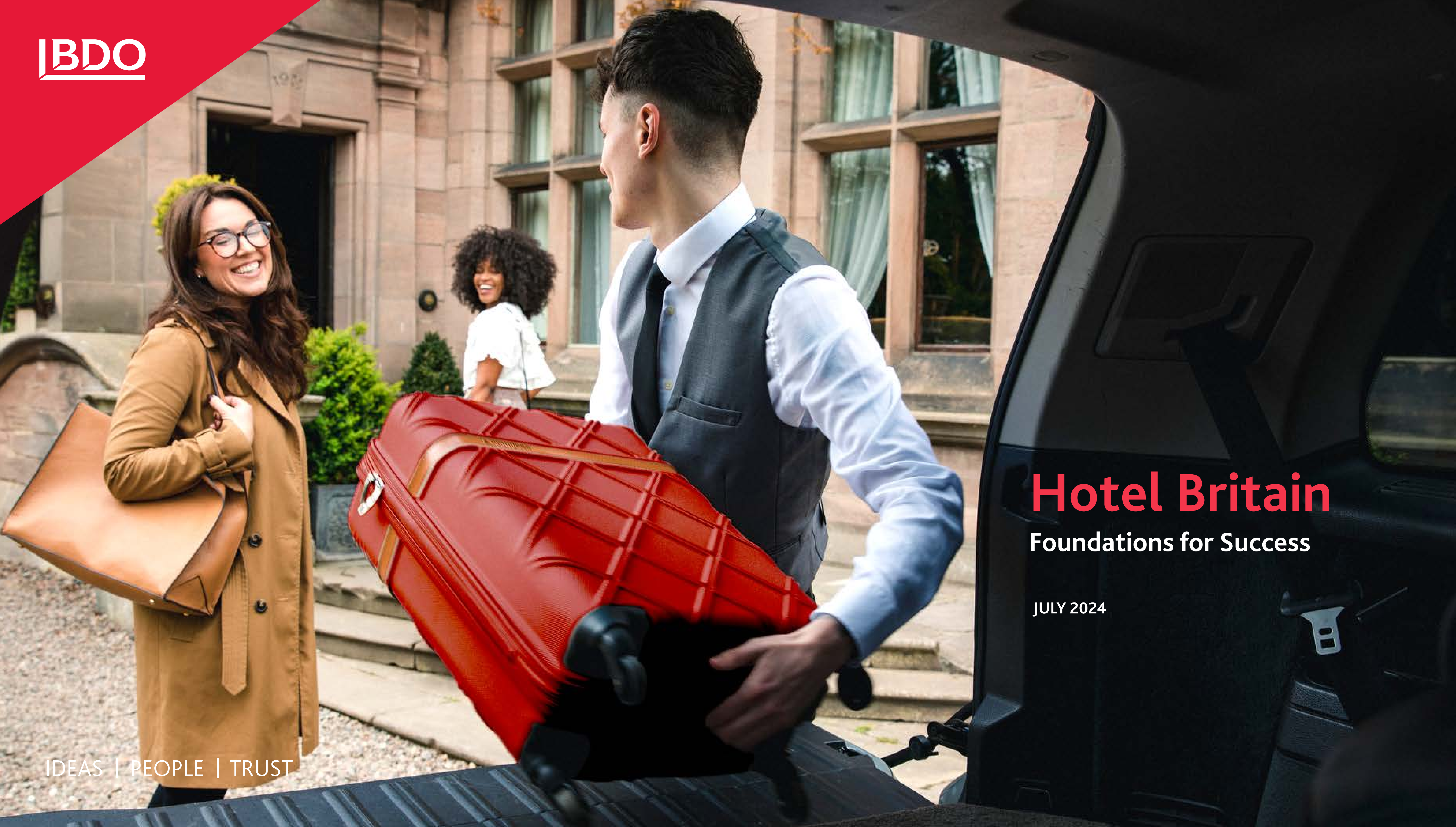


Hotel Britain

Foundations for Success

JULY 2024

IDEAS | PEOPLE | TRUST

Welcome to the Hotel Britain Report 2024

Foundations for Success

Once again, the hotel industry has adapted to a changing environment as the pent-up demand post-pandemic has begun to soften through 2023 and impact the first six months of 2024. The sector has remained resilient and agile and the economic outlook is looking hopeful for 2024 and beyond, so we believe there is a solid foundation for growth in 2025.

This edition of Hotel Britian includes an economic overview with data from the Centre for Economics and Business Research, industry intelligence from HotStats and a case study from Mollie's. This is all alongside our BDO hotel experts providing an update on tips changes, capital allowance, national minimum wages, and more.

CONTENTS

A word from Mark Edwards	3
Market Overview	4
In conversation with Darren Sweetland - Mollie's	10
Hotel industry Overview from HotStats	12
Unlocking guest loyalty and bridging the rebooking gap	15
New rules on tipping	17
National Minimum Wage	19
Capital Allowances	20
Data Protection Compliance	21
Corporate Criminal Offences	22
The challenges facing the hotel industry	23
BDO Sector Expertise	25
Contacts	26

A word from **Mark Edwards**

Head of Leisure and Hospitality

I am truly privileged to meet so many great hospitality businesses in my role, and it has been fascinating this year to hear many of them talk about mixed emotions as 2023 closed and 2024 began. There is some level of frustration that budgets weren't quite met and yet there were record years being reported for ADR. Costs have increased painfully, but rates have generally held and even the booking patterns, generally more last minute and less reliable as time has gone on – have been dealt with by revenue managers who are now much more used to the uncertain.

The requirement to hold one's nerve on price is not new but is being tested currently, particularly when the cost base operators have to deal with is much higher than in the pre-pandemic era. However, I believe a corner has been turned, and we can all look forward with a greater degree of cautious optimism than in recent years. The foundation has been laid and with proper planning to execute a strategy – which has built-in milestones and monitoring to allow adjustments as necessary, operators should feel confident in their chances of success.

I believe there are three key considerations that should form part of that planning process:

1 Focusing and delivering for your customer

Consumer behaviour and trend analysis are becoming increasingly important as the world adjusts to a post pandemic reality, with greater geo-political challenges, higher cost pressures on households, and businesses facing uncertainty in key geographical markets. Therefore, really knowing why someone would stay with you and more importantly, what would make them return and tell others about a positive experience is key.

2 Going green

Much is talked about the necessities to have a sustainable environmental plan but the reality is the next 5 years are going to see policy necessities driving behaviour as much as sentiment. Moreover, corporates globally are making environmental commitments, often with the easiest being to cut carbon emissions through reduced travel. However, we are seeing more business travel as the need for rebuilding human capital, the interaction of individuals doing business together, increases. It is a lot easier to justify that when the hospitality businesses' that facilitate the face-to-face interaction have tangible, preferably certifiable, environmental commitments.

3 Making the most of positive news

The reality is that there was such delight at the level of pent up demand post pandemic, that there was little time or energy for analysing what might happen as that naturally tails off. What we do know, though, is that all consumers are liable to be impacted by the unavoidable headlines about global crises, cost of living pressures and the need for greater investment. This creates a fairly negative cycle of news – but there is increasing evidence that this year will see the tide turn. Inflation, while potentially bumpy, is certainly nearer where it should be and this will lead to interest rate reductions. In the UK at least, there is a stable government and one that can lead across Europe which should increase the opportunity for inbound visits. Energy costs are falling and again while bumpy the shock factor has already been felt. We all have our part to play in making the most of the more positive news to benefit our sector and for that reason I am happy to say the deals market is picking up, lots of businesses have management teams that are strong and resilient and the underlying economic data is looking up. We should be proud of our sector and be confident in its future.

Market overview

The UK hotel industry started 2023 strongly but with greater uncertainty creeping in as the year went on - and it continues to face challenges throughout 2024 despite expected improvements to the economy. Although the spectre of inflation is receding, increased costs are putting industry growth prospects in danger.

Industry market analysis firm HotStats says housekeeping labour costs have risen 45% on 2019 levels, while laundry and dry cleaning is up 38% and complimentary items such as coffee kits and toothbrushes have increased by 35%. The hospitality sector also faces a wage bill increase of £3.2bn due to higher national minimum and living wages, according to trade body UKHospitality.

"Almost two-thirds of the sector's annual £5.4 billion investment in growth could be diverted into paying the new payroll and business rates costs," says the organisation, which is lobbying for a 30p-in-the-pound business rate, a reduction in national insurance contributions and a cut in hospitality VAT to 12.5%.

"Our sector firmly believes in paying people a good wage that reflects their value and importance to what we do," said UKHospitality Chief Executive Kate Nicholls. "But we need healthy and profitable businesses to do that, supported by regulation that doesn't penalise a community-based sector."

