92), Rosenberg, Bib. ref (169) and Teston, Bib. ref (195). 
42. Sawyer, Bib. ref (177). 
43. See Para 3.65 for description of 'modern' franchising. 
44. Hall, Bib. ref (92). 
45. Thompson, Bib. ref. (197), pp. 12 and 13, and Bib. ref (198) pp. 13 and 14 for differentiation between types of trademark licensing.
46. Lewis and Hancock, Bib. ref. (120) p.4.
47. Izraeli, Bib. ref (107) p.5.
48. See Chapters 4 and 7 for detailed reference to the tied trade system.
49. Monteguet, Bib. ref (144).
50. Mendelsohn, Bib. ref (135) p.3.

51. In order to differentiate between the types of franchisees with interests in between one and fifty units, an arbitrary cut-off point has been selected of up to and including five units. Those franchisees with an interest in three or more hotels are classified as multiple franchisees, for the greater complexity of operation and geographical spread leads to a less personal involvement by such franchisees, signifies much greater financial investment and implies a greater bargaining strength than in the case of 'take-away' or restaurant franchisees.

52. Mendelsohn, Martin in interview with the researcher 1976.
53. For example, Robert Rhea holds the franchise for England for the McDonald's hamburger operation, per interview in February 1977.
54. In report of the National Restaurant Association Bib. ref (151) the U.S.A. was divided by one company into 67 marketing areas which were assigned to franchisees.
55. For example, Goodwin, Bib. ref (89).
56. But see reference 51 in respect of hotel franchisees.
57. For example, franchisees in this survey concurrently held a Wimpy and a Golden Egg franchise, or a Wimpy and a Dayville franchise.
58. In Britain only two master franchisors were traced: United Biscuits owning the Wimpy and Golden Egg franchise systems (formerly belonging to a J. Lyons and Co. subsidiary), and the Zockoll Group owning Dynarod and Pit-stop Auto Silencers.
59. For example in Arthur D. Little, Bib. ref (123) pp. 21 and 22, see International Industries Inc. which in 1970 was involved in franchising five separate fast food concepts, plus a franchised education system and network of retail outlets selling clothes.
60. Goodwin, Bib. ref (88) p.29.

CHAPTER 4

2. Initiated by the Council of Trent.
3. Thompson, Bib. ref (198) p.19.
4. i.e. shops for the sale of liquor to be consumed off the premises.

5. Monopolies Commission report on Beer, Bib. ref (142), Appendix 8, paragraph 11.


9. Monopolies Commission, ibid, Appendix 8, paragraphs 16 and 17.

10. Monopolies Commission, ibid, paragraph 164. No figures are quoted for other parts of Great Britain.

11. Ibid. Table XXII.


14. For example if the recommendations of the Erroll Report, Bib. ref (51) were implemented, and see Bib. ref (180) for recent changes to Scottish licensing law. See also below Para 9.44.


19. Lewis and Hancock, Bib. ref (120) p.10.


26. Emmons, Bib. ref (60).

27. Kursh, Bib. ref (115).

28. Kursh, ibid, Appx A.


30. Produced by the International Franchise Association and published in Dun's Review and Modern Industry, April 1964, p.36, see also Note 34.


