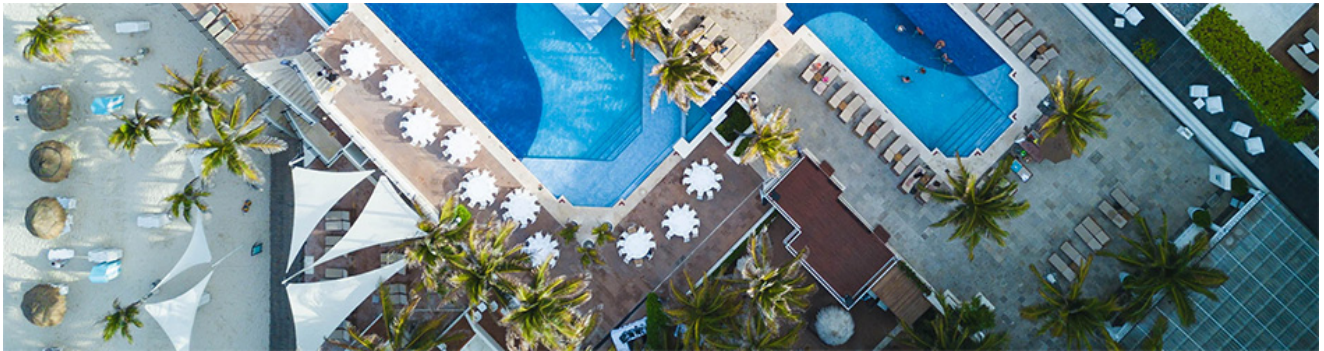


HUNGARY

Hotel Management Agreements



Introduction



One cannot discuss the evolution of hotel management agreements (HMAs) without first talking about the separation of hotel ownership and hotel operations; a transformation of the major chains' business models, more commonly known as an "asset light" strategy. Today the form taken by hotel operators in HMAs is an important factor in the effective working of the market in hotel investment. DLA Piper's Hospitality and Leisure Sector Group has negotiated HMAs for a myriad of different clients across the H&L landscape (owners, investors, operators (both branded and white label) and lenders) in all of the world's key jurisdictions.

Many consider hotel management agreements to be borne out of a modified lease for the Hong Kong Hilton back in 1963, and the main terms included in it underpin most HMAs to this day. All major chains today have, to one degree or another, expanded nationally and internationally through a combination of franchise and management, and all have their own "form" or template agreements. In summary, over the last few years, we have found that trends that started as a result of the financial crisis of the last decade have continued to develop. In many markets the advent of recession made operators more risk averse. Traditionally HMAs were a means to limit operators' exposure to fixed rental payments when revenues were dropping. In less developed markets, even with a degree of economic recovery, operators have continued to use HMAs in this way. In more developed markets, such as Spain and the United Kingdom, we have seen increased complexity in agreements, a symptom of owners becoming more knowledgeable and seeking more control and input on the operation of their hotel, although owners continue to take the lion's share of commercial risk in developments.

Another important factor, as with any real estate investment, is the attitude of those who are providing the money, be it equity or debt. Leases were the traditional mainstay of hotel developments and indeed Germany remains a country where hotel deals are commonly based around leases. However, as investors have started to see the increased returns from ownership, the boom in arrangements like ground leases and other market changes is essential to have an understanding of investors and be able to work with them in a scenario of increasingly complex legal arrangements.

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Hungary

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General

Are Hotel Management Agreements (HMAs) common in the jurisdiction?

HMAs are frequently used in Hungary for city center, upper tier hotels under a brand.

If not HMAs, what are the alternatives / what is commonly used?

Lease and franchising are the two other alternatives.

Is it common or usual for the HMA to be governed by (i) local laws; (ii) the laws of one of the parties' country of incorporation; or (iii) an alternative jurisdiction?

Either Hungarian law or the laws of one of the parties' country of incorporation is used for HMAs.

Are there any significant or unusual points to note in respect of tax on HMA payments in the jurisdiction?

This depends on the parties' country of incorporation and applicable taxation treaties.

Term and termination

Is there a standard contract period of an HMA?

The standard is 10-20 years with extension options.

Is the term usually fixed? Are early exit or similar options included (contractual or implied)?

Terms are usually fixed. In some cases an early exit option is included and always subject to an early termination fee.

Is it usual to include fees / liquidated damages for early termination?

Yes.

What is the usual position in respect of renewal?

Usually operators have an option to extend the term by five or ten years.

Fees

Is there a standard fee structure for HMAs (eg base + incentive)?

Usually there is a base fee calculated on revenues and an incentive fee based on profits.

What other fees and charges are there (such as royalties, accounting, marketing, license fees, etc.)?

Royalty fees and group services fees are usually charged for brand use, marketing, central booking, bookkeeping and other group services.

Are owners typically required to set aside funds for fixtures and fittings?

Yes, FF&E reserve is very common and is usually calculated on revenues. The percentage and the use of the FF&E reserve depends on the age and the brand of the hotel.

Performance and operations

What is the usual standard imposed on an operator in respect of the operation of the hotel?

Some HMAs contain KPIs or some other form of service level requirements; however, in most cases none of these are used since the fee structure ensures that the interests of the parties are aligned.

What performance measures are commonly used in the jurisdiction?

RevPAR against a competitive set of local similar hotels or performance against annual budget.

Is an operator or owner guarantee common in the jurisdiction?

For established brands, an operator guarantee would be very unusual, owner guarantee is also rare and usually limited to cases where there is a substantial financing on the property.

What is the usual position in respect of employees? With whom does the liability for the employees sit?

Usually the owner is the employer.

Is it usual to have a non-compete clause, eg that no other property with that brand can open within a certain radius?

Non-competes are standard.

Who is responsible for insurance?

The owner is responsible for property insurance (real estate plus FF&E), while the operator is responsible for third-party liability insurance and operational insurances.

Does the HMA give rights in real estate in the jurisdiction?

No. If a right of first refusal or purchase option is agreed over the property for the operator in a separate agreement, then those can be registered on the title of the hotel.

Does the HMA need to be recorded against the property, if this is possible in the jurisdiction?

HMAs cannot be recorded in the land registry, right of first refusal or purchase option right can be registered if granted.

Where financing is taken, is it standard to obtain a Non-Disturbance Agreement (NDA) as part of a management or lease agreement?

Yes, an NDA is usually obtained if the property is financed.

What other agreements usually sit alongside an HMA in the jurisdiction?

Usually, staff training and group services arrangements are made. If the operator is granted a right of first refusal or purchase option right over the real estate, these are established in a separate agreement.

Transfers and assignments

What are the standard rights / restrictions in respect of transfer / sale of the hotel?

Operators will require consent to any change in ownership of the hotel or the hotel owner vehicle.

When a managed hotel is sold (either asset or share deal), is it usual in the jurisdiction that either the Operator's consent is required for the sale, or that the hotel may only be sold if the HMA transfers with the hotel?

Yes.

Do HMAs commonly include a right of first refusal for the operator to purchase the hotel?

It is not common to include a right of first refusal for the operator.

Is it usual to include provisions which enable the sale of the property with vacant possession ie without the brand?

No, it is very uncommon.

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