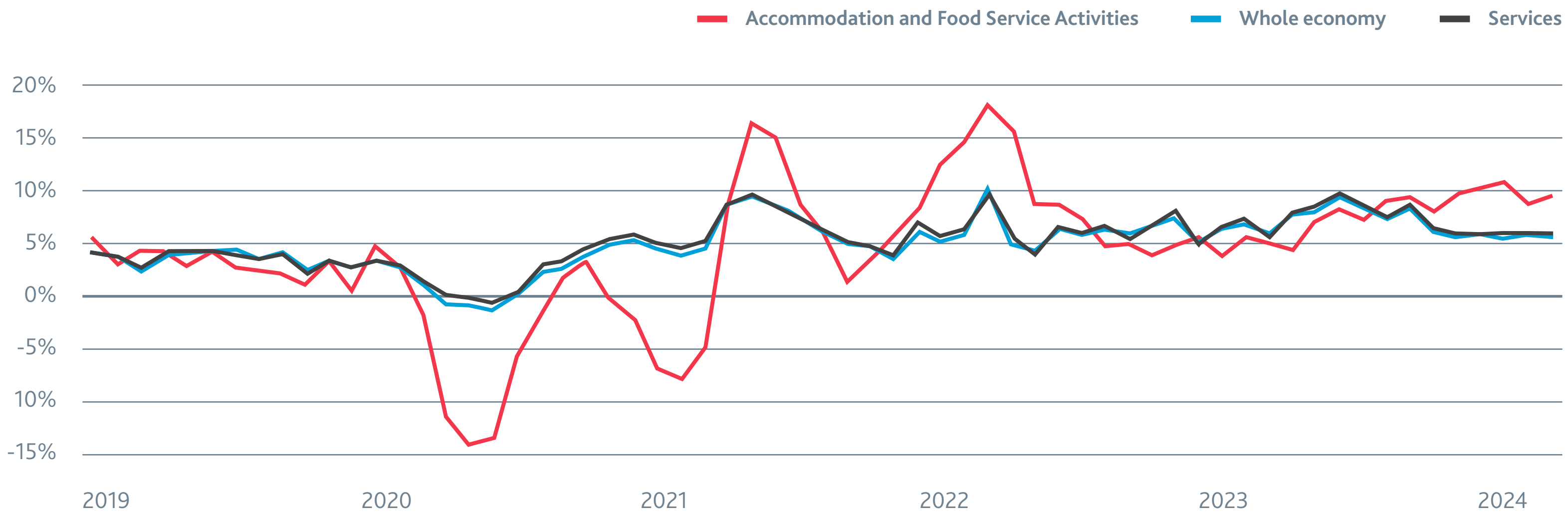
Pay growth in hospitality has surpassed that of the wider economy, says the Centre for Economics and Business Research (Cebr).

And this seems to be hitting the hotel industry's prospects, with Spain overtaking the UK as the world's favoured destination for investors in the sector and information provider Statista forecasting a drop in market size to £24.3bn in 2024. But that is only 2% less than 2023—and still above any other year previous.

An April survey by UKHospitality and the British Beer & Pub Association, Hospitality Ulster and the British Institute of Innkeeping found 50% of UK hospitality venues are just breaking even or operating at a loss, 70% have seen a reduction in profits, 66% have increased wage costs and 25% have no cash reserves.

Annual earnings growth

Source: Source: ONS, Cebr analysis



Market overview

If the hotel industry can manage costs, then the outlook is bearable. The UK is now officially out of recession, with the Cebr now predicting continuous modest quarterly GDP growth through to 2028 at least.

The economic consultancy is forecasting 1% GDP growth in 2024, along with improvements of 0.5% for productivity, 0.7% for consumption and 5.9% for earnings.

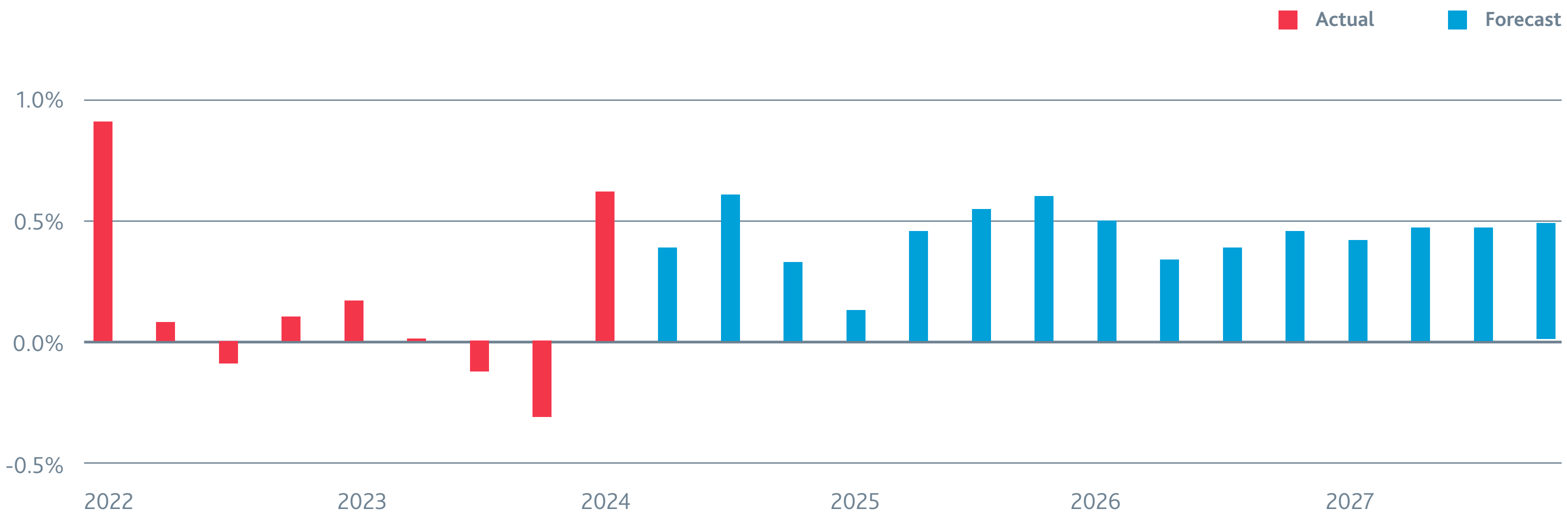
The Cebr also expects to see a 4.2% unemployment rate, up from 4% in 2023, 2.4% consumer price index inflation (down from 7.3% last year) and a Bank of England interest rate of 5.1% (up from 4.7%).

Economic indicators are more positive in 2024, but still weak by historical standards, says the Cebr. Nevertheless, consumer sentiment—which research has shown to be a key determinant of hotel occupancy, average daily rates and revenue per available room—is looking up.

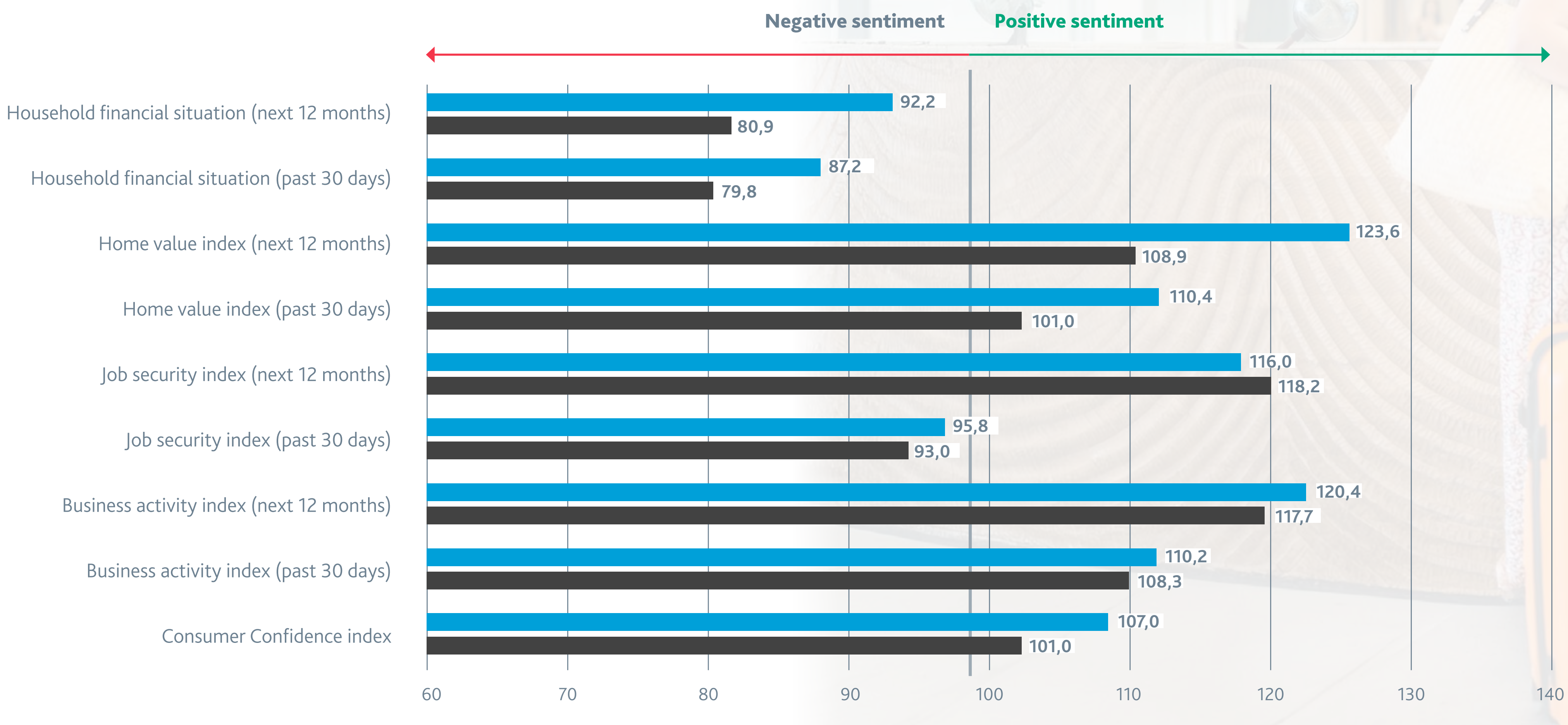
Despite the state of the economy, customer confidence was positive for most of last year, according to the Cebr's Consumer Confidence Index poll on YouGov. And eight out of nine confidence indicators had improved in the six months to March 2024.

