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TAKE-HOME POINTS

By the time you've finished reading this article, you should be able to:

- ✓ Identify key contractual considerations that need to be addressed when contemplating a business relationship with a hotel.
- ✓ Describe aspects of guest service that should be clarified in negotiations, regarding which party is responsible for what.
- ✓ Explain the unique challenges of working with a hotel that has a collective bargaining agreement with its employees.



Bed & Board

A growing number of hotel owners and management companies are looking to independent restaurants, often operated under well-known brands or by renowned chefs, to provide alternatives to the hotels' own foodservice. These restaurants are frequently marketed as much to residents of the local community as to hotel guests and, when possible, have their own street-fronting entrances in addition to entrances through hotel lobbies. High-end examples of such restaurants include Adour by Alain Ducasse at the St. Regis Washington, D.C., WP24 by Wolfgang Puck at the Ritz-Carlton Los Angeles and Emeril Lagasse at the Loews Miami Beach in Florida. In some cases, independent restaurant operators are recruited to operate a hotel's only restaurant.

The Opportunities and Challenges of
Entering Into a Restaurant Operations
Relationship With a Hotel

By Robert W. Lannan

Having a well-known, independent restaurant in a hotel can enhance a hotel's image, and give potential new guests a glimpse of the hotel. (An old technique employed by hotels that operate restaurants of their own has been to omit separate restrooms from the restaurants themselves, to force patrons to walk across attractive hotel lobbies to reach the facilities.) The relationship can work to an independent restaurant's benefit as well if the hotel is well-regarded. Moreover, the hotel can be a built-in source of a steady flow of patrons for the restaurant, especially on weeknights when it might otherwise operate below its full capacity.

However, at the earliest stages of exploring this type of opportunity, there are business and legal issues that all parties involved should consider, which are unique to operation of an independent restaurant within a hotel. Many of these issues also apply to independent operation of bars, nightclubs, casinos, music venues and other independent food, beverage and entertainment businesses within hotels. However, for the sake of efficiency, I will refer in this article only to independently operated restaurants.

Who is Contracting With Whom, and Under What Kind of Contract?

The very first of these issues is likely to be which parties will be making the contract for an independent restaurant to operate in a hotel, and what kind of contract (or contracts) they will be. If the hotel owner and manager are different entities, one or the other may be more interested in the arrangement. If the hotel owner is driving the deal, it may in the end be party to two management agreements: one with the restaurant operator and the other with the hotel operator. Instead of the management agreement, the hotel owner and restaurant operator may wish to enter into a commercial lease. A commercial lease is a better option for a restaurant operator who wants more autonomy and unqualified ownership of his business.

If the hotel management company is interested in contracting with an independent restaurant operator, the most appropriate contract may be an independent contractor agreement between these two management companies. Of course, the existence and content of this contract will have to be consistent with the management agreement between the hotel management company and the hotel owner, and the hotel owner's approval may be required.

Regardless of how the deal is structured, all three parties — the hotel owner, the hotel management company and the restaurant operator — will need to be aware of the content of the hotel management agreement, any agreement between the hotel and a franchisor, and any other agreements that may affect their discretion. The parties will need to ensure that the content of these agreements does not stand in the way of the restaurant deal, and that the terms of the deal are drafted to avoid unnecessary conflict. This may become tricky if these existing contracts include confidentiality clauses. Without the consent of the other parties to the existing contracts, the new restaurant operator may never have

an opportunity to review the contracts themselves. Even with such consent, this review will likely need to be done under a carefully drafted confidentiality agreement.

Although an arrangement for independent operation of a restaurant in a hotel may require more than one contract (and indeed these contracts may be signed by more than two parties), for the sake of simplicity in this article I will refer to the set of documents underlying the relationship as "the contract." Likewise, I will refer to the hotel owner and hotel management company collectively as "the hotel" and, to the extent applicable, any separate restaurant owner and management company collectively as "the restaurant."

Build-Out Costs and Later Fees

One of the first subjects a hotel and restaurant may need to address is the sharing of any investment costs and/or compensation between these parties. If the restaurant has a powerful brand and is likely to enhance the image and popularity of the hotel, the restaurant may be in position to demand that the hotel cover a greater portion of the restaurant build-out costs. When purchasing fixtures, furniture and equipment for the restaurant, the parties' respective shares of the cost will likely depend largely on which party will own this property. To the extent that these are treated fixtures to the real estate and therefore owned by the hotel owner, it is likely that the hotel will have to make a significant contribution to their cost. Regardless of which party is responsible for the restaurant build-out costs, the hotel may demand some input in the design of the restaurant, to ensure consistency with the design and image of the hotel. The level and timing of the hotel's input should be specified in the contract.

