



## I. INTRODUCTION

The city hotels are one of the important components to support tourism activities in Bali, Indonesia. In Bali, the existence of city hotels, which are traditionally managed and usually owned by the Balinese family local entrepreneurs, is increasingly threatened by the presence of various city hotels that are developed under a chain, franchised, or managed model. The franchise city hotels owned by large or multinational corporations commonly exhibit excellent standards of hotel hospitality. The franchise city hotels are incomparable to the Balinese family city hotel management. Currently, the emergence of various types of modern franchise city hotels in Bali, is influenced by the suitable laws and policies, such as the regime of World Trade Organization (WTO) Agreement with one of its ground bases, the “non-discrimination principle,” at the international level. Based on this principle, all the member countries, both foreign and local, are treated equally. From this perspective, the WTO Agreement, which consists of three annexes, the Trade-Related Aspects of Intellectual Property Rights Agreement, the General Agreement on Trade in Service (GATS) Agreement, and the Trade-Related Investment Measures Agreement, provides equal treatment to all the member countries to conduct business activities related with intellectual properties (IPs), services, and investments. For example, connected with the growing investment accommodation in tourism areas such as in Bali, WTO allows its member corporations to establish internationally renowned franchised city hotels in Bali, particularly if these modern franchised city hotels have met the requirements of hotel establishment.

As mentioned previously, WTO members, including Indonesia, should comply with the rules-based system of the WTO, including dispute settlement.<sup>1</sup> Internationally, under the WTO scheme, dispute settlement is considered as the central pillar of the multilateral trading system. Further, to enforce the non-discrimination principle, compliance to the regional agreements, such as those of the ASEAN Economic Community (AEC), is also needed. The Blueprint for Growth ASEAN Economic Community 2015 mentioned the four interrelated and mutually reinforcing pillars of ASEAN economic integration: (a) a single market and production base, (b) a highly competitive economic region, (c) a region of equitable economic development, and (d) a region fully integrated into the global economy. As broad and multi-faceted as these pillars are, the goals of the AEC have been met on many fronts,<sup>2</sup> indicating that the trading system, both regionally and internationally, is derived from a global economy with its binding single-market rule-based principle. This system is often criticized as being extremely liberal for several developing countries, including Indonesia. On one hand, the fruitful development of a single-market rule-based system conveys several advantages, such as providing job opportunities for people. However, on the other hand, such system also threatens the sustainability of the local business activities that are usually more traditional model-based rather than modern management-based, such as in the discourse of Balinese city hotel activities. The emergence of modern

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<sup>1</sup> Dispute settlement is the central pillar of the multilateral trading system, and the WTO’s unique contribution to the stability of the global economy. Without a means of settling disputes, the rules-based system would be less effective because the rules could not be enforced. The WTO’s procedure underscores the rule of law, and it makes the trading system more secure and predictable. See World Trade Organization, “Understanding the WTO: Settling Disputes A Unique Contribution,” [https://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/disp1\\_e.htm](https://www.wto.org/english/thewto_e/whatis_e/tif_e/disp1_e.htm), accessed August, 27, 2016.

<sup>2</sup> The ASEAN Secretariat, “A Blueprint for Growth ASEAN Economic Community 2015: Progress and Key Achievements,” p. 5, <http://www.asean.org/storage/images/2015/November/aec-page/AEC-2015-Progress-and-Key-Achievements.pdf>, accessed 9 August 2016.

chain city hotels has prevented the local city hotels from competing in terms of both the infrastructure and quality management services. To overcome these crucial issues, this study determines the adequate protection for traditional local city hotels by constructing the model provisions of the local government regulation and self-regulation framework. The provisions agree with the WTO Agreement and the laws and policies at the regional level.

Constructing the model provisions of local government regulation on the issue of empowering local or domestic city hotels bears relevance through both the "Model Provisions of Local Government Regulation" and "Self-Regulation Framework." The community values related to the customary law, human rights law within the Organisation for Economic Co-operation and Development context, and John Ruggie's *framework or United Nation (UN) Guiding Principles on Business and Human Rights are important as a legal ground to construct the model provisions of local government to aid successful development of domestic city hotels as modern franchised city hotels.* In addition, to urge hotel associations to take the initiative in constructing the "Self-Regulation Framework," concepts of corporate social responsibility (CSR) and partnership should be appropriately considered as a protection model. In this context, the hotel associations or relevant stakeholders are expected to help and strengthen the local city hotels to compete fairly with the international or modern franchised hotels through partnership programs, such as chain city hotel associations, to provide access to modern franchised management, capital, modern marketing, service standards, and CSR programs. By helping and supporting the local city hotels with the concept of modern franchising management through the so-called "Self-Regulation Framework," they can create opportunities for the local city hotels in Bali to develop as internationally renowned franchised hotels, enabling the creation of a new model of standard city hotels with the community values in line with modern standards of franchised city hotels.

The regulation framework plays an important role in improving the quality standards and performance of the local city hotels as it is commonly used by international chain hotels. As an example, the tourism and hospitality sector (THS) in Nigeria, during the difficult periods (military coups, a civil war, and two failed republics), most of the hotels are owned by the government. However, the government-operated hotels perform inconsistently in delivering acceptable levels of services. By collaborating with branded international chain hotels, the number of new-build hotels increased dramatically; these hotels include the Sheraton, Hilton, Radisson Blu, Swiss International, Le Meridien, InterContinental, Best Western, Southern Sun and Sun International, and Marriot. Belinda Nwosu (2016) indicated that the significant changes over the past two decades in the THS of Nigeria have facilitated further understanding of the hotel industry and the salient issues, namely, institutional framework (system of formal laws, regulations, procedures, informal conventions, customs and norms, and restrained socio-economic and behaviors), human capital profile, and the recruitment and skill gaps (employment relationship and human capital development).<sup>3</sup> The review of the THS of Nigeria failed to directly elaborate on the local city hotels, but the information gathered can be considered from perspective of Nigeria, that is, the hotel industry, including local city hotels, can achieve international standards through an institutional framework, employment, and human capital development.