Quarterly GDP growth

Source: Source: ONS, Cebr analysis



Market overview



Source: YouGove/Cebr Consumer Confidence Index

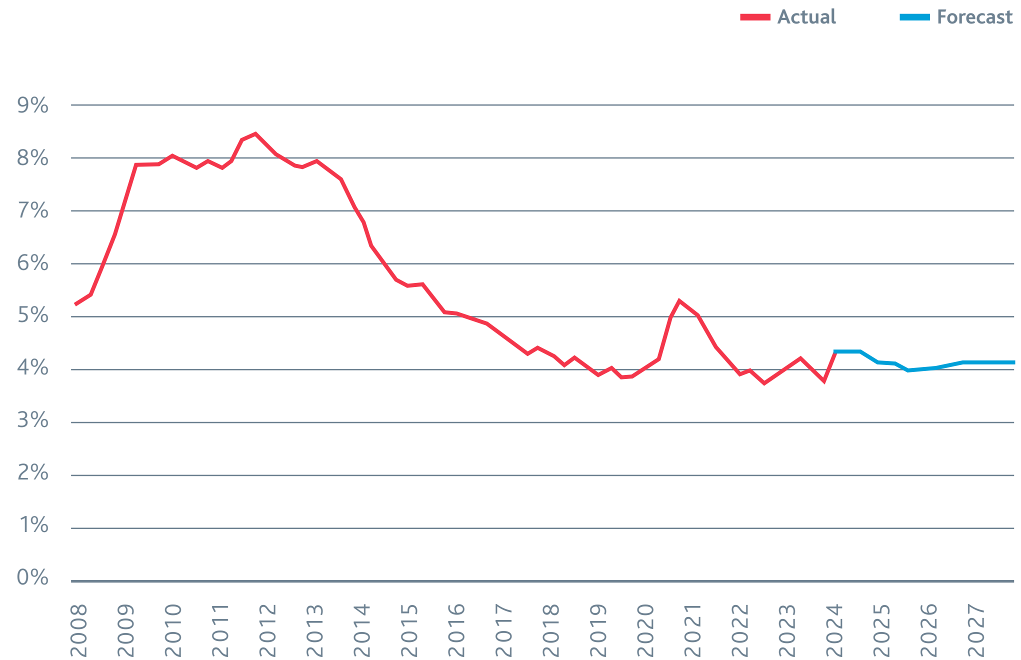
The only indicator that had dropped—the job security index—only saw a minimal fall, from 118.2 to 116. Another positive trend is that discretionary spend was expected to spike in the second quarter of 2024 and is forecast to continue rising thereafter, potentially breaking through the £250-a-week barrier this year.

Market overview

Meanwhile, the number of jobs in hospitality accommodation and food services is expected to fall slightly, to less than 2.5 million —possibly due in part to the shrinking hotel market. Hospitality vacancies are also on a downward trend, although this looks set to level off in 2024, the Cebr says.

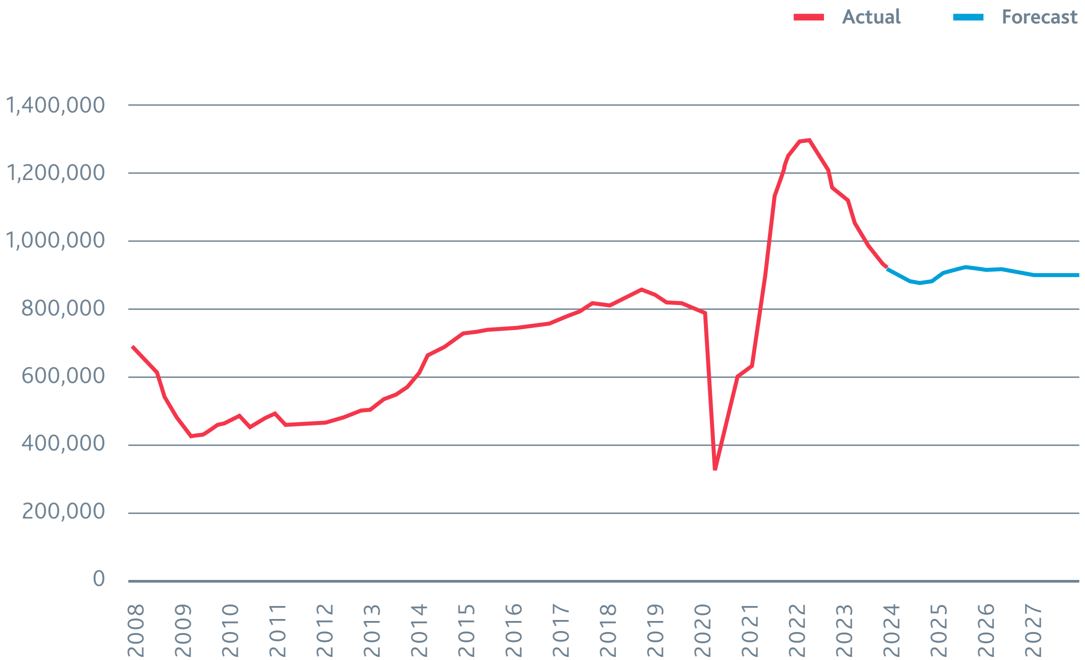
Unemployment rate

Source: Source: ONS, Cebr analysis



Number of vacancies

Source: Source: ONS, Cebr analysis

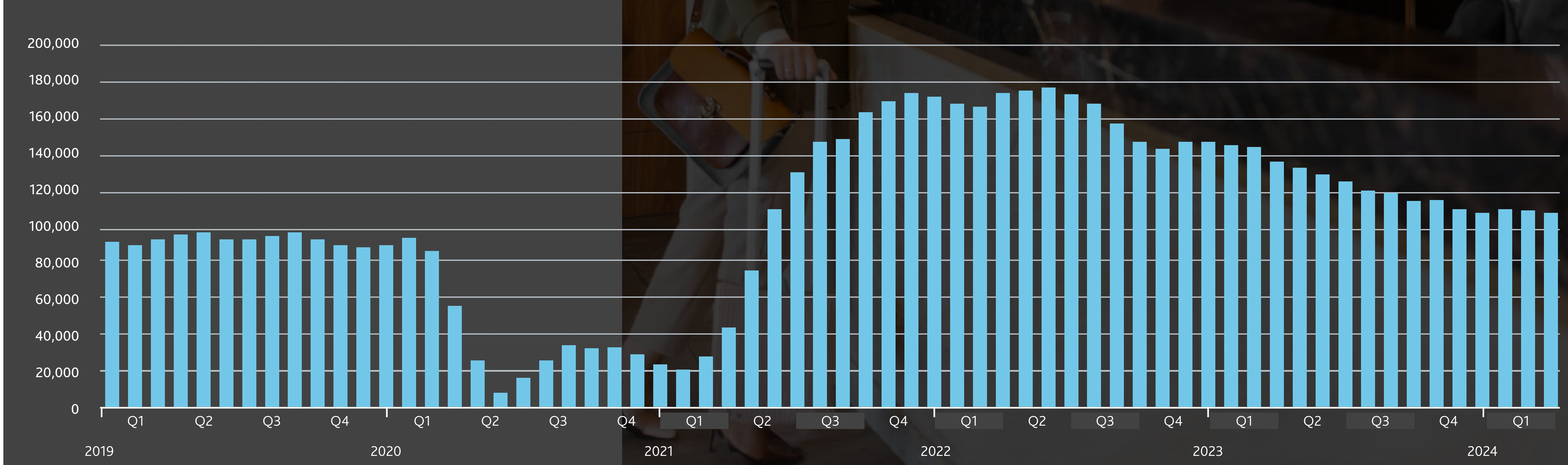


Market overview

Indeed, most of the key economic variables tracked by the Cebr look set to stabilise in the coming months and years following a period of significant turmoil.