If the hotel is expected to provide the restaurant customers that it would not otherwise receive, the hotel may be in a position to demand some concession fee from the restaurant, probably measured as a percentage of gross revenues or profits. Conversely, a restaurateur may be in a position to demand fees from the hotel, especially if (as discussed later) a collective bargaining agreement at the hotel or other circumstances requires the hotel to be the restaurant operator, with a high degree of input and involvement from the restaurateur.

Accommodating Hotel Guests

The parties will also need to address accommodations unique to hotel guests that the restaurant may be required to make. First and foremost, hotel guests will expect to be able to charge their restaurant bills to their guestroom accounts. Even if the hotel and restaurant accounting systems are otherwise run entirely separately, the parties will need to negotiate an accommodation to make this possible.

If the independent restaurant will be the only one in the hotel, there will be several more issues to address. The hotel management company will likely need the agreement to clearly address responsibilities for room service and breakfast. For many restaurants, it is difficult to make money serving breakfast. However, breakfast is something that business and leisure hotel

guests demand, and they have very specific expectations about what will be served, when it will be served and how much it will cost. If the hotel is part of a brand system, the system may also impose brand standards on this subject. Often these expectations and standards clash with the theme of a high-end restaurant. These are issues the parties will need to address while the contract is negotiated.

Room service presents additional issues if an independent restaurant is to be the only one in a hotel. What items should be on the room service menu? At what hours should room service be available? Here, again, hotel guests have certain expectations and hotel brand standards often impose specific requirements. Both the hotel and restaurant operator should come to a clear understanding of which standards the restaurant will accommodate. Another issue is which employees will deliver the food from the restaurant to guestrooms. Often this will need to be employees of the hotel — not the restaurant. Because of an innkeeper's unique legal responsibilities to provide for the security and privacy of hotel guests, hotels will be (and indeed should be) reluctant to provide regular access to guestroom corridors and guestrooms to another company's employees.

Catering events in ballrooms and meeting rooms is another issue altogether. Here, especially if an independent restaurant is the only one in the hotel, the restaurant's employees will need to have access to common spaces in the hotel, and the hotel will need assurance that the restaurant has capacity to accommodate such events.

For a very popular restaurant, another accommodation that the hotel may seek for its guests is for the restaurant to keep a certain number of seatings in reserve for hotel guests, who are less likely to book reservations well in advance. Before the restaurant opens, it will likely be too difficult to anticipate demand from either the surrounding community or hotel guests to agree upon specific numbers. However, the contract can require the hotel and restaurant to consider the levels of demand over the first several months and then to negotiate in good faith toward a reasonable accommodation that will enable some level of availability to hotel guests without costing the hotel revenue.

Employment Considerations

Other issues that the parties will need to consider relate to the restaurant and hotel employees. One of the first questions the restaurant operator should ask is whether the hotel's workforce is unionized and, if so, which requirements of the collective bargaining agreement (CBA) will affect the restaurant's operations. The CBA may altogether prohibit anyone but members of the bargaining unit from working below management levels at a restaurant located in the hotel, even though the restaurant is independently operated.

This requirement in a CBA may complicate a deal for an independent restaurant in a hotel, but does not have to kill it. The contract can provide for hotel employees to work at the

Public Relations and Marketing Issues

Independent restaurants and hotels seeking to collaborate under one roof need to address use of one another's names and trademarks in marketing and public relations. Especially if both the restaurant and the hotel operate under well-respected names, each is likely to want to make reference to the other in marketing materials. This will begin with announcements about the restaurant even before its opening date, and continue in marketing efforts afterward. The contract should indicate whether either party will be permitted to use the other's trademarks and possibly address the broad circumstances under which this will be allowed. However, the contract also should give each party a right to review and approve in advance any materials that the other party proposes to use that include the former party's trademarks. The contract may require the parties to cooperate and act in good faith within this process, but it is unlikely that either party will (or should) give up its right to veto any use of its trademarks that it finds objectionable. A distinct but related set of issues extends from signage inside and outside of the hotel that refers to the restaurant. The restaurant is likely to want some signage, at least outside of the building, to show patrons and potential patrons that it is there. It may also want promotional signage to appear in hotel elevators, in-room directories and even tent cards placed in guestrooms or at the front desk. The contract itself should clearly address what outside signage is permitted. It should also anticipate whether any inside signage may be used and require the parties to agree in writing on what will be allowed from time to time as the parties' needs change, and who will be responsible for related costs.

restaurant under the supervision — or quasi-supervision — of restaurant employees. I use the term "quasi-supervision" because it may be necessary for these employees to continue reporting to a hotel manager who coordinates with restaurant management and touches base with the employees periodically. If hotel employees are to be supervised by restaurant managers, the hotel will likely want some input in the restaurant's recruitment and selection (and, if necessary, the termination) of these managers. The restaurant also should be bound to strict confidentiality in employment matters, and its management employees should be required to adhere to any code of conduct the hotel may have that governs relations with employees. To the greatest extent possible, all of these procedures should be specified in the contract and not left to later agreement of the parties.

