



A Review on Hotel Operation Engagements in Turkey

Due to the increase of brand loyalty by consumers, the leading trend amongst global and big chain hotel business owners has been to turn over the running of their hotel operations. Rather than acquiring property and operating the hotel, global and big chain hotel owners prefer entering into (i) franchise/management, (ii) the build, operate and transfer (the “BOT”) or (iii) lease agreements to carry out their hotel operations.

The choice of model depends on the scale of investment by the hotel chain (the “**Hotel Chain**”). Most of the big chains do not prefer making long-term investments such as purchasing properties and operating the same in foreign countries; they prefer to enter into engagements such as lease, management or franchise agreements in order to operate a hotel business. The main reason for not operating a hotel as an owner is to minimize the exit risks from the relevant country.

Most land and building owners (the “**Hotel Owner**” or the “**Landowner**”), that are keen on getting into the hotel business in Turkey, also prefer leasing the relevant land or building or transferring the operation of management to third parties who have know-how and are also well-known in the hotel business. The main reason for this choice is to increase profits by using the brand name and the quality standards of the Hotel Chain.

The parties are free to determine the form of the agreement for the operation of the hotel based on their commercial standing. It could either be a management agreement, franchise agreement, BOT model or a lease agreement. Every contract has pros and cons for each respective party. Below is a brief explanation regarding the advantages and disadvantages based on the relevant party and the type of the contract.

I. Lease Agreements¹

Running a hotel business through leasing a building is very similar to ownership, in terms of the Hotel Chain’s liabilities. The Hotel Chain basically rents a building, runs the entire operation and simply pays the rent every determined term as defined in the relevant lease agreement. The opportunity to annotate lease agreement in the relevant land registry record is a great advantage for Hotel Chains. Annotation of the lease protects the Hotel Chain from eviction in the event of the sale of the leased property to third parties by the Hotel Owner. On the other hand, by leasing the building and operating the hotel, in its capacity as the employer of the employees within the relevant hotel, the Hotel Chain is responsible to ensure compliance with the labor legislation. In this respect, all the possible labor law related claims are attributable to the Hotel Chain in the lease model.

¹ The terms and conditions of lease agreements are defined under the Turkish Code of Obligations (the “TCO”). However, as a result of the freedom of contract principle, on most issues, the parties are free to agree to provisions that fall contrary to the provisions of the TCO. The provisions of the TCO are applied to matters not agreed upon between the parties.

If the main goal is to avoid getting involved in the hotel management business, then Hotel Owners prefer to lease out their relevant property.

II. BOT Model

The BOT model is also a common model of engagement between mostly public sector Landowners and the Hotel Chains. In this model, the legal relationship between the parties is based on the lease, construction and management of the hotel. The Hotel Chain leases the land in order to build the hotel as per the pre-determined specifications and operate the hotel for a certain period of concession and return the hotel to the owner at the end of the concession term. Since the BOT model is an option for financing the infrastructure and boosting the economic growth of Turkey without the direct utilization of government funds, the public sector mostly prefers this model.

III. Management and Franchise Agreements

Management and franchise agreements are contracts between a Hotel Owner and Hotel Chain under which, for a fee, the Hotel Chain operates the hotel.

Under Turkish law, management and franchising agreements are categorized as *sui generis* contracts. In this respect, unlike lease agreements, the parties to these agreements are not granted certain rights and obligations by the applicable legislation. Accordingly, these agreements are fairly voluminous documents that incorporate access to the brand and the operator based functions related to the hotel.

From a legal point of view, a franchise agreement and a management agreement seem quite similar since they both rely on a license and service relationship. However with a management agreement, the Hotel Owner also provides a comprehensive mandate to the Hotel Chain in order to carry out all day-to-day business operations and also provides access to its accounts. The mandate issue is the main distinction between these agreements from a legal point of view.

From a commercial point of view, the demand of control of the Hotel Chain and Hotel Owner affects type of agreement and the fundamentals of each agreement lie in the level of control either party maintains during the relationship. As a result of transferring the control and certain liabilities to the Hotel Chain, management agreements are less profitable but more convenient for the Hotel Owners than franchise agreements.

In both the franchise agreements and management agreements, the Hotel Chain is obligated to provide (i) know-how utilization in the relevant business system and integration of products and/or services; and (ii) uniform appearance of trademarks and logos on business items.

As per the differences between these agreements, under a franchise agreement, the Hotel Owner is independent from the Hotel Chain and can act on its own behalf and for its own account. However, under a management agreement, the Hotel Owner is completely dependent on the Hotel Chain by authorizing the Hotel Chain to act on its own and on behalf and for the Hotel Owner's account. The Hotel Owner loses its control over the business under a management agreement and the Hotel Chain carries out all day-to-day business with respect to the hotel, as opposed to a franchise agreement.

Moreover, the Hotel Owner is required to pay the Hotel Chain a certain royalty fee plus a service fee under a management agreement whereas it is only obliged to pay a royalty fee

under a franchise agreement. Last but not least, the Hotel Chain is obligated to increase the profitability of the business under franchise agreements, whereas there is no such obligation under management agreements.

The separation of ownership and operation in the hotel business is a new global trend. As an emerging market, the effects of the new global trends in the hotel sector are directly reflected in Turkey. Since all the globally used legal forms in order to create separated relationship are available under Turkish law, the parties are free to choose one depending on their commercial standing.

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