Number of vacancies in accommodation and food services

Source: Source: ONS, Cebr analysis

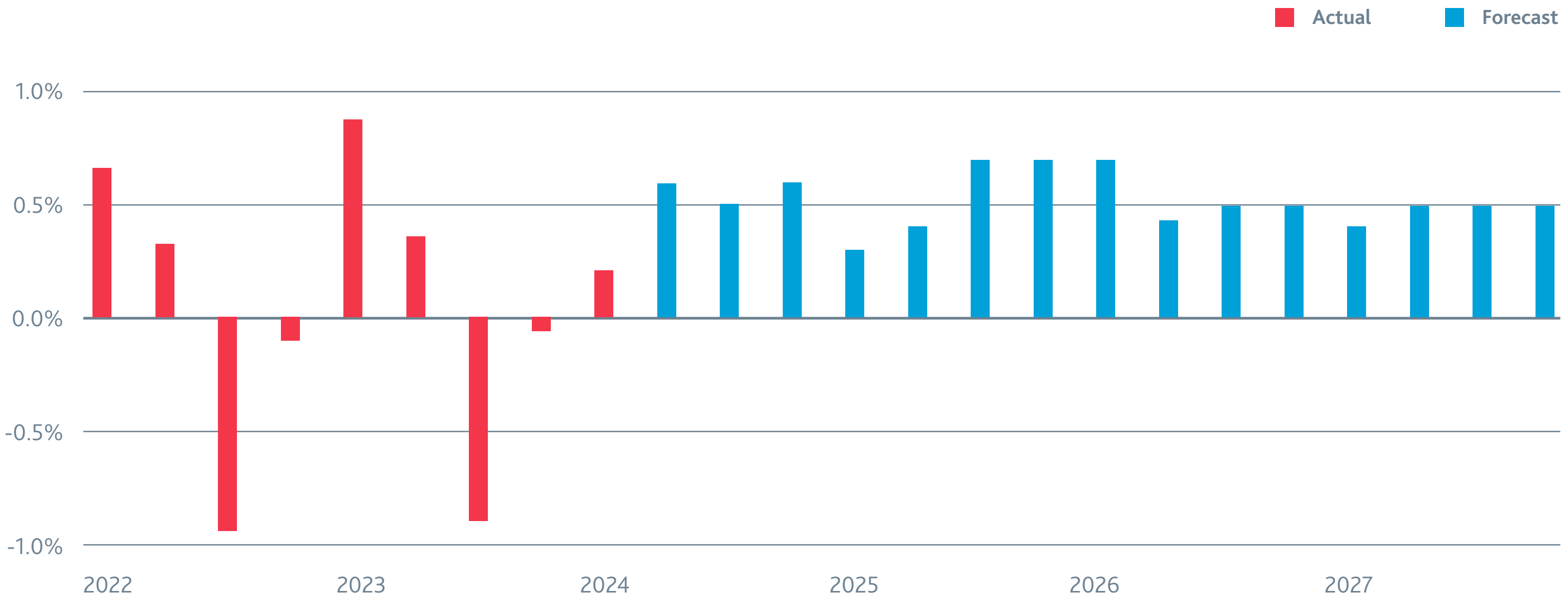


Market overview

The Cebr also expects interest rate cuts from the Bank of England in the second half of the year, although borrowing rates are unlikely to return to pre-crisis levels. Quarterly consumption, meanwhile, will return to growth, albeit hovering around the 0.5% mark.

Quarterly consumption growth

Source: Source: ONS, Cebr analysis



In summary, the Cebr is expecting—or perhaps hoping for—a few stable years ahead in terms of the economy, but not a return to the low-interest, higher-growth times.

For the hotel sector it will be important to overcome cost constraints and woo customers back in the wake of Brexit, COVID-19 and the cost-of-living crisis.

The international tourism signs are at least encouraging. According to national tourism agency VisitBritain, there were 38 million inbound visits to the UK in 2023, which was 7% below pre-pandemic levels but up 21% on 2022. Visitors spent almost 293 million nights in the country, up 1% on 2019 and 11% on 2022.

International tourism spending figures were more of a mixed bag because of the impact of inflation. Visitors spent a record £31.1bn, 17% more than 2022 and 9% more than 2019, although these figures were down 9% and 10%, respectively, taking inflation into account.

The average spend per visit was £819, nominally up 18% on 2019 and down 3% on 2022, but down 3% and 10% in real terms after inflation.

It remains doubtful whether UK hotels will be able to better these figures in 2024, although many in the industry will doubtless be happy just to have some months, or maybe even years, of certainty ahead now the UK General election is complete and such a significant majority has been secured.

In conversation with **Darren Sweetland** – Mollie's

Darren Sweetland
Managing Director, Mollie's

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Thank you for chatting to us Darren. Let's start at the beginning, please tell us how Mollie's was dreamt up.

The original idea came from Nick Jones MBE – the founder and then Chief Executive of Soho House. He recognised an unexploited gap in the roadside hospitality sector and set out to fill it with an elevated, contemporary take on the classic American-style motel and drive-in diner. The idea was to disrupt and innovate with a distinctive brand that offered a real alternative – high-spec, design-led, at an affordable price. Having worked closely with Nick on the Soho House expansion, I was invited to take on the role of Managing Director, to deliver the Mollie's concept and drive its evolution.

I took it on with a vision to redefine the concept of stylish travel; it's always been about building a resilient, resonant brand and offering as much as we can for the best possible price.

So far, you have two motel-diners (Oxfordshire opened in 2019 and Bristol followed in 2021) with a mega Mollie's in Manchester on track for early next year. We'd love to hear more about your new site and your future plans.

With a capital investment of approximately £30 million in real estate to date, Mollie's is set to open our third and largest motel in Manchester early next year.

Both the Oxfordshire and Bristol sites involved land acquisitions and design-and-build development – both were purpose-built with a view to creating a blue-print for future Mollie's; both are sited on suburban roadside sites. Mollie's motel in Manchester is a very different proposition, as it makes use of an existing building in the heart of a city.

Mollie's Manchester is a reinvention of the former Granada TV Studios – a familiar (we like to say 'iconic') landmark which has, in the past, been a beacon for Manchester's post-war regeneration and integral to the city's cultural identity. With a gym, a live music venue, meetings and event spaces, up-graded rooms and an integrated, Soho House members' clubs, the Manchester site is different but still very much Mollie's.

Meanwhile, we are planning to add meetings and events spaces to Mollie's Bristol – and we are looking for new sites. The company is aiming to announce more new roadside locations in the near future, and is looking at cities in Scotland, the North East and the South East. The longer-term ambition is to open 10 new Mollie's as soon as possible.

As we all know, the hotel industry can be tricky at the best of times, how have you used your strong branding to secure excellent reviews and maintain a steady flow of bookings?

Like any start-up we've had our fair share of hiccups – not least, the pandemic which hit just before Mollie's Bristol was due to open – but from the outset, Mollie's has achieved consistently excellent customer feedback. And despite the prevailing economic climate, within 12 months the company was EBITDA profitable – exceeding all expectations.

The 'designed by Soho House' tag has clearly helped put us on the map, especially in terms of press coverage, but our real strength is in delivering our promise: an innovative hotel brand known for its carefully curated design, cutting-edge technology and dedication to exceptional service.

In conversation with Darren Sweetland – Mollie's

Mollie's has successfully built a strong brand that resonates with our guests – and this is reflected in the consistently high guest-satisfaction ratings on public review sites and our internal mystery diner performance KPIs.

As well as exceptional guest satisfaction ratings across leading platforms, Mollie's has achieved strong PR and digital engagement within a short period of the brand's growth.

In 2021, shortly after the Bristol opening, Mollie's was The Times' 'Budget Hotel of the Year'.