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<sup>3</sup> Belinda Nwosu, "A review of the hotel industry in Nigeria: size, structure and issues," *Worldwide Hospitality and Tourism Themes*, no. 2 (2016): 118-122.

As in Nigeria, at the Asian-country level, establishing international hotel companies remains a concern. Previous studies mostly focused on developing multinational hotel companies in Asian countries, but current research should examine the obstacles and solutions for Asian hotel companies expanding internationally to benefit from transferable marketing. Carmen Lam *et. al.* emphasized that several success factors of Asian hotel companies include location advantages, depth of knowledge of the local markets, unique founding vision, strong local identification, and core competencies, such as authentic service experience, low-cost strategy, and focus strategy.<sup>4</sup> Furthermore, their study also demonstrated the importance of tying the development strategy to the success factors of the companies.<sup>5</sup> Although this study focused on expanding internationally the top 53 Asian hotel companies in the Hotel 325 list and excludes smaller Asian companies, the key success factors, namely, the strategic development choices should be adopted for local city hotels to strength and improve their quality and management standard.

CSR-related activities may be relevant as one of the strategic developments to empowering local hotels, including the local city hotels in Bali, to achieve better performance and service hospitality and to become chain hotels that can possibly expand internationally. The CSR is not merely an obligation and responsibility for companies; implementing CSR will also provide positive reputation for the companies. E. Arikan *et al.* emphasized that firms engaging in CSR-related activities spread positive signals to internal and external audience; this engagement serves as basis on which the audiences build their reputational perceptions.<sup>6</sup> Zulhamri and Aziz mentioned that CSR initiatives are significant predictors of dimensions of corporate reputation.<sup>7</sup> Karpal Singh Dara Singh and Md. Aminul Islam revealed that current organizations should strongly consider the CSR as a means of achieving strategic outcomes in terms of increased reputation and brand equity.<sup>8</sup> Matthew Tingchi Liu *et al.* stated that the customer brand preference can be enhanced by CSR performance. Performance in each of the three CSR domains (environment, society, and stakeholders) positively impacts brand preference; however, to a different degree, CSR on stakeholders results in a stronger positive impact for brand preference.<sup>9</sup> CSR activities contribute advantages both for the reputation of companies and their stakeholders, such as smaller companies; an example is the improvement of the management quality and service standard through the CSR activities of branded international chain hotels.

The CSR model by John Elkington, the so-called, "Triple Bottom Line" (TBL) or 3-based P (profit, people, and planet), and the pyramid CSR model by A. C. Carroll

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<sup>4</sup> Carmen Lam, Grace K. S. Ho, Rob Law, "How can Asian hotel companies remain internationally competitive?", *International Journal of Contemporary Hospitality Management* 27, no. 5 (2015): 834.

<sup>5</sup> *Ibid.*, p. 846

<sup>6</sup> E. Arikan, D. Kantur, C. Maden, E. E. Telci, "Investigating the mediating role of Corporate reputation on the relationship between corporate social responsibility and multiple stakeholder outcomes," *Qual Quant* 50 (2016): 144. DOI 10.1007/s11135-014-0141-5.

<sup>7</sup> A. Zulhamri, and Y. A. Aziz, "Institutionalizing corporate social responsibility effects on corporate reputation, culture, and legitimacy in Malaysia," *Social Responsibility Journal* 9, No. 3 (2013): 344-361.

<sup>8</sup> Karpal Singh Dara Singh and Md. Aminul Islam, "Validating an instrument for measuring brand equity of CSR driven organizations in Malaysia," *Management & marketing Challenges for the Knowledge Society* 12, no. 2 (2017): 248-249.

<sup>9</sup> Matthew Tingchi Liu, Ipkin Anthony Wong, Guicheng Shi, Rongwei Chu, James L. Brock, "The impact of corporate social responsibility (CSR) performance and perceived brand quality on customer-based brand preference," *Journal of Service Marketing* 28, no. 3 (2014): 181.

with its partnership model may strengthen small and weak companies. To employ the TBL of the CSR model and pyramid CSR model, local government regulations and initiative self-regulation framework of relevant stakeholders must be provided by hotel industries to implement better business practices, including the tourism sector in Bali. Therefore, this study examines and discusses the role of the local government and its awareness of international chain hotels that have existed in the tourism sector in Bali to strengthen local city hotels on the other. The following questions arise. To what extent should the local government regulate a “model provisions” in Bali to strengthen local city hotels without conflicting with the non-discrimination principle? Can constructing “the self-regulation framework” by the hotel association empower the local city hotels to compete fairly with the franchise donees?

This article first examines the concept of franchising in relation to franchised hotels, the so-called chain hotels, particularly the emergence of international chain hotel brands in the commercial and legal contexts to understand several international and legal context-related international instruments, such as the WTO Agreement, the UN World Tourism Organization (the UNWTO), the World Intellectual Property Organization Franchising Guides (the WIPO Franchising Guides), and the Federal Trade Commission’s Franchise Rule (FTC Rule). At the national level, particularly Indonesia, several provisions of regulations are discussed; they include Law No. 20 of 2008 on the Small and Medium Enterprises, Law No. 10 of 2009 on the Tourism, Law No. 25 of 2007 on the Investment, Government Regulation No. 44 of 1997 on the Partnership, the Government Regulation No. 42 of 2007 on Franchising, and the Ministry of Trade Regulation No. 53/M-DAG/8/2012 on the Implementation of Franchising. The emergence of chain hotels in Bali is elaborated as part of the local dimensions. Second, this article discusses the importance of self-regulation framework and the government model provisions in underpinning the emerging franchised city hotels in terms of their impact to the local city hotels in Bali. Furthermore, this article elaborates the possibility of developing Balinese city hotels as franchised or chain hotel models by implementing traditional community values, such as *Tri Hita Karana* (THK) principles, and CSR as a strategic development.

