Restaurant License & Consulting Agreements with Celebrity Chef Companies for Restaurants in Hotels

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Over the past decade, many hotel owners and management companies have looked to independent restaurant concepts—often associated with celebrity chefs—to increase revenue and enhance hotels' images and guests' experiences. One way to do this is to lease space to a celebrity chef's company (a "ChefCo") and allow the ChefCo to operate the restaurant independently. A similar approach is for the hotel owner to enter into a management agreement with the ChefCo—separate from the management agreement with a hotel management company for the rest of the hotel. A third approach is for the hotel management company to subcontract management of the restaurant to the ChefCo. Under each of these alternatives, the ChefCo operates the restaurant, whether or not it owns it.

A "Restaurant License & Consulting Agreement" is an alternative to the above approaches in which the hotel management company (whether or not it is affiliated with the owner) operates the restaurant pursuant to a license from the ChefCo, and with the ChefCo's advice. This approach can be preferable to the others for both the hotel owner and management company because it retains more revenue and profit for the hotel. A ChefCo will prefer this approach if it does not wish to invest in owing or assume the responsibilities of managing a new restaurant, but is looking for a new stream of revenue from use of the celebrity chef's name, recipes and other concepts. The ChefCo may enter into a Restaurant License & Consulting Agreement with either the hotel owner or an independent hotel management company.[1] Because the interests of the two hotel companies in relation to ChefCo are generally aligned, the remainder of this article will refer to the hotel owner and management company together as the "Hotel."

As its name indicates, under a Restaurant License & Consulting Agreement[2], ChefCo provides both a license and consulting services to the Hotel. The ChefCo licenses its brand and/or sublicenses the name of its celebrity chef to the Hotel for use in marketing and operation of the restaurant. The ChefCo also licenses its recipes, designs and thematic concepts for the Hotel to use. Meanwhile, the ChefCo trains Hotel personnel and provides other consulting services to ensure that the restaurant operates consistently with the ChefCo's brand and concepts. All of this is in exchange for a series of fees, mostly based on the restaurant's revenue and profit.

This article discusses the relationship between a Hotel and a ChefCo under a Restaurant License & Consulting Agreement, and summarizes provisions that a Hotel should expect or seek in such a contract.[3]

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[1] The factors determining which of these hotel companies should enter into the contract with ChefCo are beyond the scope of this article.

[2] These contracts can and do have titles other than "Restaurant License & Consulting Agreement." I prefer this title because it captures the most essential components of the contracts.

[3] In several instances, the article states that a Restaurant License & Consulting Agreement "should" address a topic one way or another. Whether a Hotel is able to negotiate one of these provisions will ultimately turn on its bargaining

Is it a Franchise?

A Restaurant License & Consulting Agreement has many elements in common with a franchise agreement. Depending on the content of the contract, the parties' relationship may meet the definition of a "Franchise" under federal law in the United States.[4] However, Restaurant License & Consulting Agreements usually do not identify themselves as franchise agreements. In fact, a ChefCo may demand that the contact expressly disclaim any franchise relationship, possibly because the ChefCo may not have complied with disclosure requirements for franchising under applicable laws.[5]

If a ChefCo disclaims a franchise relationship (and/or fails to comply with applicable disclosure laws), a Hotel pursuing a Restaurant License & Consulting Agreement should use this distinction to its advantage to avoid an undue amount of control by the ChefCo in the relationship.[6] If a ChefCo demands rigid compliance with multiple and minute "system standards," it can be reminded that this is not a franchise agreement. Moreover, if the restaurant will be only the second or third one to operate under the celebrity chef's name, it is unlikely that a true "system" exists. The lack of a franchise should give the Hotel an opportunity to negotiate a contract that tailors the ChefCo's concepts and expertise to meet the particular needs of the Hotel and its guests, even if this results in a restaurant that is different from the ChefCo's others.[7]

Development of a Restaurant Concept

A ChefCo's opening responsibility under a Restaurant License & Consulting Agreement is to develop a thematic concept for the restaurant in consultation with the Hotel. The concept does not have to be identical to those of the ChefCo's other restaurants, and should blend well with the Hotel's image.