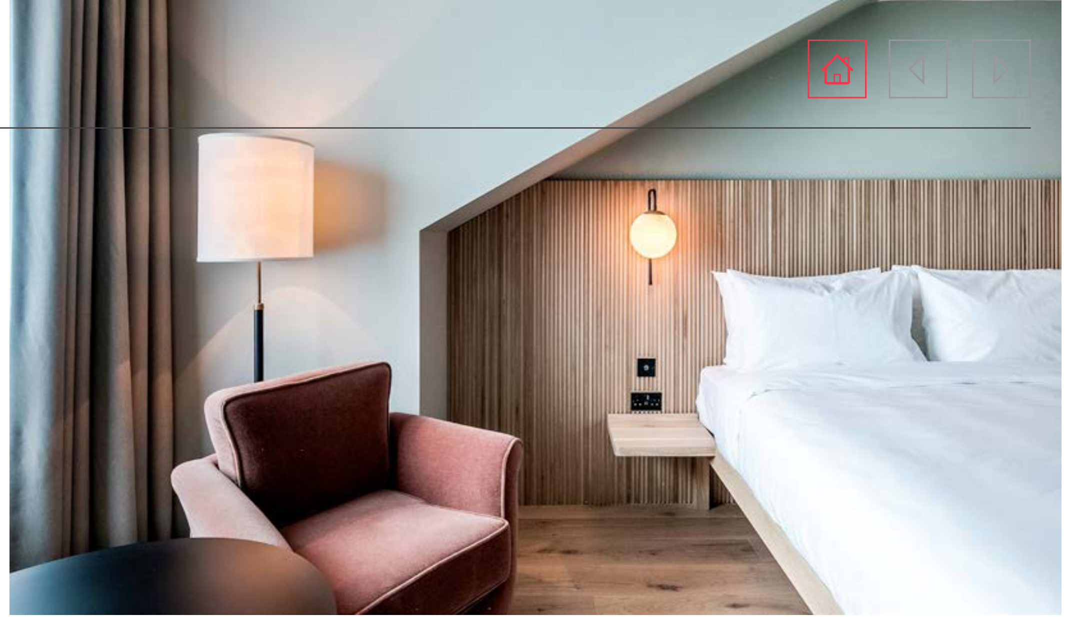
Tech is becoming increasingly important for hotels to maximise customer experience. How are Mollie's using it and where have you seen the most success?

In addition to our real estate investments, Mollie's has invested heavily in an advanced IT ecosystem which won Best Use of Technology in Hospitality in the Catey's Awards. Leveraging cutting-edge, open AI platforms, our integrated system connects all areas of the business, fostering data-driven decision-making. This technology not only enhances operational efficiency but also alleviates repetitive tasks for our teams, allowing them to focus on delivering a seamless customer journey.

Our investment in technology allows future scalability, transforms the guest experience, removes operational inefficiency and provides a platform for making the right decisions to grow. The Mollie's app, for example, opens a raft of benefits for our guests: online check-in, digital room key, pre-booked EV charging, TV casting, 24-hour online chat support in multiple languages, among many other benefits.

Looking to the new 12 months, what trends do you see evolving and how will that impact Mollie's?

Guests are seeking unique experiences. Mollie's are responding to that demand by curating bespoke experiences through our technology. The increasing use of AI to personalise the guest journey and enhance guest convenience (for example, 24/7 chat, CRM and mobile app) alongside support to the back-of-house operational infrastructure (things like revenue management and data analysis). Mollie's are looking to leverage AI to analyse data enabling better forecasting, dynamic pricing and targeted marketing strategies.



Guests are increasingly prioritising sustainability – and our industry holds a unique and powerful position in driving sustainable practices. Mollie's is in the process of obtaining our B-Corp accreditation prioritising sustainability to form part of our core values and long-term vision. Our commitment to minimising environmental impact and fostering positive social change is at the heart of everything we do. Over the past 12 months, we have made significant strides in our efforts, achieving notable progress in community engagement, diversity, inclusion and employee development initiatives while reducing our environmental footprint.

Another industry trend is the growth of loyalty programmes designed to encourage direct bookings. Mollie's is working on enhancing our CRM data analytics to drive direct bookings and reduce reliance on third party booking platforms.

Any final words...

Our focus on providing seamless guest experiences is underpinned by the best technology and an unwavering commitment to our people and their development. By investing in our people, we maintain high standards of service and offer a market-leading product at a competitive price. Mollie's reputation for quality and value is a testament to our ongoing efforts to exceed guest expectations.

Hotel industry Overview from HotStats

Michael Grove
CEO, HotStats

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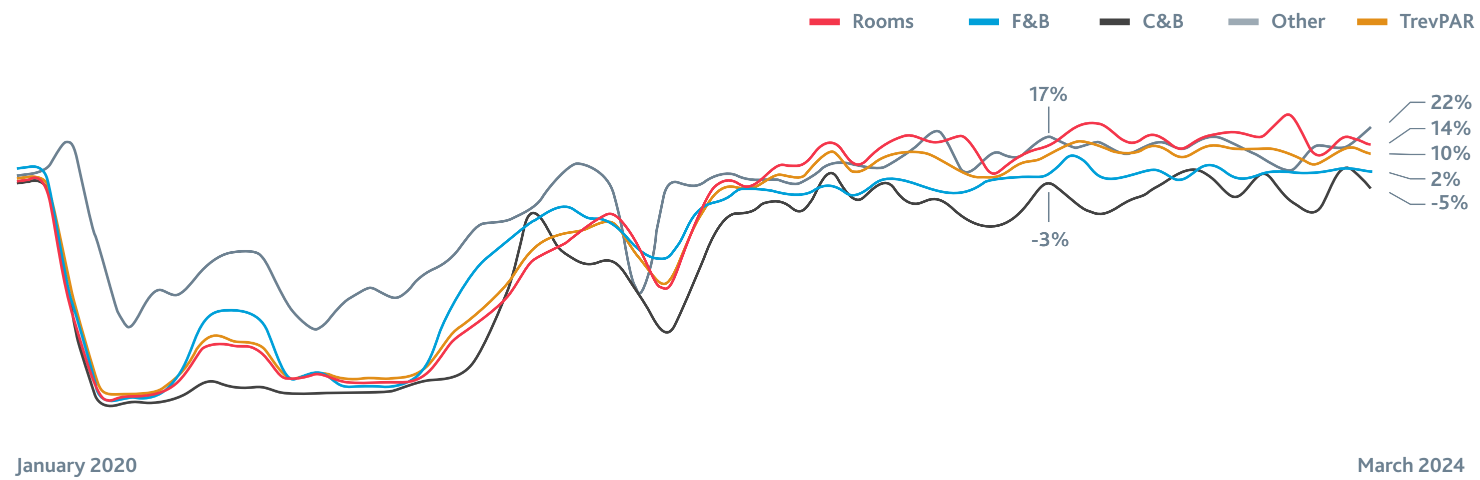
Hotel Britian is delighted to have hotel industry bench marking data and commentary from Michael Grove, CEO of HotStats. HotStats enable the industry to understand hotel profitability like never before with intelligent benchmarking, financial performance reporting, market data and insights, all in one place.