## II. DEVELOPMENT OF FRANCHISED HOTELS IN THE COMMERCIAL AND LEGAL CONTEXTS: INTERNATIONAL, NATIONAL, AND LOCAL DIMENSIONS

By exploring the concept of franchising, particularly from the commercial and legal contexts, and its characteristics, franchise can be regarded as a commercialization relationship between two agents, namely, the franchisor and franchisee, who are legally and financially independent but share a common target. A franchise is contract-based; the franchisor provides the franchisee the right to use a developed concept of business, including the brand, products, and marketing services and methods. By allowing the use of this business model, the franchisor requires in exchange a payment from the franchisee; in addition, the franchisor has an obligation to regularly develop and supervise the business format.<sup>10</sup> Further, franchising is a relationship between a supplier and a dealer. This form of relationship is an effective way to combine the strengths, skills, and needs of the franchisor and the franchisee. This relationship also

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<sup>10</sup> Juan M. Berbel-Pineda and Jose M. Ramirez-Hurtado, “Issues About The Internalization Strategy of Hotel Industry by Mean of Franchising,” *International Journal of Business and Social Science* 3, no. 6; Special Issue-March (2012): 285

requires a medium level of risk, control, and/or resource commitment and allows sharing of cost of expansion.<sup>11</sup> From the concept above, the characteristics of a franchise can be drawn as follows: a cooperation system, a contract-based/format, a party consisting of franchisor and franchisee, a developed concept of business including the brand reputation and product and marketing services, and requirement of an exchange payment paid by the franchisee to the franchisor.

From the economic perspective, the development of the international franchised hotels has brought considerable advantages and benefits, especially to the corporation that engages in the hotel sector. Notably, the success of franchised hotels results in a positive impact, especially to the surrounding community and employees who work for the hotel, revealing that franchising as an organizational form triggers economic development.<sup>12</sup> From the economic perspective, franchising hotel chains is more efficient than owned hotels. Franchised chain hotels provide access to the reputable and independent hotels, such as local city hotels, where as chain integration will increase hotel efficiency. Sami Ben Aissa and Mohamed Goaid discovered that international attraction and market competition directly influence hotel efficiency.<sup>13</sup> SuzanaBaresaet. al. revealed that franchising enables the transfer of business knowledge, experience, and technology to an unlimited space. Franchising is a type of business transaction worldwide, and it causes a certain impact on national economies.<sup>14</sup> One of these impacts is providing additional job opportunities at the national level.

At the domestic level, for example, in Bali, the development of franchised hotels provides more job opportunities for people; this type of business is also managed by professionals and modern management. The agency theory is relevant to explain why this franchising strategy can grow substantially and become the model strategy selected to develop business activities. In their study, Baker and Dant pointed out that the agency theory is the dominant paradigm that can explicate the meaning of franchising especially in the USA. This theory suggests the agency relationship between the franchisor and franchisee (agent). Furthermore, Elsenhardt revealed that, *“since the parties may have divergent goals, agency costs arise along with the risk of opportunism. Principals can reduce agency costs and opportunism through direct observation and monitoring or through a system of aligned incentives.”*<sup>15</sup>

According to the Indonesian Franchise Association, franchise is a distribution system of goods or services to end consumers and in which the brand owner (the franchisor) gives right to individuals or corporations to conduct business with a trademark, name, system, producer, and ways that are already previously set up for a certain period of time and covers certain areas. Based on the Government Regulation No. 42 of 2007 concerning Franchise, franchise is a special right owned by an individual or business entity (with its characteristics) to market their goods and/or services, which have been proven successful and may be utilized and/or used by other parties based on the franchise agreement, to another individual or business

<sup>11</sup> S. Jiménez-Burillo, J. J. Jiménez-Moreno, “The Role of the Top Management Team in the Choice of Entry Modes – Theoretical Perspective.”, *Entrepreneurial Business and Economics Review*1, no. 2 (2013): 53.

<sup>12</sup> S. Michael, “Can franchising be an economic development strategy? An empirical investigation,” *Small Business Economics* 42, no. 3 (2014): 611-620.

<sup>13</sup> Sami Ben Aissa and Mohamed Goaid, “Determinants of tourism hotel market efficiency,” *International Journal of Culture, Tourism and Hospitality Research*10, no. 2 (2016): 173.

<sup>14</sup> SuzanaBaresa, Zoran Ivanovic, and Sinisa Bogdan, “Franchise Business as a Generator of Development in Central Europe,” *UTMS Journal of Economics* 8, no. 3 (2017): 281.

<sup>15</sup> Ilan Alon, Liqiang Ni, Yuncheng Wang, “Examining the Determinants of Hotel Chain Expansion Through International Franchising”, *International Journal of Hospitality Management*31, no. 2 (2012): 381.

entity.<sup>16</sup> Franchising, especially with the type of business format, is perceived to convey benefits and has been proven successful for the businesses in general and hotel business in particular. With regard to his result, the hotels in Bali will possibly benefit from using the franchising management to facilitate tourists at the domestic, national, and international levels. Based on an empirical study conducted in hotel sectors in Bali, 23% of the respondents reported that city hotels are operated with the international franchising management system. The representative examples include the Marriott Hotel, Holiday Inn, Ibis Hotel, and other chain hotels that are found globally. The results also showed that 31% of the respondents stated that city hotels operate in Bali using the national franchised hotel management system.<sup>17</sup>

The development of franchising business model including the franchised or chain hotels originated from the developed countries such as America. In the 1950s, the Hilton Hotel, Sheraton Hotel, and Holiday Inn were developed using a chain model with its internationalization strategy of leasing and management contract. In the context of operating hotels internationally, Cho implied that the franchising model reduces the investment risks related with highly capital-intensive hotels. The franchising system has become a mainstream model in America to expand hotels internationally.<sup>18</sup> Several studies showed that America is considered to be the originator of franchising in a hotel sector.<sup>19</sup> Franchising provides franchisees with the opportunities to develop their hotel businesses without high investment capital or risk. The franchisees possess the opportunity to use an owned international brand, including its reputation and recognition, its economic scale, and its managerial expertise from the franchisor with an obligation to pay a certain initial fee and royalty. In a commercial context, further development of the marketing strategy driven by the franchise model moves toward standardizing several aspects of the marketing strategy all over the world.<sup>20</sup> Meanwhile, in the legal context, a franchise model is developed based on the contractual notion that refers to the freedom of contract principles.