32. Bib. ref (209).
33. This figure, as did previous estimates, includes outlets of franchisees and those directly owned and operated by franchisors.
34. Thompson, Bib. ref (198) p.30.
35. Bib. ref. (209) is the sixth annual survey undertaken by the Bureau of Domestic Commerce.
36. eg. Lewis and Hancock, Bib.ref. (120) and Ozanne and Hunt, Bib. ref (159).
37. Ozanne and Hunt Bib.ref. (159) p.16.
38. Kursh, Bib.ref (115).
40 eg. in franchising bibliographies of Kursh and Thompson in Kursh Bib. ref(115).
41. Boston College Center for the Study of Franchise Distribution.
42. For example, see contributions to Bib.ref (197), edited by Thompson, and also list of postgraduate theses in Bib.ref (159).
43. Resulting in the publications of Bib.refs (197) and (48), for example.
46. An example of an inter-company association is the National Association of Franchised Businessmen, founded in 1965 (but whose continued viability has been questioned by Vaughn Bib. ref (213) p.23); examples of intra-company associations are given in Bib.refs (40) p.94 and (69).
47. This section is based on the following sources: Curry, Bib.ref. (48) p.95; Lewis and Hancock, Bib. ref (120) pp. 14 - 17; A. D. Little, Bib. ref (123) p.8; Thompson, Bib. ref (198) p.21; Vaughn, Bib. ref (213) p.19.
48. Bib. ref (203).
49. Ozanne and Hunt, op. cit p.124 Table 4.11.
50. Milner Bib. ref (139).
51. Bib. ref (203).
52. Izraeli, Bib. ref (107) p.6.
53. Emmons, Bib. ref (60).
54. Izraeli, Bib. ref (107) p.6.
55. For example, see Burck, Bib.ref (19) and Brown, Bib.ref (17)
56. Zeidman, Bib. ref (226) p.100.
57. For example, Senator Philip Hart's Franchise Competitive Practices Act of 1967; and the Federal Trade Commission's proposed trade regulation rule.
58. For example, the action by Chicken Delight franchisees against their franchisor, the Chock Full O'Nuts Case and the Dunkin' Donuts Case in Bib. refs. (102) and (226).

59. Zeidman, Bib. ref. (226).


61. For further discussion, see Izraeli, Bib. ref. (107), pp. 88 and 89.

62. Interview with representative of J. Lyons and Co.

63. Such as ovens, refrigerators and washing machines.

64. For example, Dunkin' Donuts and Orange Julius.

65. Information given by 'informed individuals' during interviews.

66. Domestic franchise systems which have ceased operating altogether or have ceased franchising include Golden Kitchen, Gingham Kitchens, Carpetbagger, Cook Inns, Monte Franks, Sandwich Supermarkets and Seafarer.

67. For example, Coombes, Bib. ref. (41), Symes, Bib. ref. (190), Hotel and Restaurant Management, Bib. ref. (98), Marketing, Bib. ref. (128).

68. Business Ideas Letters, Bib. ref. (21).

69. For example, Gamble, Bib. ref. (82).

70. For example, the British Institute of Management, Institute of Marketing, and the London Graduate School of Business.

71. Gamble, Bib. ref. (82) Section I, p.8.

72. Ibid, Section VII p.3.

73. Held at the Gottlieb Duttweiler Institute, October 23-25.

74. The Institute of Marketing retains a list of such consultants.


76. British Franchise Association brochure, issued at inaugural luncheon November 1977.

77. According to the Secretary of State for Trade, in reply to a written Parliamentary question; Hansard, 29 April 1976, p.184.

78. According to a spokesman at the Office of Fair Trading, questioned in January 1978.

79. See Bib. refs (78) and (107).

80. Including Kentucky Fried Chicken, Wimpy International, Little Chef, Baskin-Robbins, Dayvilles and Happy Eater, as recorded in the Catering Times, 9 September 1976, p.23; and Caterer and Hotelkeeper Bib. ref. (220), 13 October 1977.

81. Including McDonalds, Burger King, Pizza Hut, Mister Donut and Holiday Inns of America.

82. Milner, in Sunday Times, Bib. ref. (139); Clarke, Bib. ref. (37), p.167; and Dakin, Bib. ref. (49).

83. Goodman in Financial Times, Bib. ref. (78) p.13. Note that no definition is given of franchising, nor any sources quoted.
84. For greater detail on historical background, see Koudra, Bib. ref. (114), pp. 44 - 46.
85. Medlik, Bib. ref (133), p.41.
86. Ibid, p.41.
87. Koudra, op cit p.46.
88. Ibid p.46.
89. Differences in definition and in the methods of data collection account for this variation, see Koudra, p.53.
90. Ibid p.53.
92. Koudra, ibid, p.125.
93. Department of Trade and Industry, Inquiry into the Catering Trades for 1969, HMSO, quoted by Koudra, Bib. ref (114), Table 1.7 and Table 4.1.
95. Koudra p.127.
96. Interviews with catering contractors.
97. For general background see Kiener, Bib.ref (110) and Brener and Gamoran, Bib. ref (12).
98. The main difference being that an operating lease agreement places the risk of loss on the operator, not the owner.
100. See Cornell Hotel and Restaurant Administration quarterly, Bib. ref. (44) and Estroff and Gluck, Bib. ref (64) for further information.
102. Eyster, Bib. ref (65) note (1) to Table 5.
104. Eyster pp. 18 and 19.
105. Hallway Hotels Overseas Ltd.
106. For example, the Penta hotel belonging to the European Hotel Corporation and the Stratford-upon-Avon Hilton, owned by Lex Hotels.

