

Bad Reviews Could Shut Down Your Hotel Franchise

Law360, New York (June 29, 2015, 10:58 AM ET) --

In most cases, courts and state legislatures have made it more difficult for franchisers to terminate franchise agreements. However, one federal court in New York recently upheld the use of negative guest satisfaction surveys as a basis for termination.

In *HLT Existing Franchise Holding LLC v. Worcester Hospitality Group LLC* (U.S. Ct. App., 2nd Cir., Case No. 14-593-cv, April 9, 2015), the U. S. Court of Appeals for the Second Circuit upheld a franchiser's decision to terminate a franchise based largely upon the results of guest satisfaction surveys.

The terminated Hampton Inn franchisee argued that the guest satisfaction surveys were inadmissible hearsay statements and should not have been considered by the court in assessing whether the franchiser acted properly in terminating the franchise. "Hearsay" is defined as any out of court statement offered into evidence to prove the truth of the matters asserted in the statement. (Fed. R.



Eugene J. Podesta

Evd., R. 801(c)). The guest satisfaction surveys were clearly out of court statements. However, the court reasoned that the surveys were not offered to prove the truth of the matters asserted in the survey reports, but rather "were admitted solely for the purpose of showing their effect on [the franchiser's] decision to terminate the franchising agreement." The court relied on a line of cases holding that a statement offered to show its effect on the listener is not hearsay. The survey data tended to show that the franchiser did not act arbitrarily, irrationally or in violation of its implied obligation of good faith and fair dealing. The court found it proper to consider the survey data for that purpose.

Failing in its primary argument, the franchisee pursued a different line of attack. The franchisee pointed out that the survey data was not even collected by the franchiser. The survey data was actually collected by Medallia Inc., a large third-party survey administrator and transmitted to the franchiser. Since it came from some third-party, the franchisee argued it should not have been considered by the court. The court found that Medallia regularly compiled guest survey scores at the time the guests submitted those survey responses. Medallia's reports recorded guest impressions in the course of regularly conducted business activity. Additionally, the franchisee did not dispute the trustworthiness of Medallia's records. Thus, the survey results were properly considered.

Finally, the franchisee claimed that the liquidated damages provision in the franchise agreement should not be enforced. The court noted that a contractual provision fixing damages in the event of future breach will be enforced if the preset amount bears a reasonable proportion to the probable loss and the actual loss is difficult or impossible to estimate with any precision. The burden rests with the party

seeking to avoid the payment of damages. Expressing a reluctance to “interfere with the parties’ agreements,” the court upheld the liquidated damages provision.

Twenty-one states currently have some version of franchise relationship statutes. Seventeen of those statutes require the franchiser to show good cause in order to justify franchise termination. Additionally, most states’ laws require any contracting party to meet an obligation of “good faith and fair dealing.” As this case demonstrates, guest satisfaction surveys can provide a powerful tool to help franchisers meet that legal hurdle.

Not only are guest satisfaction surveys a powerful tool for hotel franchisers, they are also a tool already on hand. Almost every major hotel franchiser employs guest opinion surveys and the uses to which they are put continue to expand. Historically, guest surveys formed a part of the franchiser’s quality assurance program. The surveys, along with periodic site inspections, were the principal means by which franchisers determined how well individual franchisees were complying with brand standards and requirements.

Today, hotel franchisers and operators use these surveys for more than just internal research or compliance purposes. Many hotels now use individual answers to optimize a guest’s experience. One chain is working to integrate its survey system into its guest profiles. Much of this information is now available to the front desk at check-in. Thus, for example, the front desk can remind the guest at check-in that the guest is two or three stays away from a rewards program upgrade or the guest can be assigned to a room far from the elevator based upon a prior complaint of noise in an earlier survey.

In addition to surveys conducted by and for the hotels directly, great attention is paid to guest comments on travel websites and social media. Many hotel operators have discovered that higher room rates can be charged at locations consistently rated high on sites such as Trip Advisor.

This raises an interesting question in light of the holding in *HLT Existing Franchise Holding v. Worcester Hospitality*. In that case, the franchiser relied on surveys conducted on its behalf by a third-party vendor. These surveys were sent only to guests who had actually registered at the hotel and were maintained by the vendor in the ordinary course of its business. These factors gave the surveys the added reliability which the court found necessary in order for them to be considered.

Could the franchisers have relied solely upon negative reviews on Trip Advisor or other travel websites? That would likely prove problematic. Comments on such sites are anonymous. There is no assurance that input is coming from actual hotel guests. The comments lack the structure of a formalized guest opinion survey and therefore cannot be used to spot trends or to compare facilities. It would seem that website comments probably lack the necessary veracity and reliability needed to be admitted as evidence in litigation.

While the New York court did not extend its holding to the use of website or social media postings, its decision to allow the use of guest satisfaction surveys will make it easier for franchiser to terminate

franchise agreements and still comply with the statutory and common law requirements for good cause or good faith and fair dealing.

—By Eugene J. Podesta, [Baker Donelson LLP](#)

[Eugene Podesta](#) is a shareholder in Baker Donelson's Memphis office and co-chairman of the firm's hospitality industry service team.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of the firm, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

All Content © 2003-2015, Portfolio Media, Inc.