In the European context, although franchising in the hotel industry shows a less rapid growth than that in the US, it considerably grows stronger. In the beginning, five hotel industries account for the first 20 world-class franchising companies: the Wyndham Hotel Group, Choice Hotels, Inter-Continental Hotel Group, Hilton Worldwide, and Marriott International. The franchised hotels developed in Western European countries, such as Germany, the United Kingdom, France, Italy, and Spain. To build a franchised hotel, considerable money is initially needed for several franchising fees, namely, the initial fee or membership fee, royalty fee, advertising or marketing contribution fee, reservation fee, loyalty fee, royalty fee, and other various fees. However, franchising provides a number of advantages for the franchisee in relation to its competitiveness. Considering the market recognition, a famous company brand

<sup>16</sup> Andri VB, 2013, *Jurus Sukses Franchise 100% Pasti Untung (Kick Successful Franchise 100% definitely Profit)* (Jakarta: PT Gramedia Widiasarana Indonesia, 2013), p. 26.

<sup>17</sup> Ni Ketut Supasti Dharmawan, et. al., "Implementing the Traditional Community Values for the Development of Franchised City Hotel" (paper presented in the International Seminar Traditional Community in A Global World Facing ASEAN Economic Community 2015, Jointly Organized by FL Udayana University, ASEAN Secretariat, Charles Darwin University School of Law, Denpasar Bali Indonesia, 25 September 2014

<sup>18</sup> Alon, et. al., "Examining the Determinants," p. 5.

<sup>19</sup> J. Marković, J. Jelica Petrović, D. Marko, "Presence of the Largest Hotel Franchise Companies on the European Market," *Researches Reviews of the Department of Geography, Tourism and Hotel Management* 42 (2013): 166

<sup>20</sup> C. M. Sashi & Devi Prasad Karuppur, "Franchising in Global Markets: Towards a Conceptual Framework," *International Marketing Review* 19 (2002): 500.

plays an important role for the satisfaction of the customers or hotel guests; thus, the emergence of franchising strategy including franchised hotels benefits both the franchisor and franchisee and the customers.<sup>21</sup>

The development of international franchised hotels not only occurs in the USA, Canada, the UK, and other Western European countries but also extends to the centers of world tourism, including China and other Asian nation states. As one of the top five tourist destinations in the world, China is a very promising place for the growth and development of an international hotel chain. This condition holds true, especially as five-star hotels are rapidly growing in China. According to the UNWTO, in 2020, China will become the number one tourist destination, with a tourist arrival level approximating 130 million travelers per year. Therefore, the hotel development and growth in China progresses rapidly. For example, the data in 2002 showed that the number of international franchised hotels and state-owned hotels in China totaled 8,880, including one-star to five-star hotels.<sup>22</sup>

International franchised hotels also grow at a rapid rate in Indonesia, of which Bali is an example. Bali has been recognized as one of the famous world tourism destinations. For better services, convenient accommodations are needed to provide hospitality and comfort to the guests. The directory of Bali Provincial Tourism Office 2013 reported that Bali features 223 stars-hotels with 21,704 rooms.<sup>23</sup> From this number, 46 are international franchised hotels (21%) that operate in Badung Regency and Denpasar City, whereas around 177 hotels (79%) are identified as locally managed hotels. The massive existence and the development of international franchised hotels in Bali have started in the last 7 years. In addition, based on the Research and Forecast Report 3<sup>rd</sup> Quarter 2015, the four-star hotels dominate the tourism areas in Bali. Considering the further supply projection between 3Q of 2015 and 2019, the room projection will reach 3,075 (three-star hotels), 9,350 (four-star hotels), and 8,121 (five-star hotels).<sup>24</sup> The emergence of various branded hotels in Bali is needed to make the Balinese tourism destination become more convenient for all stakeholders, more specifically the hotel customers. However, considering that Bali is categorized as a small island compared with the other islands in Indonesia, this area should not be burdened with massive international and local hotels. Therefore, the existing locally managed hotels must be maintained by supporting the international franchised standardization rather than having the government invite foreign investors to build more international hotels. By providing more social conduct and improving the surrounding environment, the franchised hotels will gain advantages as a part of their implementation of the CSR.

Internationally, in the legal context, several legal instruments underpinning the emergence of franchised hotels, including franchised city hotels, can be explored. The WIPO regulates the type of franchising business strategy through a set of rules known as the Franchising Guide. The WIPO bears relevance in regulating the franchising model as the franchising business is intertwined with the IP rights, especially the trademark and trade secret, similar to that in the business franchise of McDonald's. Basically, the Franchising Guide established by the WIPO determines various

<sup>21</sup> Marković, Petrović and Marko, "Presence of the Largest Hotel Franchise," pp. 167-168.

<sup>22</sup> Vincent C. S. Heung, Hanqin Zhang, Chen Jiang, "International Franchising: Opportunities for China's State-Owned Hotels," *International Journal of Hospitality Management* 27 (2008): 368-369.

<sup>23</sup> Bali Provincial Tourism Office, (2013):3. See also The Central Bureau of statistics of Bali Province (2014), p. 1.