CHAPTER 5
1. Koudra, Bib. ref (114).
2. Ibid, p.127.
3. Ibid, p.131 and Table 7.2.
4. One was fifty per cent owned by a large public company.
5. By one of the other contractors in this survey.
6. The accounting treatment of revenue attributable to such activities was altered during 1976, when a separate company was established.
7. Precise information about the early policies of the long-established companies could not be supplied by respondents.
8. 'Multiple clients' being those with two or more units at separate locations, which were operated by any one contractor.

9. One contractor refused to reveal the names of any clients; thus the responses of only eighteen clients are recorded throughout this section.

10. In practice, respondents were unable in some instances to distinguish between original motives for employing contractors and subsequently perceived benefits.

11. However, this benefit was not utilized by several clients who concurrently employed more than one contractor (see Para. 5.32).

12. In one client company all directly-employed staff were awarded inflation-indexed pensions worth two-thirds of their salary after a prescribed number of years with the company, and were guaranteed against redundancy.

13. See Appendix H for description and comparison of these fee structures.

14. Whilst some clients were willing to disclose the cost to them of providing catering services to employees, in the time available it was impossible to make a distinction between net food costs (after full or partial payment of such costs by employee-customers), credited discount passed on by the contractor, and management fees.

15. Contractors were more willing to discuss the practices of their competitors than they were to reveal their own.

16. This was usually due to instances where pension rights of staff, who had formerly been directly-employed by the client were non-transferable, or where catering employees still remained on the clients' payroll following their transference at the time when Selective Employment Tax was levied (thus avoiding the payment of such tax if the client's business was not classified within the service sector).

17. Relevant paragraphs of the Food Hygiene (General) Regulations, 1970, were made applicable either to contractor or to client. Details included in the agreements related to precise areas, eg. contractors were normally responsible for cleaning the kitchen and ancillary areas up to six feet high; clients were responsible above that height and usually, for cleaning the dining area (except the floor) and for maintaining heavy equipment.

18. Varying in title amongst the different contractors' organizations.

19. Some contractors required payment for plans and specifications, such sums being refunded in full if a contract ensued.

CHAPTER 6

1. Even where an hotel's managed status was mentioned in company accounts, reports or brochures or publicly acknowledged by a plaque at the entrance of the hotel, it was not necessarily a characteristic that was widely known. Often no such mention was made. In a few instances hotel companies denied involvement in any managed hotels, such statements subsequently being discovered to be erroneous.

2. Para 3.32.
3. A leased hotel is classified as one in which an hotel company be-
comes the lessee or sub-lessee of an hotel for a number of years
at an agreed rent (however calculated), and in which the hotel
owner does not participate in operating losses nor normally invests
in furniture, equipment or working capital.

4. In operating-lease agreements, a contractor provides managerial,
operational and marketing advice and services; substantially
similar contractual arrangements obtain as in management agree-
ments.

5. More recently a further eight management contracts have been
announced in the trade press: HCIMA journal, June 1977, p.35;
Catering Times, 19 May 1977, p 24; ibid 16 June 1977 pp. 2 and 4;
ibid 1 Sep 1977 p. 3; ibid 8 Sep 1977 p. 16; ibid 27 Oct 1977 pp 2 and 12

6. The small total population of hotels operated under management
contract may also have contributed to their reluctance to provide
information, despite assurances that their responses would not be
directly attributable to them.

7. Though not necessarily in respect of only one hotel.

8. All were known to be interested in obtaining management contracts
within Britain.

9. One such company being majority-owned by a substantial hotel group,
itsl now part of a larger company with wider interests.

10. See above, para 6.12.

11. Estimated total number of hotels in Britain being some 35,500,
Medlik, Bib. ref (133), p.135.

12. See below, para 6.432 and Appendix L.

13. Most British contractors commenced operating management contracts
after 1970; such contracts still remain relatively few. In the
U.S.A., very few companies operated management contracts before
1970, but growth has been spectacular, see above, para. 4.63.