Front-of-House Design. The ChefCo will likely design most or all of the "front of the house" space of the restaurant. The contract should include an exhibit identifying exactly where in the Hotel the restaurant will be located. It should also include an estimated development cost, and either an itemized budget or an agreement to negotiate a budget based on the estimate. The ChefCo will likely demand that the Hotel acknowledge that the designs (along with the receipes,

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power in relation to that of the ChefCo. The provisions recommended in this article are both advisable and reasonable for a Hotel to demand in a negotiation.

[4] *See* 16 CFR 436.1(h). Because the United States has a well-developed body of franchise law that imposes stringent requirements on franchisors, some Restaurant License & Consulting Agreements for restaurants outside the United States would be subject to regulation as franchises in the United States.

[5] A "ChefCo" considering whether to pursue a Restaurant License & Consulting Agreement with a Hotel or independent restaurant owner should consult with an attorney on whether applicable laws require franchise disclosure for the relationship the ChefCo has in mind.

[6] Under federal law in the United States, one of the defining elements of a "Franchise" is an expectation that "[t]he franchisor will exert or has authority to exert a significant degree of control over the franchisee's method of operation, or provide significant assistance to the franchisee's method of operation." 16 CFR 436.1(h)(2).

[7] On the flip side, the Hotel should be counseled that if the ChefCo does not hold itself out as a franchisor, it may not have disclosed as much information about itself as it otherwise would in a franchise disclosure document. However, a Hotel can compensate for much of this by conducting its own due diligence on the ChefCo.

brands and other concepts) are ChefCo's intellectual property, to be used by the Hotel under a license. Of course, the Hotel should be assured that the ChefCo indeed owns all of this intellectual property and that nothing prevents the ChefCo from licensing it as done in this contract. This can be done through a series of representations, warranties and indemnifications in the document.

At the same time, the Hotel should ensure that the licensed designs expressly exclude elements that the ChefCo does not own: the restaurant's general color scheme, as well as fixtures, furniture and equipment (FF&E) or operating supplies that are not specially designed. (As will be noted later, the same applies to any items that appear on the menu but were not developed by the ChefCo.) If the parties' relationship is not successful and the contract is terminated early, this extra language will save the Hotel from having to abruptly replace everything in this space (and on the menu).

Back-of-House. The contract should clearly identify which kitchen area(s) in the Hotel will serve the restaurant and whether the Hotel will be permitted to use the same kitchen facilities to support any other food and beverage outlet in the hotel.[8] It should identify any particular FF&E the Hotel should procure for this space (consistent with an agreed-upon budget).

Menu Selections. The ChefCo's expertise is most needed to develop and select items for the restaurant's menus. The ChefCo will claim ownership of the recipes for the signature items in the menus. However, as with the more basic design concepts for the front-of-house space, the Hotel should add language to ensure that this ownership does not extend to everything. The contract should exclude from the ChefCo's ownership any items of a general nature that could be found on the menu of many restaurants (e.g. filet mignon). The Hotel should also consider whether it needs this restaurant to provide foodservice for breakfast, room service and/or catered events in meeting rooms outside the restaurant space. If the Hotel needs this restaurant for these purposes, it should require the ChefCo to develop menus to serve these needs in consultation with the Hotel.

Staffing Plan. The contract should also require the ChefCo to work with the Hotel to develop a staffing plan for the restaurant, including positions to be filled, the number of people required for each position and expected hours for each.

Restaurant Name and Marks. The ChefCo should be required to develop a name and trademarks for the restaurant, in consultation with the Hotel. (This assumes that the ChefCo will not use the same name and trademarks it uses for another of its restaurants.)

Signage. The parties should be required to develop and agree on signage in the Hotel (including in materials placed in guestrooms) directing guests to the restaurant.