<sup>24</sup> Ferry Salanto, "Bali Hotel Market Report", Research & Forecast Report (2015), p. 5.



important elements in the development of business franchising; these elements include the standard license agreement, franchising arrangements, a license to use the system, grant of a license to use the franchised product, licensing of a uniform system; "business format" franchises, service franchises, distribution franchises, franchise developer agreement, master franchising, and combined structures.<sup>25</sup> The Franchising Guide also stipulates the rights and obligations of the franchisor, and they consist of an operating manual, training, opening assistant, and continued support. Furthermore, the rights and obligations of the franchisee consist of 1. A development schedule; 2. Payment of fees including the initial fee, ongoing fee, advertising and promoting fee, and fee for specific services; 3. Compliance with the quality control to allow inspection and requirement to order supplies from an approved source; and 4. Confidentiality requirements.<sup>26</sup> The WIPO Franchising Guide also explores the rights and obligations of the parties primarily concerning the expiration of franchising, the transfer of agreement, and renewal of the franchising agreement. As previously mentioned, the legal basis of franchising business strategy is based on contractual relationships. The similar notion also appears in the arrangement of the WIPO Franchising Guides.

The investment and consumer protection laws are also considered appropriate in protecting franchising business activities both for the business sectors and the consumers and among others, the preference to use a specific arrangement under the so-called a *sui generis* provision concerning franchising. The United States, for example, has set certain rules dealing with the franchising business; these rules include the FTC Rule, the Uniform Franchise Offering Circular, the Small Business Franchise Act, whereas at the state level, the United States has enacted rules concerning State Franchising and Disclosure Laws and Deceptive Trade Practices Acts, which are so often known as "Little FTC Acts."<sup>27</sup> Other countries, such as Malaysia and China, regulate the franchising business by a hybrid model through foreign trade and investment franchise laws. The South African countries regulate franchising through the Consumer Protection Act 2009, which also shows the existence of a hybrid model of regulation between anti-trust regulations and pure franchise regulations. In contrary to the countries mentioned above, New Zealand does not regulate franchising in specific *sui-generis law*. This country regulates franchising as a part of Investment Law especially foreign capital investments.<sup>28</sup> Overall, several similarities are observed with the regulation of franchising regulating basic details of the franchisor, description of the franchise and the market, financial information about the franchisor, details of the franchise network, litigation details, initial fee, initial investment and continuing fees, earning claims, restriction on the franchisee, descriptions of the obligations that the parties owe toward one another, purchase ties and personal involvement of the franchisee; term termination and renewal details about the franchisors' IP rights; and details of financing arrangements offered by the franchisor exclusively.

In Indonesia, franchising is regulated under several provisions of regulations (embracing the hybrid model) such as the following: Law No. 20 of 2008 on the Small and Medium Enterprises, Law No. 10 of 2009 on the Tourism, Law No. 25 of

<sup>25</sup> WIPO, Franchising Guide (Geneva: International Bureau of WIPO, 1994), pp. 22-23.

<sup>26</sup> Ibid, p. 35-37

<sup>27</sup> Debra Burke & E. Malcolm Abel II, "Franchising fraud: The continuing need for reform," *American Business Law Journal* 40, no. 2 (Winter, 2003): 371-380

<sup>28</sup> Mark Abell, "The Regulation of International Franchising," (2010), <http://whoswholegal.com/news/features/article/28705/the-regulation-international-franchising>, accessed 19 August 2014.

2007 on the Investment, Government Regulation No. 44 of 2007 on the Partnership, Government Regulation No. 42 of 2007 on Franchising, Ministry of Trade Regulation No. 53/M-DAG/8/2012 on the Implementation of Franchising, the Decision on the Business Competition Supervisory Commission (KPPU) No. 57/KPPU/Kep/III/2009, Article 50 letter b, especially concerning the Agreement that is related with Franchising, Guideline of the Implementation of Article 50 Letter b concerning the Exemption of the Application of Law No. 5 of 1999 toward Agreement that is related with Franchising, and Ministry of Trade regulation No. 07/M-DAG/PER/2/2013 concerning the Development of Partnership in Franchising for Food and Drink Service-Type of Business.

As mentioned above, various regulations have been enacted to underpin the rapid development of franchising businesses including hotels. On one side, the existence of franchised hotels can provide satisfaction and maximum services to the guests or tourists. For example, in China, as one of the world tourism destination, the research results showed that almost 83% of the general managers stated that the companies of franchised hotels are benefited by the reputation of internationally franchised hotels, which are usually preferred by guests and recognized widely by consumers.<sup>29</sup> However, on the other hand, the local hotels or hotels which are operated independently without the support of a chain hotel with international standardization may not be able to use the management of international franchised hotels owing to the high franchising fee. The local or independent hotels may require 5 years to pay the franchising fee in relation with using the international franchised hotels.<sup>30</sup> The hotels that have followed the international franchising business can suffer from such high amounts of management fee, loyalty fee, and royalty fee, which need to be paid as an obligation of using the brand name of an international franchised hotel. In other words, most of the benefits flow into the franchisor. In the Chinese context, to overcome the problems of traditional management hotels or independent city hotels to compete with international franchised hotels, China has suggested reforming a hotel management system toward franchised hotels. However, the study of Vincent *et al.* (2008) failed to elaborate further whether their suggestion to address the traditional management hotels to become part of international franchised hotels means that the owners of local hotels become franchisees, or whether they may create their own national franchised hotels to becoming international franchised hotel; in such condition, the legal construction will automatically change. The local owners of city hotels will no longer be franchisees but serve as franchisors.

As noted above, given the high price of several fees to use a franchising business strategy, several franchisees eventually stop using the international brand hotel with international standard management and instead start their own brand. In the Indonesian dimension, Sumarsono (2014) has proven that business hotels that were originally used international franchised hotels have changed their names into new local brands, achieving better results. Several of these hotels include the Aston Hotel Serpong (changed its name into Hotel Atria), Hilton Hotel (Sultan Hotel), Quality Hotel (Hotel Sunan Solo), Ritz Carlton Bali (The Ayana Bali), and Lotus Garden Hotel Kediri (Sahra Hotel Kediri). Sumarsono also suggested that the development of the standards of hospitality in business hotels in Indonesia starts from a budget hotel chain and then grows from national branding toward an international franchised hotel chain. Locally managed hotels need not to build their image by using internationally

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<sup>29</sup> Heung, Zhang, and Jiang, "International Franchising," p. 374.