14. See Appendix I for classification of current and potential
types of clients.


16. See Appendix J for terms defined within standard management con-
tracts.

17. The contractor could terminate after three years, giving three
months notice; the client could terminate after ten years, giving
one year's notice.

18. One company had a formalized weighted fee structure varying
according to different areas of the world.

19. See Appendix K for example of financial consequences of differ-
ent fee structures applied to the same hotel.

20. Usually excluding land and sometimes excluding other capitalized
costs such as financing charges, professional fees, operators
fees, and organizational and development costs.

21. See Appendix M for summary of pre-opening services normally
offered in technical assistance agreements.
22. It was normal practice for a project manager to be the incoming general manager. Other staff were usually dispatched at intervals prior to the hotel's opening; for example, line managers - six months before opening; departmental managers - three months before opening; and all other employees - six to eight weeks beforehand.

23. See Appendix N for summary of marketing services included in some management contracts.

24. For example as required by new laws or regulations, see below para 6.46.

25. One example was given in respect of a stable economic period when the advent of the contractor doubled the hotel's profit made in the previous year.

26. In one instance, the multi-national background of a significant number of guests at a small, remotely-situated hotel in England was directly attributed by the owner to the contractor's world-wide advertising and sales promotion.

27. Whilst being the only practical measurement of head office interest in a managed hotel, it was not necessarily indicative of the total availability of advice and skills of the contractor's organization, which might also be proffered by telephone or written communication.

28. In one example, the contractor claimed to have received no management fee nor a reimbursement of expenses from a particular client (a foreign government) during the course of one year, despite the agreed contractual terms stipulating payment of the basic fee at monthly intervals.

29. Particularly if the management fee were calculated as a percentage of gross operating profit.

CHAPTER 7

1. Tenanted off-license outlets, i.e. shops selling liquor for consumption off the premises, are excluded from this study.


3. Ibid, and interviews with brewery representative.

4. Two breweries which were initially selected, declined to participate in the survey.

5. In both instances the separation of financial information for each company proved difficult.

6. See below, para 7.42 for explanation of terms, and 7.363 for tenants' reported payments.

7. See above, para 4.2.

8. The government standstill on rents for public houses was not lifted until early in 1975. See also National Board for Prices and Incomes, Bib. ref. (148) para 40.

9. One company reported a need for smaller public houses in which to begin the training of new directly-employed managers, prior to installing them in large houses.
10. In contrast with the standard division of such responsibilities between tenant and brewer, see below paras. 7.43 and 7.45.

11. The severe 'rent-freeze' on public house rents lasted from 1966 to 1972, at which time a 12% increase on the frozen rent level was allowable against the cost of improvements.

12. Tenants also tended to remain with the same brewery as that with which their parents or grandparents had held tenancies.

13. Including sons, daughters, parents, brothers and cousins.

14. See below, paras 7.42, 7.421 and 7.422.


16. In each case relating to a single public house.


18. In some instances a separate agreement was signed regarding the amount and timing of payments from the tenant to the brewer.

19. One brewery representative provided a standard formula used by his company for the calculation of rent.

20. Unless a recent valuation of the property had been undertaken.


22. As noted in Financial Times, 27 September, 1976, Courage ended practice of imposing 'wet' rents, and reduced the cost of beer to tenants by 1½p per pint.

23. In ten of the breweries tenants were allowed complete freedom of choice regarding minerals, fruit juices, cigarettes and tobacco, or could choose from recommended brands and suppliers.

24. In one exceptional case, a tenant of long-standing was not tied to his brewer for the supply of wines and spirits.

25. See Brewers Almanack, op. cit. pp. 362 and 363. 'The Panel' can be either a local body nominated by the recognised associations of brewers and retailers for each local district, or a central body nominated by the Brewers' Society and by the National Consultative Council of the Retail Liquor Trade, such a body being approached to arbitrate on matters in dispute between brewers and their tenants.

26. Some agreements included clauses which stated that written permission to buy outside the tie would not be refused in such circumstances.