HOTSTATS
Hospitality Intelligence

The Recovery Position
Month to month Index vs 2019 - Revenue PAR - UK



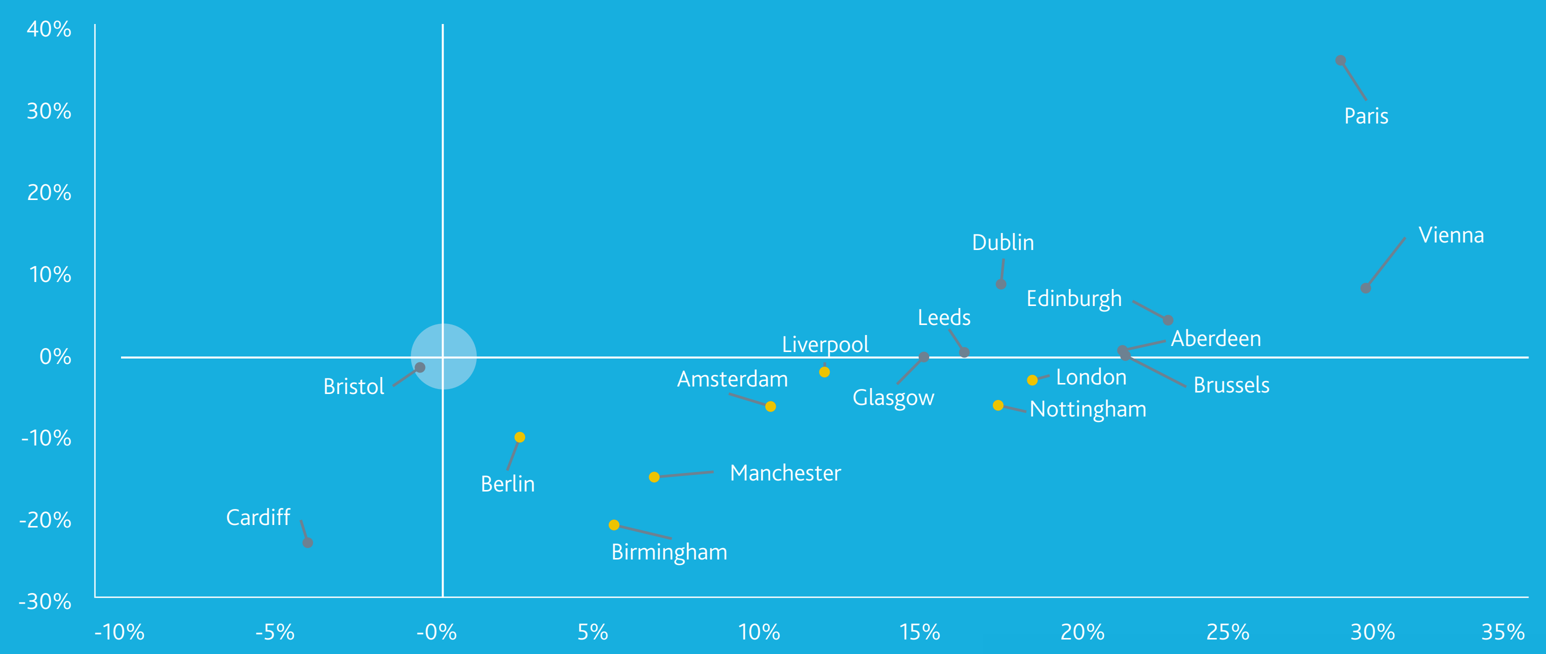
The Recovery Position

Revenue Per Available Room (RevPAR) data for the UK indexed back to 2019 generally paints a moderately positive picture, while Food and Beverage (F&B) revenues have been flat since March 2023. C&B (Conference and Banqueting) is down two percentage points versus last year at -5%, which is a bit of a sticky start to the year.

Room revenues in the UK are following the same pattern as Europe at +14%, 1PP higher than March 2023. This indicates a more positive growth picture and support the growth of overall TrevPAR to 10%.

More recently

TrevPAR Change % vs GOP Margin % Change - Rolling 12 months to March 2024 vs 2019



Considering the TrevPAR margin change v Gross Operating Profit (GOP) change since 2019 by key cities, we see Bristol and Cardiff struggling both with revenue and their conversion to profit. For London and all of those in yellow, there is a greater need for cost focus where revenue conversion has been more challenging.

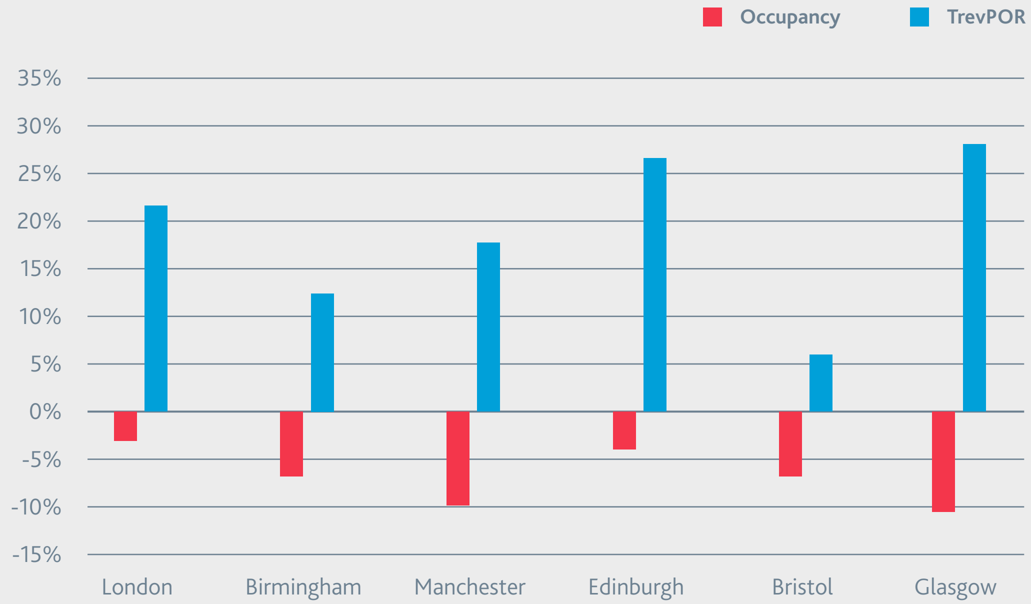
Occupancy Challenge and Revenue Gain

This is where we might strike a continuing note of caution for 2024. Hotels have been doing more with less and leaning on the Average Daily Rate (ADR) to head off some of those economic headwinds.

However, HotStats are keeping an eye on this. With the potential softening of the demand that was so strong in 2022 and 2023, there may be a developing struggle here. While the main focus remains maintaining Total Revenue, it is the costs, particularly for labour, that are creating that pressure on profitability – and this is compounded by reductions in occupancy numbers. ADR is the crucial element that has been holding the profitability puzzle together, and getting the balance right is going to be even more important through 2024 where the ADR and other revenue increases that we have enjoyed over last year potentially start to soften, and the occupancy levels continue to remain sluggish.

Occupancy Challenge and Revenue Gain

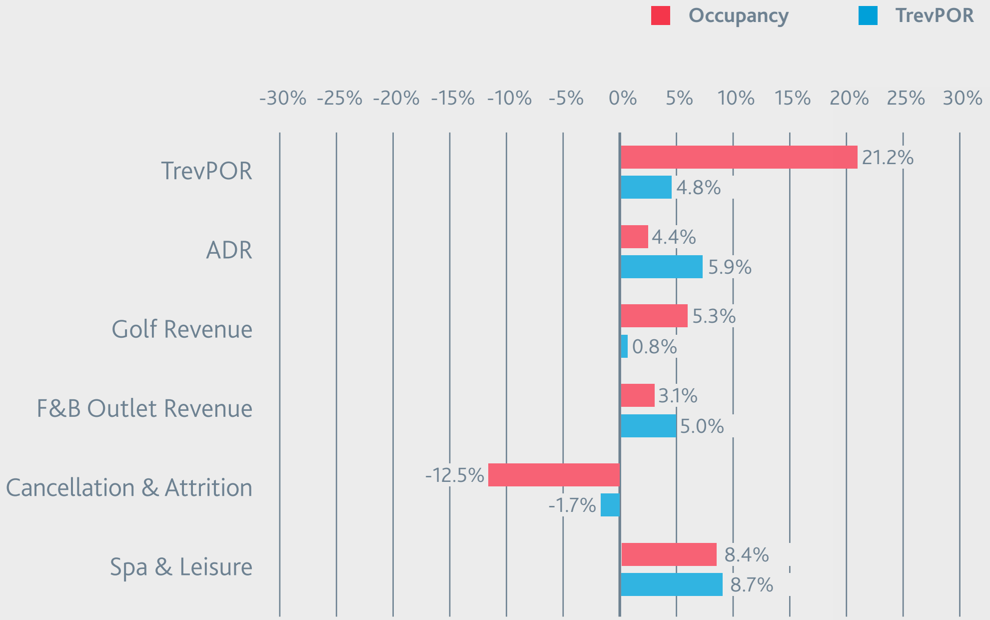
% Change - March 2024 Rolling 12 Months vs 2019 - UK Key cities



Hey Big Spender

Total Revenue POR-% Change 12 Months Rolling March - 2024 vs 2023

HOTSTATS



Looking now at how revenue is split by type and region, we can see rooms revenue driving that total revenue piece. For F&B outlet revenue, this small growth is currently not enough to keep up with the costs. Menu prices have increased and guests are still prepared to pay up to a point, however we will also see the profitability being challenged. The attrition and cancellation rate at -12.5% comes from 80% attrition and just 20% from cancellation; because of this we are seeing a change of strategy in how hoteliers are holding event organisers to account for their uptake of contracted F&B and rooms. This revenue stream has declined significantly, both since the pandemic and since last year, where it stood at +37.3% v 2019.