<sup>30</sup> *Ibid.*, p. 377.

franchised hotels. Differently put, such establishments are advised to develop their own network hotels.<sup>31</sup>

In a practical dimension, although creating one's own franchised hotels can be used to overcome the massive emergence of international chain hotels threatening the existence of local hotels, a legal dimension must be considered, specifically in correlation to the principles of non-discrimination. The basic principles of non-discrimination, based on the WTO Agreement, include the most-favored-nation treatment and national treatment. Article II of Annex 1B of WTO Agreement, GATS,<sup>32</sup> regulating clearly that the GATS prohibits discrimination between services from different member countries. In detail, the provisions are as follows: "With respect to any measure covered by this Agreement, each member shall accord immediately and unconditionally to services and service suppliers of any other Member treatment no less favorable from that it accords to like services and service supplier of any other country."<sup>33</sup> In general, the WTO agreement covers good services and IPs, which include liberalization and the permitted exceptions.<sup>34</sup> At the regional level, the AEC also contains a liberalization notion that requires comprehension.

Being aware of legal provisions that prohibit discrimination, both internationally and nationally, means that eliminating the threat of the emergence of hotel franchising by banning their establishment in Indonesia is improbable. Thus, a solution, such as strengthening hotel owners by building franchising-based hotels but not contrary to the principle of the non-discrimination system should be developed.

### III. SELF-REGULATION FRAMEWORK AND GOVERNMENT MODEL PROVISIONS UNDERPINNING THE EMERGING FRANCHISED CITY HOTELS

To create and run a sustainable and long-term business that remains intertwined with the roots of the local community, the business industry, including those who engage in the field of city hotels, can utilize the traditional community values, which have been available since a long time ago. With regard to this matter, the city hotels located in Bali can also implement such values that are especially rooted from the Balinese traditional community, i. e., THK. The traditional community values contained in the THK itself are widely used and implemented by the Balinese local community. Furthermore, this THK is similar to the concept of CSR, which is internationally used in the international *fora* by corporations (including hotels around the world) to maintain their businesses in a sustainable and long-term manner.

The values of THK are relevantly implemented as an underpinning to strengthen local city hotels toward developing into franchised city hotel chains. Supasti Dharmawan (2017) expressed that the values to balance the relationships in human life are widely known as the THK philosophy and implemented by the Balinese

<sup>31</sup> Dicky Sumarsono, *Dahsyatnya Bisnis Hotel Di Indonesia Smart Strategy, High Revenue* [The Great Business Hotel In Indonesia Smart Strategy, High Revenue] (Jakarta, PT Gramedia Pustaka Utama, 2014), p. 60.

<sup>32</sup> WTO, "WTO Legal Text", [https://www.wto.org/english/docs\\_e/legal\\_e/legal\\_e.htm](https://www.wto.org/english/docs_e/legal_e/legal_e.htm), accessed 9 August 2016.

<sup>33</sup> Peter Van Den Bossche, *The Law and Policy of the World Trade Organization Text, Cases and Materials*, (Cambridge, University Press: 2008), pp. 334-335; See also, WTO, "Uruguay Round Agreement General Agreement on Trade in Services (Article I-XXVI)", [https://www.wto.org/English/docs\\_e/legal\\_e/26-gats\\_01\\_e.htm#ArticleII](https://www.wto.org/English/docs_e/legal_e/26-gats_01_e.htm#ArticleII), accessed 9 August 2016.

<sup>34</sup> WTO, *Understanding The WTO: The Agreements Overview: a navigational guide*, 2016, [https://www.wto.org/english/thewto\\_e/whatis\\_e/tif\\_e/agrm1\\_e.htm](https://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm1_e.htm), accessed 9 August 2016.

community to maintain the balance and harmony of the relationship between human and the environment, between humans, and humans and God.<sup>35</sup> These values concern such balances in life. The THK itself stands for the sources of wealth or happiness and consists of three balanced and harmonious relationships: (1) cultural aspects (the balanced relationship between humans and God); (2) community aspects (the balanced relationship between humans); (3) environmental aspects (the balanced relationship between humans and the environment).<sup>36</sup> Jan Hendrik Peters and Wisnu Wardana emphasized that the phrase THK originally came from Sanskrit words, *Tri* (three), *Hita* (prosperity), *Karana* (cause). This philosophy signifies the three causes of prosperity produced by balanced and harmonious relations in one whole unity between human and God, human and society, and human and nature.<sup>37</sup> Therefore, corporations that engage in the city hotel business sector in Bali need to utilize these values to keep their business sustainable and not only to profit for their corporations but to maintain balance in their businesses in relation to the three aspects of life. In practice, these balanced and harmonious relationships can be observed through several examples, such as the religious opening ceremony held by the hotel management to ask for God's blessing toward their business, how they share and hold social activities, such as through CSR activities to help the local community, including strengthening local city hotels as part of the relationship between human and society, and caring for nature and not destroying the trees as part of the relationship between human and nature when they build their hotels.

The above mentioned traditional community values of the Balinese THK are similar to the concepts of CSR, which also aims to achieve business sustainability. The CSR features various definitions, and one of them is given by the ISO 26000. According to ISO 26000, CSR is,

*"The responsibility for the impacts of its decisions and activities on society and the environment, through transparent and ethical behavior that: contributes to sustainable development, health and the welfare of society; takes into account the expectations of stakeholders; is in compliance with applicable law and consistent with international norms of behavior; and is integrated throughout the organization and practiced in its relationship."*<sup>38</sup>

Nowadays, the business owners face difficulty in focusing only on profit maximization. To survive in the business industry, the city hotel management also uses CSR to gain the interest from the community and cares about international, national or local issues. The managers must perform more functions instead of just gaining profits to create a sustainable development. One concept of CSR which is similar to THK is the TBL by Elkington. According to the THK, the three values of balanced relationship occur among humans and between humans and God and the environment; according to Elkington, corporations who are engaged in their business

<sup>35</sup> Ni Ketut Supasti Dharmawan, "Protecting Traditional Balinese Weaving Through Copyrights Law: Is it Appropriate?" *Diponegoro Law Review* 2, no. 01 (2017): 79.