CHAPTER 8

1. See above, Para. 3.58.

2. A term denoting the manager who has been granted the licence to operate a management incentive scheme.

3. These include the above mentioned management licence schemes, which unless specifically excluded, are encompassed throughout the remainder of this chapter under the term 'franchise'. The parties to such schemes are included in this chapter under the terms 'franchisor' and 'franchisee'.

4. Because of constraints on time and costs no interview was carried out with one franchisor, whose representatives were based overseas.

5. Since this survey was undertaken, one system has ceased operating as an integrated unit and two of the systems have been sold to another company.

7. An endeavour was made to establish the overall business interests of franchisees. However, many franchisees were unwilling to divulge information that was not directly related to their franchised unit(s).

8. See above, Paras. 3.71 and 3.73 for fuller description.

9. See below, Para. 8.421 for more detailed discussion.

10. See below, Para. 8.422 for more detailed discussion.

11. Franchisees presumed (correctly so in almost all cases) that the concept offered them by their franchisor had undergone pilot testing - this being one of the hallmarks of 'ethical' franchising.

12. Refer also to Paras. 8.443 and 8.465.

13. For example, a first installment was payable on application; a second installment upon signing the agreement, and a final sum upon the franchised unit becoming operational.

14. Refer to the previous chapter on catering contractors, Para. 5.423 concerning similar problems of isolating discounts awarded to contractors by suppliers.

15. In some instances restrictions upon, or alterations to the system's standardized internal or external appearance were enforced by local authorities or landlords, not by the franchisor or franchisees.

16. Pilot units had been operated by another company prior to the franchisor adopting the system and franchising it.

CHAPTER 9

1. Refer to Chapter 5 for detailed information on catering contractors, their clients, terms of their agreements etc.

2. In order to simplify the subsequent examination of interactions between parties, field supervisors/area managers - as representatives of the contractor - have been omitted, and assumed to reflect the characteristics of the contractor.

3. Such as the wide-spread industrial actions in 1972/73 culminating in the 'three day week'.


5. Koudra, Bib. refs. (112), (113) and (114).

6. Refer to Chapter 6 for detailed information on hotel management contractors, their clients, terms of their agreement etc.

7. In order to simplify the subsequent examination of interactions between the various parties, no separate reference is made to the role or characteristics of district managers or others employed by the contractor to monitor the performance of hotel managers. Their characteristics are assumed to reflect those of their contractor.
8. Eyster Bib. ref. (65) pp. 108 and 109 in which he states that 50% of clients minimally adhered to the relationship as defined in the contract and "tended to be on-site monitoring operations", taking "liberties in attempting to influence and control the general manager and the hotel's operating policies".

9. Development of Tourism Act 1969, Part II, establishing the Hotel Development Incentive Scheme which made available substantial sums for grants or loans.

10. As stated for example by Sir Charles Forte, quoted in Caterer and Hotelkeeper, 24 March 1977, 'Finance' page.

11. For example, to comply with the requirements of the Fire Precautions Act 1971, and Health and Safety at Work (etc.) Act 1974.

12. Such as Centrelink Hotels Ltd., Interchange Hotels, Inter-Hotel, Prestige Hotels.

13. See for example Brener and Gamoran, Bib. ref. (12) and Kaven, Bib. ref. (109).

14. The following examples were given by contractors of problems arising in managed hotels in overseas locations: the closure of an hotel for a number of years because of civil war; the nationalization of hotel properties, key hotel jobs being assigned to patriates lacking sufficient qualifications; non-availability of work permits for expatriate staff; import regulations against certain supplies; restriction on repatriation of funds; tariff controls imposed by governments; interference in the operator's discretion in policy concerning standards of operation; non-payment by a foreign government or agency of contractors' fees and expenses.

15. Such terms in favour of clients are also found where their initial negotiating position is particularly strong, due to their experience as hotel operators or as former clients of other contractors, or due to the contractor's particular dependency on locating suitable client-owned hotels (i.e. if the contractor has no wholly-owned interests).

16. Eyster, Bib. ref. (65).

17. See Chapter 7 for detailed information about breweries, tenants, terms of their agreement etc.

18. The position of multiple tenants has been ignored in this discussion. None with five or more outlets took part in the survey, and multiple tenants (such as large companies) are not representative of the majority of tenants.