Timeline. The contract should set out a timeline in which the ChefCo must finish developing the restaurant in consultation with the Hotel.

Operating Manual. The contract should require the ChefCo to develop an Operating Manual for the restaurant in consultation with the Hotel, and to provide the Hotel a complete copy

[8] If there are other restaurants in the Hotel (or if the Hotel wishes to reserve the right to add any), the contract should also clearly state that the restaurant operating under the ChefCo brand will not necessarily be the only one in the Hotel.

of the Operating Manual. The "Operating Manual" consists of all requirements that the Hotel must follow to operate the restaurant according to the ChefCo's standards. The contract should provide that any components or additions to the Operating Manual must be expressly identified as such.

Licensing the Restaurant Concept

The Restaurant License & Consulting Agreement will grant the Hotel a license to operate the restaurant with the theme, concepts, designs and menu items developed by the ChefCo throughout the term of the contract. The Hotel should ensure that this license is exclusive to the Hotel's restaurant within a specifically defined territory. If possible, the Hotel should demand that this protection extend to a broader range of similar restaurant concepts within this territory.

Pre-Opening Assistance

After the restaurant has been designed, the Hotel will rely on the ChefCo's expertise to help the Hotel implement the designs and prepare to open the restaurant.

Oversight of Restaurant Development. The contract should require the ChefCo to provide oversight during construction of the restaurant space. The ChefCo will likely demand an opportunity to inspect the entire premises and sign-off before the restaurant is allowed to open. The Hotel should welcome this involvement, as long as the ChefCo's sign-off on opening cannot be unreasonably withheld, conditioned or delayed.

Hiring Key Personnel. The staff plan discussed above will likely identify positions in two categories: key personnel and all other restaurant employees. Key personnel will include the head chef and sous-chefs, front-of-house restaurant managers and possibly others. The ChefCo will likely demand some involvement in the selection (and later replacement) of all key personnel. This may include opportunities to interview them and/or a veto on their selection. It may also include some input in how much they are compensated.

Initial Training. One of the most important pre-opening contributions of the ChefCo is training of key personnel and other restaurant employees. Ideally this should all be done on-site. However, the ChefCo may demand that some key personnel also receive training at one of its other restaurants. The number of ChefCo representatives who will perform training and the number of days of training (both on-site and off-site) should be specified in the contract. If off-site training is required for key personnel, the Hotel will likely be responsible for their travel expenses. However, there should be no fees (beyond the Initial Fee discussed below) for the initial training.

Pre-Opening Events and Grand Opening. The contract should expressly require participation of the celebrity chef himself or herself at a specified number of pre-opening promotional events (possibly including a "soft" opening) as well as a grand opening event.

Continuing Assistance

The Restaurant License & Consulting Agreement will also impose requirements on both parties related to ongoing operation of the restaurant after it has opened. One challenge for a Hotel at this stage can be continuing a sufficient level of involvement of the celebrity chef himself or herself in the ongoing promotion and enhancement of the restaurant. This should be addressed by requirements in the contract.

Marketing. The contract should address the parties' duties related to marketing of the restaurant. Usually, marketing specific to the Hotel's restaurant is controlled by the Hotel (with input from the ChefCo) at the Hotel's expenses, while general marketing of the ChefCo's brands and group of restaurants is controlled by the ChefCo at its own expense. The same is true of the restaurant-specific website (which will likely require the ChefCo's approval) and the ChefCo's general website. The contract should address each party's rights and restrictions with respect to use of the other party's names and trademarks. The contract should also require the celebrity chef to be present at the Hotel restaurant for a specified number of days per year for promotional events. (The Hotel may be responsible for travelling expenses of ChefCo personnel after the restaurant opens.)