<sup>36</sup> Anak Agung Gde Raka Dalem, "Achievements and Challenges of Implementation of "Tri Hita Karana" for Creating Sustainable Tourism in Bali-Indonesia: A Case Study in Hotel Sectors," p 5, [http://www.ritsu-mej.ac.jp/acd/re/k-rsc/hss/book/pdf/vol03\\_02.pdf](http://www.ritsu-mej.ac.jp/acd/re/k-rsc/hss/book/pdf/vol03_02.pdf), accessed on 22 September 2014.

<sup>37</sup> Jan Hendrik Peters and Wisnu Wardana, *Tri Hita Karana the Spirit of Bali* (Jakarta: Kepustakaan Populer Gramedia, 2013), pp. 40-41.

<sup>38</sup> International Organisation for Standardisation, "International Guidelines: ISO 26000 on Social Responsibility," <https://www.iso.org/files/live/sites/isoorg/files/store/en/PUB100418.pdf>, accessed on 22 September 2014.

shall consider three aspects, namely, people, planet, and profit dimensions or 3Ps.<sup>39</sup> Therefore, in conducting their business, city hotels should pay attention to economic aspects which are reflected in their financial condition (profit), to their interaction and awareness of social issues and fulfilment of the quality of community around them (people), and to participation in the protection of the environment (planet).<sup>40</sup>

The CSR is used by corporations to show to the community the extent of their social and environmental responsibility for the surrounding community. Both the THK as a part of the Balinese traditional values and TBL as a part of internationally recognized concepts of the CSR guide the corporations to balance their daily business activities with their environment, community, and economic or religious aspects/values. However, McBarnet also classifies CSR based on law aspects. Mc. Barnet's CSR classifications are (1) beyond the law, (2) through the law, and (3) for the law. If a business implements a CSR policy that is beyond what is actually required by the law, this CSR is called beyond the law, in which the adoption of CSR policy is characterized as voluntary.<sup>41</sup> Meanwhile, if the CSR is introduced in different forms of formal regulations, it is called through the law.<sup>42</sup> Further, the law determines how to put pressure upon the corporations to review their compliance, shifts the social responsibility and ethical legitimacy threshold, and raises the legal control effectiveness.<sup>43</sup> Furthermore, the ethical dimension, in relation to corporate services brands, can be considered to positively impact stakeholders and customer loyalty. Stefan Markovic (2018) revealed that employee empathy positively influences the customer ethically in terms of effective customer commitment, whereas customer loyalty positively impacts the customer word-of-mouth.<sup>44</sup>

#### IV. DEVELOPING BALINESE CITY HOTELS AS A FRANCHISING MODEL BY IMPLEMENTING TRADITIONAL COMMUNITY VALUES AND CSR

Regarding the development of franchising hotels in Bali to support tourism activities, a study showed that around 57% of tourists originate from developed countries, such as America and Europe, 25% from Asia, and 18% from other nations; the respondents mentioned unawareness of the headquarters of corporations.<sup>45</sup> Studies also showed that although the ownerships of franchising hotel have gradually improved to the Indonesian people, as the franchisee, they still pay a high royalty rate, as required by the franchisor, in relation to the right to use, operate, manage, and develop hotels under the name of a prominent franchised hotel.<sup>46</sup> Faced with such dilemma, several hotels in Indonesia including in those in Bali that previously

<sup>39</sup> Gratvan den Heuvel and Ni Ketut Supasti Dharmawan, "Corporate Responsibility and Crime Control in Tourism," in Michael Gerbert Faure, Ni Ketut Supasti Dharmawan and I Made Budi Arsika, *Sustainable Tourism and Law*, eds., (The Hague: Eleven International Publishing, 2014), p. 288.

<sup>40</sup> *Ibid.*

<sup>41</sup> Doreen McBarnet, Aurora Voiculescu & Tom Campbell, eds. *The New Corporate Accountability Corporate Social Responsibility and the Law* (Cambridge: Cambridge University Press, 2009), p. 11.

<sup>42</sup> *Ibid.*, p. 27.

<sup>43</sup> *Ibid.*, p. 54.

<sup>44</sup> Stefan Markovic, Oriol Iglesias, Jatinder Jit Singh, Vicenta Sierra, "How does the Perceived Ethicality of Corporate Services Brands Influence Loyalty and Positive Word-of-Mouth? Analyzing the Roles of Empathy, Affective Commitment, and Perceived Quality," *Journal Business Ethics* 148 (2018): 721.

<sup>45</sup> Ni Ketut Supasti Dharmawan, et. al., "The Model Regulation to Strengthen Local City Hotel in Bali Based on Partnership from Various Stakeholders," *Research Report of Invention Research Grand LPPM Udayana University Bali No. 238-39/UN14. 2/PNL. 01. 03. 002/2014*, p. 40

<sup>46</sup> *Ibid.*, p. 42.

used international franchised hotels, created their own brand hotels, for example, the Aston Hotel Serpong became Hotel Atria, the Hilton Hotel became Sultan Hotel, and the Ritz Carlton Bali became the Ayana Bali.<sup>47</sup> Thus, in the future, hotels can be managed by creating our own international franchising brand. We learn from this information that hotel owners change and stop using the names of distinguished franchised hotels but instead create and develop their own.