19. District managers or other brewery representatives of a similar status have been omitted from the subsequent examination of interactions between parties in order to simplify matters.

20. Bib. ref. (39), (51), (52), (142), and (148).

21. Reform introduced by the Licensing (Scotland) Act 1976, following some of the recommendations of the Clayson Committee. The abolition of 'Veto Polls' has made breweries less vulnerable to the potential loss of a liquor licence at premises which were mismanaged by a licensee, and may therefore cause an increase in the ratio of tenanted: total outlets, because of the reduction in the need for the previously close control maintained over managed houses.
22. In 1965, there were some 6,000 restricted on-licensed premises in the U.K.; by 1975 the number had risen to almost 16,000. In 1965, there were some 25,000 clubs, which by 1975 had exceeded 30,500. The number of off-licenses rose from less than 30,000 in 1965 to almost 36,000 by 1975. Whilst the numbers of full on-licensed premises dropped in the ten years by some 2,000 to less than 74,000. Beer Facts 1977, The Brewers Society.


24. On 1 January 1976, being an amalgamation of the National Federation of Licensed Victuallers and the Central London Board.

25. Either by payment of a 'wet' rent or by the likely increase in fixed rent levied upon a higher turnover by the brewer.


27. Monopolies Commission, Bib. ref (142) para 386.

28. The average net profit in 1967/68 for a tenant outside London before charging his wife's wage, was found to be £1,339 according to NBPI, Bib ref (147) Para 50.

29. Bib. ref (95).

30. Refer to chapter 8 for detailed information on franchisors, franchisees and their contractual arrangements.

31. See above, Para 3.73 for definition.

32. Not being the case with management licensees and some franchisees who were formerly direct employees of their franchisors.

33. In order to simplify the assessment of interactions, district managers have been omitted from the diagram and are not included as separate parties in the subsequent discussion. Their role and characteristics are assumed to reflect those of their employer, the franchisor.

34. No specific period is suggested, it varying according to the complexity of the operation and to the time taken by each franchisee to master it.

35. Stanworth, Bib. ref. (186).

36. 52 usable replies to self-administered questionnaires were returned to Dr. Stanworth by franchisees of the catering system examined, thus providing data from more franchisees than obtained by this researcher. However, responses to some questions showed inconsistencies with answers to previous related questions, and there was a high 'no response' rate to certain questions regarding, for example, financial performance. A further 20 catering franchisees were subsequently interviewed in depth by members of his research team.

37. See below, Chapter 10.

38. See Udell, Bib. ref. (206); Ozanne and Hunt, Bib. ref (159); Curry, Bib. ref. (48); Lewis and Hancock, Bib. ref. (120); Conference Board, Bib. ref. (40).
39. Particularly in Oxenfeldt and Kelly, Bib. ref. (151); Stephenson and House, Bib. ref. (187); Parker, Bib. ref. (160); and also see Thompson, Bib. ref. (198) pp 53 and 54; Curry, Bib. ref. (48) pp 19 – 22.

40. See below, Para 10.72.

41. For example, Mendelsohn, Bib. ref. (135); Izraeli, Bib. ref. (107); Curry, Bib. ref. (48); Lewis and Hancock, Bib. ref. (120); Vaughn, Bib. ref. (213).

42. Thompson, Bib. refs. (197) and (198); Conference Board, Bib. ref. (40); Lewis and Hancock, Bib. ref. (120); Curry, Bib. ref. (48); Izraeli, Bib. ref. (107); Hunt, Bib. ref. (100).

43. Some catering contractors are now expanding into the business of providing accommodation services.

CHAPTER 10

1. Drawn from the following main sources: Boursican, Bib. ref (9); Brown, Bib. ref (17); Conference Board, Bib. ref (40); Curry, Bib. ref (48); Downie, Bib. ref. (57); Hunt, Bib. ref (100); Izraeli, Bib. ref. (107); Kursh, Bib. ref. (115); Mendelsohn, Bib. ref. (135); Oxenfeldt and Kelly, Bib. ref (157); Oxenfeldt and Thompson, Bib. ref. (158); Ozanne and Hunt, Bib. ref. (159); Parker, Bib. ref. (161); Stanworth, Bib. ref. (186); Stephenson and House, Bib. ref. (187); Thompson, Bib. ref. (198); Vaughn, Bib. ref. (213);