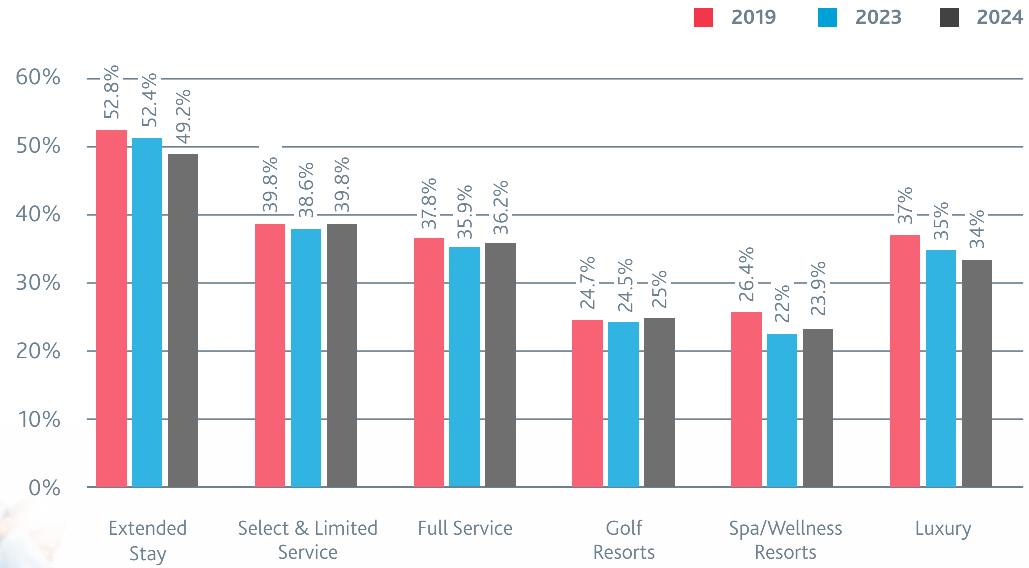
The Margins

Looking at Gross Operating Profit (GOP) margin by asset type for the UK, despite the high ADRs and revenue increases, the overall profitability picture shows the struggle across all asset classes. There is a lot of pressure here, and this likely will not be changing to any significant extent in the coming year. Only the Golf resorts and select service seem to be holding their own and interestingly, perhaps a nod to the times that we find ourselves in….

The Margins

Gross Operating Profit Margin - Asset Type 12 Month Rolling March 2024 - UK

HOTSTATS



Total hotel revenue PAR is sitting at £162.07 v £150.71 LY , up by around 7.5% . Total hotel revenue is driven by rooms and ADR, holding up profitability against the headwinds that we have examined. The dilution of ADR with cheaper segments is just not one that hotels are able to entertain, and we can see that despite the hikes in overall revenue, hoteliers are still not able to improve GOP, only just holding the status quo v LY and 1.7PP down on 2019 levels.

So what picture does all of this paint? A tricky balancing act – some positivity continues, but all of this underlines the importance of evaluating every revenue stream and all of the related costs to balance the profitability picture in the year to come.

Unlocking guest loyalty and bridging the rebooking gap

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BDO is pleased to have spoken to Agilysys' about their latest research into guest loyalty, looking at ways hoteliers can increase rebookings and attract new guests.

Agilysys' research has confirmed what we always suspected; hospitality can be a tough industry. However, small tweaks to business models can substantially increase profitability and loyalty is a major player in the key to success. If that aspect can be enhanced by clever technology, then why not consider the benefits of increased automation? Whether it is to reduce guest waiting times by boosting efficiencies or by offering better, personalised options to each guest—there are lots of quick wins here that can have a significant impact on the business's bottom line—and ultimately, craft a memorable experience.

There are times when human interaction is welcomed and times when it is not so welcome, and although it is easy to assume we might know what a guest might like, there are always exceptions. Therefore, it is more important now than ever for hotels to truly understand their key audience and the type of experience they're looking for. Once these nuances have been established, hotels will be in a stronger position to offer meaningful personalisation and employ a tech stack that supports your business.

There is rarely any harm in making a guest feel special, but finding the best way to do so, and leaning on technological advancements is always a positive step towards an exciting new era of hospitality.

Unlocking Guest Loyalty

There are several things hoteliers can do that consumers say would make them more likely to rebook a venue.

Central to success is harnessing the right technology to create seamless experiences end to end from booking to check-out and even after the stay to cement guest loyalty. Almost two-thirds (64%) of consumers said that staying at a hotel where wait times are reduced across all touch points would make them more likely to rebook. 62% of survey respondents said they would be more likely to leave a negative review as a result of a bad experience with wait times. Hoteliers should take this to heart as more than half (52%) of UK travellers surveyed indicated they read reviews every time before booking a hotel.

Just **27%** of UK travellers have re-booked a hotel in the last 12 months.

So, how can hoteliers keep wait-time to a minimum and elevate the overall guest experience end to end?

Of survey respondents that did rebook a venue, **48%** said they chose to rebook because the venue delivered an exceptional experience end-to-end from booking to check-in, services, activities, dining, and check-out.

Booking

Simplify booking with a user friendly mobile-first approach.

Ensure quick response times and personalise offers based on guest data. Enable guests to upgrade their rooms and book extras to maximise revenue per guest.

Check-in

Offer guests options such as mobile app or kiosk check-in. Promote the benefits of app-based check-in and use the process to promote the hotel's amenities and upgrade options.

Service

Provide convenient services such as on-demand ordering and cashless transactions, integrating loyalty programmes and special guest offers. Enabling food and beverage delivery anywhere on property increases satisfaction.

Food & Beverage

Provide convenient services like on-demand ordering and cashless transactions, integrating loyalty programmes and special guest offers.

Check-out

Enable guests to choose traditional front-desk assisted, mobile or kiosk check-out options, emphasising speed, preference, and convenience.

Post-experience

Continue to engage with guests after their stay through personalised marketing driven by guest preferences, loyalty initiatives, and feedback, via email and SMS messaging.

The power of reviews

The power of reviews cannot be overstated. They are pivotal in shaping a potential guest's choice in where to stay and can significantly impact a hotel's reputation and overall loyalty scores. The Agilysys study uncovered several statistics that highlight the critical role of reviews.

59%

Influencing booking decisions:

59% of potential customers said they would be less likely to book a hotel if they read a bad review.

53%

Review reading habits:

More than half (53%) of people read reviews when booking a hotel. They are an essential part of the decision-making process for many travellers.

38%

Reviews as decision-makers:

Almost four in ten (38%) said reviews could be the deciding factor when choosing between your hotel and another venue.

63%

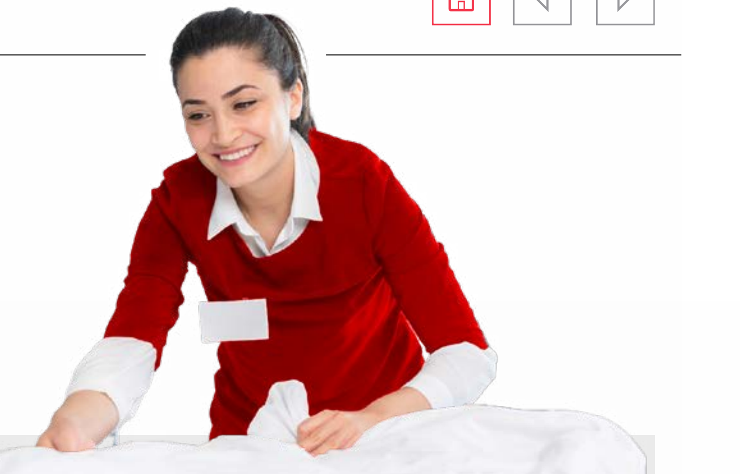
Encouraging guest feedback:

A negative hotel experience can lead to a surge in reviews. Sixty-three per cent of people are more likely to leave a review after a negative experience.

Every interaction counts in hospitality. Disappointing guests can result in negative reviews. While investing in staff training and instituting best-practice protocols can counter the likelihood of disappointing a guest, leveraging innovative technology to remove friction and wait times from processes and provide staff with guest preference insights that can help them take the best actions in the right moments is a smart way to aspire to clear the high bar of never disappointing a guest.

Technology, at key touchpoints such as booking, check-in, service, dining, check-out, and post-experience, plays a crucial role in ensuring guests have positive and enjoyable experiences end-to-end, ultimately leading to positive reviews.

You can read Agilysys' full report and findings here.



New rules on tipping – are you prepared?

Jacqui Roberts
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From 1 October 2024, the Employment (Allocation of Tips) Act 2023 will require employers to ensure that workers receive the full tip from a customer. The overhaul of tipping practices is set to benefit more than 2 million UK workers across the hospitality sector.

The legislation places a legal obligation on businesses to distribute all discretionary tips, sets out a time frame in which to distribute them and a requirement to implement a business policy ensuring fair and transparent distribution of tips.

Key points of the new rules on tips

What is a tip?

The legislation applies to 'Employer-received' and 'Worker-received' tips. As well as payments, tips also include vouchers, stamps, tokens, casino chips or similar with a monetary value or capable of being exchanged for money, goods or services.

How should tips be paid?

All tips, service charges and gratuities must be paid to workers and cannot be subject to deductions including administrative fees. Tips must be paid to workers by the end of the month following the month they were paid by the customer. Tip distribution must be fair and transparent with due regard to a Code of Practice (COP), this can include a tronc arrangement.