Ongoing Training. The contract should also require a specified number of ChefCo personnel to conduct training sessions at the Hotel over a specified number of days per year throughout its term. This training will be primarily directed to new employees. The ChefCo may require new Key Personnel to receive additional training off-site. In addition to this periodic training, the ChefCo may demand an opportunity require additional training when it believes this is necessary. Unlike the pre-opening training sessions, the ChefCo is likely to demand additional fees for post-opening training (both scheduled and unscheduled). Particularly if the ChefCo is able to compel unscheduled training, the Hotel should demand that the contract limit the expense of these training sessions. While a reasonable amount of post-opening training will be helpful to the Hotel, it should not become a significant source additional revenue to the ChefCo.

Inspections. The ChefCo will likely demand an opportunity to conduct both front-of-house and back-of-house inspections of the restaurant throughout the term of the contract. The contract should expressly limit the number of inspections during any year. Back-of-house inspections should require a reasonable amount of advance notice, and should be escorted. For front-of-house inspections, the ChefCo may demand an opportunity to send "ghost shoppers." It may also demand an opportunity, unannounced, to take food samples for laboratory testing.

Fees

Restaurant License & Consulting Agreements typically provide for the Hotel to pay the ChefCo three primary types of fees:

Initial Fee. The contract will likely require the Hotel to pay the ChefCo a fee for all of its services prior to the opening date of the restaurant. This is usually a substantial fee. (For a high-end restaurant, an initial fee of between $250,000 and $500,000 is not unusual.) At least part of this fee is likely to be due upon the signing of the contract. The balance may be due after the restaurant opens.

Base Fee. Throughout the term of the contract, the Hotel is typically required to pay the ChefCo a base fee equal to a percentage (between 4% and 6% is common) of the restaurant's gross revenue from sale of concept foods. For sales of non-concept items (the filet mignon in the above example), the Hotel might demand that the base fee be lower. *Alcohol sales should be excluded completely from calculation of base fees, unless they are from sales of signature drinks developed by the ChefCo*. Especially if the potential for incentive fees (discussed below) is limited, base fees may be payable on a graduated scale, in which the fee percentage increases when revenue thresholds are reached during any year of the term.

Incentive Fees. The contract typically also requires the Hotel to pay the ChefCo an incentive fee equal to a percentage of the restaurant's profit from food sales. The percentage fee may start at ten percent or less on the first dollar of profit, and possibly increase with profit thresholds on a graduated scale over a year. Alternatively, the incentive fee may not begin until the Hotel's profit exceeds a preferred rate of return on its total investment in the restaurant. If the Hotel is allowed such a preferred rate of return before there can be an incentive fee, then this fee is likely to begin at a higher percentage rate when it becomes payable.

Term, Termination and Post-Relationship

A Hotel should expect a Restaurant License & Consulting Agreement to have an initial term of at least four years. If the ChefCo pays for a portion of the restaurant development or waives all or a substantial part of its initial fee, a longer initial term should be expected (along with higher base and incentive fees). The Hotel's written consent should be required for any renewal of the contract. Renewal should not be automatic or at the ChefCo's option.

The Hotel should have the option to terminate the contact before the end of its term for specified causes, which should include:

- Death, incapacity or misconduct (e.g. conviction of crime) of the celebrity chef
- Poor performance of the restaurant (as measured by a specified performance target) after a specified ramp-up period
- Uncured default in performance of the ChefCo's obligations.

Upon termination of the contract, the hotel will be required to immediately cease using the ChefCo's name, trademarks, recipes and other proprietary concepts. However, it should be able to operate a restaurant in the same location with a more general theme.

If a Hotel terminates a Restaurant License & Consulting Agreement without cause before the end of its term, it is usually required to pay the ChefCo liquidated damages estimated to equal the fees it would have earned over a specified period of time less than the full-remaining term.

Proceed Carefully

A Restaurant License & Consulting Agreement can be an effective way for a Hotel to garner the expertise and image of a renowned celebrity chef while retaining most of the profits from operating a successful restaurant that enhances the hotel's reputation. However, this is a contract that must be negotiated carefully, with the advice of a business consultant familiar with the local market and experienced legal counsel.