2. For summary see schedule 10.1.


4. Spiegel, Bib. ref. (185).

5. The need for standardization amongst outlets of any given franchise system is inherent, but the degree of standardization is dependent upon the type of outlet and product. It is suggested that the extent of required standardization is a factor of the cost of the product and of the length of exposure of the consumer to it. For example, absolute conformity in all details is expected of a single product bought in a take-away outlet and purchased and consumed in minutes. Where a consumer is purchasing a twenty-four hour stay in an hotel, including accommodation and meals, greater flexibility is likely to be permitted within the franchised system in respect of products and services.

6. Stemming from the often quoted comment of John Y. Brown, head of Kentucky Fried Chicken in the U.S.A. "We'll make more profit from 300 company-owned stores than we will from 2,100 franchise outlets", cited in Burck, Bib. ref. (19) p.121.

7. For example, Izraeli, ibid, p.22; Mendelsohn, ibid, p.21 Vaughn, ibid p.29.
8. Except in some circumstances where a franchisor may benefit from a new multiple franchisee's established local goodwill, see para. 10.41.


11. Office of Fair Trading, Bib. ref (155). Note that some restrictive agreements are exempt, such as those concerning transportation, banking and professional services.


13. For summary, see schedule 10.2.

14. For summary, see schedule 10.3.

15. For summary, see schedule 10.4.

16. Particularly in Thompson, Bib. ref (198), pp.37 and 38; Lewis and Hancock Bib. ref (120) chapter 5; Stanworth, Bib. ref (186) pp. 17 and 18.

17. For summary, see schedule 10.5.

18. Hunt, Bib. ref (100) and Oxenfeldt and Kelly, Bib. ref (157).


20. The I.F.A.'s publication, ibid, was withdrawn following Criticism of Atkinson's misinterpretation of data, on which was founded the claim that franchising substantially reduced the rate of failure. This criticism was levied by Ozanne and Hunt, Bib. ref. (159) pp 68, 96 and 97. In addition to Atkinson's overstated figures of the general failure rates in businesses, the definition of 'failure' is open to widely different interpretation.


22. Oxenfeldt and Thompson, Bib. ref (158) suggest that franchising may not increase the overall number of people employed in independent outlets nor the overall investment, but merely leads to earlier employment and investment, and to the shift of such resources into different trades.

23. For example, the Government Committee of Inquiry on Small Firms, commonly referred to as the Bolton Committee, presented its report in 1971. See also Clarke, Bib.ref (37) and Brown, Bib. ref (18).

24. Ozanne and Hunt, opus cit, pp. 51 to 54.

25. One third of responding single franchisees in this survey were born outside Britain, see para 8.35. Statistics provided by Dr. Stanworth also reveal that some 36% of catering franchisees surveyed by him were born outside this country.

27. See for example, Vaughn, Bib. ref (216); Walker and Etzel, Bib. ref. (218); Downie, Bib. ref (57) and Sweeney, Bib. ref. (189).

28. Oxenfeldt and Thompson see note 22 above.

29. For a detailed analysis of tying practices amongst U.S. franchisors and legal decisions, together with an assessment of their pro- or anti- competitiveness, see Thompson, Bib. ref (198) chapters 6 - 8.

30. Thompson, Bib. ref (197) p.21.

Chapter 11
1. See above, Chapter 10.
2. See below, Para. 11.3 et seq.

Chapter 12
1. See above, Para 10.252.
2. See above, Para 4.42.
4. Quoted by Medlik, Bib. ref (133) p. 132.
5. See Monteguet, Bib. ref. (144)
6. See Bib. ref (85).
7. Franchising is already being used to a very limited extent in some of these types of outlets.
8. As demonstrated, for example, by the French franchised two star hotel system, Ibis, see Caterer and Hotelkeeper, 24 Feb 1977, p.11, and able to be introduced in systems similar to that mentioned in Catering Times, 16 Dec 1976, p.13.
9. Davey, Bib. ref (50).
10. For example, in Caterer and Hotelkeeper, 27 Oct 1977, an advertisement was placed by a major catering contractor for a manager to undertake conference management in hotels on a contractual basis.
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