An arrangement for joint supervision of hotel employees sounds rife with possibilities for complications and conflict, and indeed it is. However, the arrangement also has one

Who is Responsible for What?

An important subject for a restaurant and hotel to begin discussing early on when contemplating a business relationship is which party will be responsible for performing which hospitality functions on the premises of the restaurant and elsewhere within the hotel. For example, will the restaurant operate under its own liquor license, or will it need to rely on the hotel's liquor license, especially during the first few months while it may be applying for its own? Who will be responsible for ensuring that the restaurant receives utility services and who will pay for these services? Often the hotel is responsible for bringing heat, electricity and water to the restaurant as part of the larger physical plant of the hotel; however, "submeters" are installed to measure the restaurant's use of these utilities so that the hotel can be reimbursed. Likewise, who is responsible for cleaning and routine maintenance of the restaurant premises? Who is responsible for ensuring the security of the premises?

If the independent business is not a restaurant but a bar, nightclub or music venue, will it offer its guests some limited foodservice? If it does, who will be responsible for preparing the food? Who will be responsible for serving the food? Particularly, if the independent business is a music venue, who will be responsible for serving the drinks?

key advantage: It allows for greater flexibility in staffing. During periods of low demand at the restaurant, there may be other duties in the hotel that the employees can perform (especially if there is another restaurant managed by the hotel). During periods of high demand, there will be a pool of trained employees of the hotel from which the restaurant manager can draw.

If the CBA prohibits independent operation of any food outlet within a hotel and the union will not agree to an exception, the parties' options are obviously more limited. One strategy that could allow an independent-branded restaurant to operate on the premises would be for the hotel to operate the restaurant as a franchise, with a consulting agreement with the would-be restaurant operator. However, this arrangement would add the expense of franchise and consulting fees, and undoubtedly many restaurant operators would not be interested in giving direct control of management of one of their restaurants.

If the restaurant has employees separate from those of the hotel, one issue that the parties will need to address is which employees of each party will have what access to the premises managed by the other. For example, in the likely event that the hotel will demand that only its employees can make room service deliveries from the restaurant to guestrooms, there will need to be a clear

understanding of where in the restaurant premises these employees should go to pick up orders. If the restaurant will be catering events in hotel ballrooms and meeting rooms, a similar understanding will need to be reached for restaurant employees to access them. Related issues include which entrances the employees should use, and whether deliveries within the premises should be made by back-of-the-house routes, including which elevators the employees should use. I am aware of one instance in which a hotel has negotiated with the independent operator of its only restaurant terms under which hotel employees can use a breakroom and refrigerators in a "back of the house" area of the restaurant.

While the parties' contract should anticipate procedures like these, it probably is not the best place to outline these procedures. Rather, the contract should require the parties to specify these procedures in a separate writing that can be more easily changed from time to time as needed. The contract might also require the hotel and the restaurant to make good-faith efforts to resolve these kinds of issues as they surface.

Interaction Between the Two Management Companies

The contract should contain some provision for formal interaction between the restaurant and hotel to address common issues related to their management. At the very least, it should require representatives of the two businesses (probably the general manager of each) to meet at least monthly to address these issues in good faith. On the opposite end of the spectrum, depending on the level of its bargaining power, a hotel could demand that the restaurant submit an annual business plan for the hotel's review and comment, followed by periodic reports on the restaurant's performance against the plan and a right to conduct audits.

In the likely event that the hotel guests are permitted to charge restaurant bills to their guestroom folios, and the hotel forwards payments it collects to the restaurant, each of the parties will likely want the contract to provide some right to audit the other's records related to these transactions. These audit rights will likely also extend to common maintenance expenses and any utility costs passed by the hotel to the restaurant.

Anticipate and Address

Opening an independent restaurant under a well-known brand in a respected hotel can be a great opportunity for both the restaurant and the hotel. However, with this opportunity comes challenges that are unique to this arrangement, which the restaurant would not have to face if it opened in another kind of building or in a free-standing building of its own. To make the most of this opportunity and avoid later conflict, it is important for the parties to anticipate these issues and ensure that they are addressed and resolved in contracts and/or other documents before commitments are made and money is invested in the venture.

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