As mentioned previously, establishing hotels as a business is highly capital-intensive. Therefore, by selecting an international franchising hotel model, the corporations may gain certain advantages, such as the following: less capital intensiveness, a chance to use the name of well-known and recognized brand image, available chain hotel networking, management by a professional and modern management expertise, excellent hospitality based on international hotel management standards, and a representative competitive price. However, this famous business hotel model also results in several disadvantages; namely, it exists with a rigid license agreement, expensive royalty, and criticized for profiting the franchisor rather than empowering communities in host countries where the franchised hotel is located. Given these facts, Sumarsono (2014) suggested that in developing a hotel business, we must create our own group for international franchising rather than select image hotel chains. As small business enterprises, we can start from "budget hotels."<sup>48</sup>

To help and strengthen the local city hotels, including budget to chain hotels, various franchised hotels that already exist in Bali are needed. The franchised hotels, particularly the franchised hotel associations, are expected to increase the standard of quality of locally managed hotels toward franchised-managed hotels through implementation of the CSR. By implementing the CSR in connection with good fellowship to support the local city hotels, the franchised hotel associations show their respect for human rights and community values. Why then performing CSR can be considered as reflecting the value of respecting human rights in business activities? The answer lies in the wide scope of the CSR. According to the TBL concept of the CSR defined by John Elkington, the CSR covers the areas of people, planet and profit, where social and environmental performances are also the elements to create a business sustainability that actually goes beyond financial performance<sup>49</sup>. Therefore, the corporations respect human rights by conducting CSR activities especially in the field of "people responsibility."

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<sup>47</sup> Sumarsono, *Dahsyatnya Bisnis Hotel*, p. 60.

<sup>48</sup> *Ibid.*

<sup>49</sup> Bill Wallace, *Becoming Part of the Solution: The Engineer's Guide to Sustainable Development*, (Washington DC: American Council Engineering Companies, 2005), p. 37.

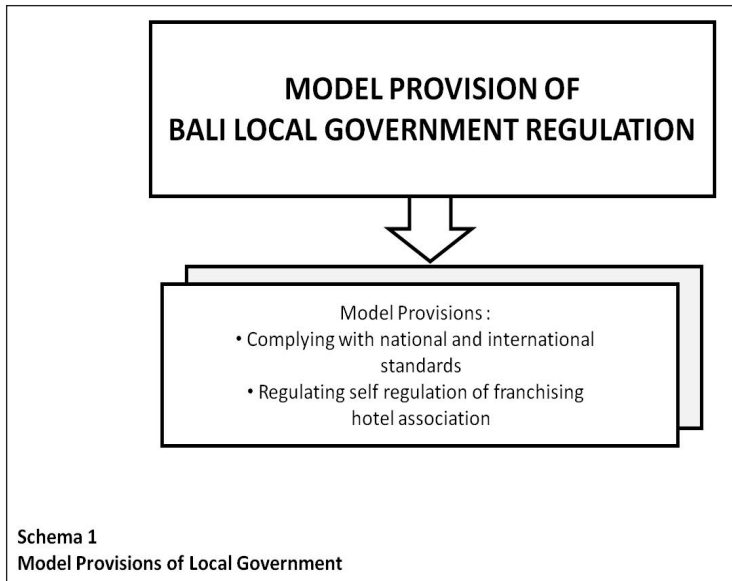


Figure 1. Scheme of Bali Local Government Regulation on Hotel Franchising

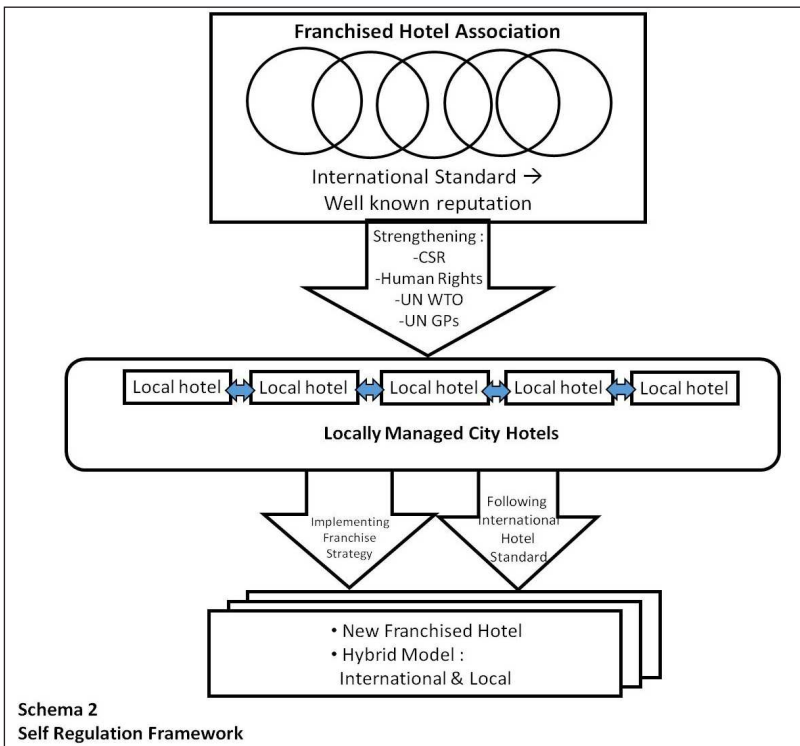


Figure 2. Scheme of Self-regulation Framework

## V. CONCLUSION

The model regulation of city hotels in Bali is related with tourism activities to compete with international chain hotels in addition to being regulated based on international and national regulations. The model is also suitable to regulate hotels under the Provincial Government Regulation of Bali. The CSR related with human rights approaches and the UN WTO can be employed to strengthen the local city hotels in Bali toward facing the globalization era. Although the international franchised hotels grow faster in Indonesia, hotel businesses in Bali are expected to emerge as new franchised hotels with roots from the local dimensions and adopting the international standards. Combining with international approaches, Bali can develop its locally managed hotels for two main reasons. First, Bali can develop its tourism sector by promoting the local concept of THK, which complies with the concept of the CSR program as a strategic development. Second, Bali can enhance the welfare of the local people/community. The government of Bali, the provincial parliament, and business community, especially the hotel associations, must collaborate for the development of the international city hotels in Bali and determine their negative impact on the local city hotels and determine the appropriate solutions to the problems. The establishment of the model provisions of Bali local government regulation and self-regulation framework is expected to strengthen locally managed hotels toward developing new franchised hotels that adopt traditional community values, e. g. , the THKconcept.



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