Paperwork

There must a written tips policy to include whether the employer requires or encourages customers to pay tips and how the employer ensures that all qualifying tips, gratuities and service charges are paid and distributed fairly. The employer must retain a tipping record of the total tips received and details of their allocation to workers for up to three years.

What are workers' rights?

Agency workers will be entitled to receive tips in the same way as employees. All workers will have the right to request details of the total amount of tips received and the amount paid to them. Employees and agency workers can raise a tip dispute through an employment tribunal and have 12 months to make a claim.

Supporting Code of Practice

Following public consultation, the Department of Business & Trade released the final draft Code of Practice on 22 April 2024 to support the new legislation to promote fairness and transparency.

Changes to the COP since the consultation draft, although small in number, provide some further clarity in a few areas. This includes confirming that tips that a customer pays direct to workers digitally via an app are not 'employer-received' and are therefore outside the scope of the legislation. In addition, an agency employer will be required to distribute the tips to their workers once allocated by the Employer.

You can read the code in full here.

How should tipping work until 1 October 2024?

Before October 2024, employers may apply a discretionary service charge to bills. Legally, the service charge belongs to the employer until it is transferred to an employee in full or with a deduction made by the employer. The tips can be paid to the employee by the employer via the payroll subject to PAYE/NIC or by a troncmaster where a tronc scheme is in place. Typically, deductions are made from the tips to cover certain costs such as credit card charges or the cost of administering and paying the tips to employees.

Tronc arrangements

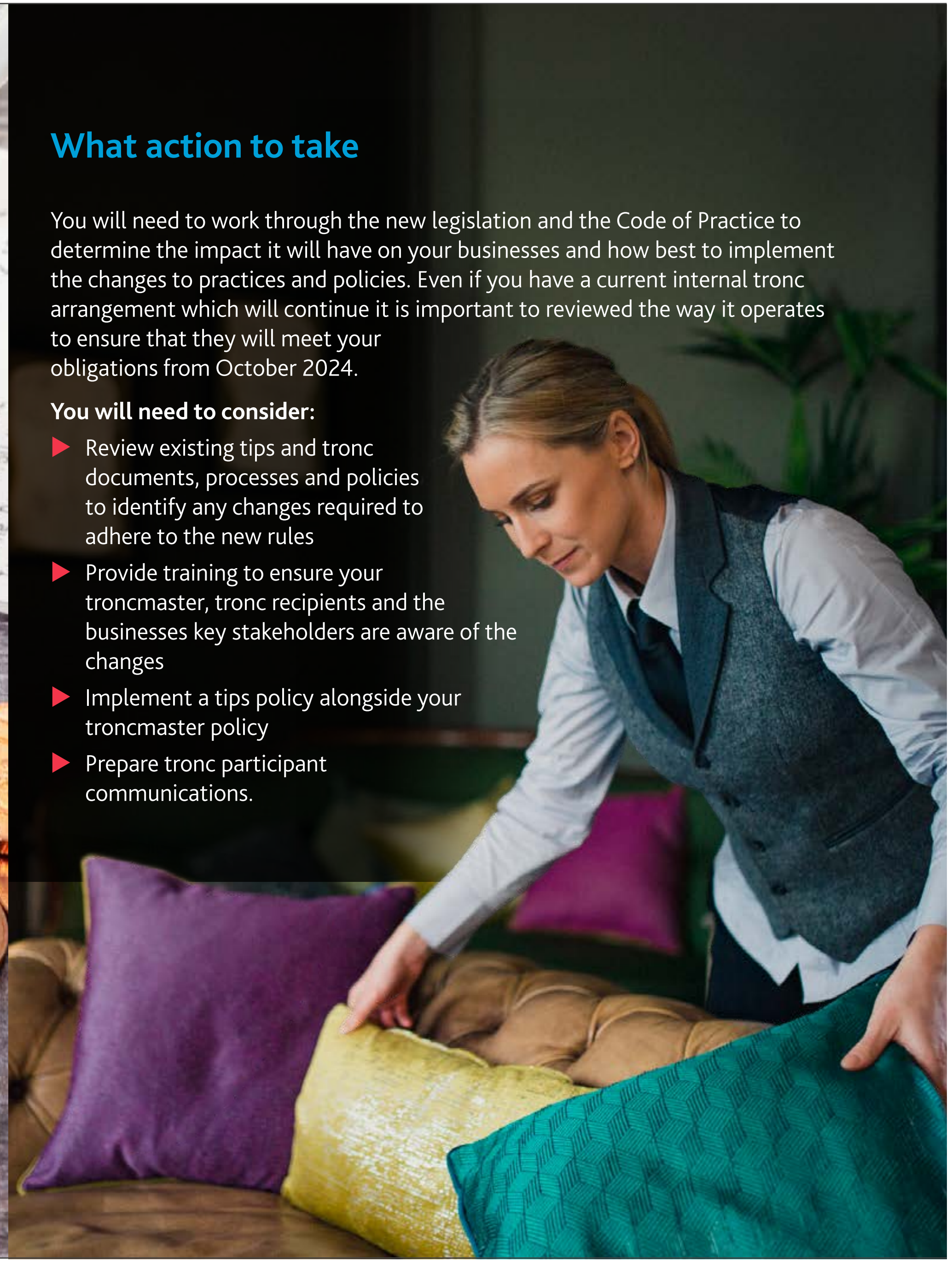
The majority of businesses currently use a tronc arrangement overseen by a troncmaster to manage the allocation and distribution of tips. They are typically a general manager, who independently oversees the allocation of tips and administers the arrangement. Neither the employer nor its senior management can be the troncmaster, but the employer can have oversight of the appointing or removal of a troncmaster. The advantage of a robust tronc scheme is that the tips are exempt from Class 1 employers and employees NIC.

What action to take

You will need to work through the new legislation and the Code of Practice to determine the impact it will have on your businesses and how best to implement the changes to practices and policies. Even if you have a current internal tronc arrangement which will continue it is important to reviewed the way it operates to ensure that they will meet your obligations from October 2024.

You will need to consider:

- Review existing tips and tronc documents, processes and policies to identify any changes required to adhere to the new rules
- Provide training to ensure your troncmaster, tronc recipients and the businesses key stakeholders are aware of the changes
- Implement a tips policy alongside your troncmaster policy
- Prepare tronc participant communications.



National Minimum Wage

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From 1 April 2024, the National Living Wage (NLW) was extended to apply to workers aged 21+ and increased to its highest ever amount. There were also significant increases to the other National Minimum Wage (NMW) age and apprentice rates.

While it is important to consider the impact of the increase, it is worth remembering that NMW compliance is more complex than simply paying at the correct rates, and with penalties of up to 200% of any underpayment and the possibility of being 'named and shamed' publicly, there are both financial and reputational risks to getting things wrong.

HMRC Activity – How likely are HMRC to enforce in hospitality?

We have seen recent HMRC activity in the Hotel Sector, asking employers to review their practices and assurances against NMW rules. The common areas of risk HMRC are asking employers to check are:

- Apprentices
- Deductions from pay for items in connection with the job
- Deductions or charges for accommodation
- Paying workers for all time worked.

There are other areas of focus during any enquiry, but we do recommend hoteliers regularly review their business' NMW compliance to they aren't inadvertently underpaying their workers through a technical breach of the rules ahead of any potential HMRC activity.

How to check current NMW compliance levels – where to start

The first things to check are entitlement to NMW and worker status. A worker may be self-employed for tax and NIC purposes but also a "worker" for NMW purposes and, therefore, be entitled to at least the minimum rate for their age.

There are five other key areas to consider:

1. **Worker type.**
   Failure to classify worker type correctly can result in incorrect pay calculations and hence underpayments. There are four worker types for the NMW: salaried, timed, output and unmeasured — all have strict criteria to be met. A common error here is when someone paid an annual salary is automatically assumed to be a "salaried" worker: if the criteria are not fully met, there is a risk they could be working more hours than their salary covers for NMW purposes.
2. **Working time.**
   All working time must be paid: this may be more than contracted hours.
3. **Pay frequency.**
   It does not matter when wages are paid, the important thing is the period the payment covers. A pay reference period can't be longer than a month.
4. **Different elements of pay.**
   NMW pay is not the same as total gross pay — some payments, such as overtime and bonuses, can't be included.
5. **Deductions.**
   Deductions from wages can result in underpayments for NMW if not within allowed categories, even if the worker agrees or opts for the deduction. For example, an employee signing up to a savings club or taking advantage of a benefit through a salary sacrifice scheme could result in a breach.

Careful consideration of all of the above, alongside robust processes and controls, record keeping and monitoring of evidence that NMW is being paid are vital for your hotels business.

Capital Allowances

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The UK capital allowances regime has never been as generous for corporation-tax-paying businesses, with multiple opportunities for hoteliers investing in their properties, portfolios, and equipment to accelerate claims for tax relief.

Between March 2021 and April 2023, temporary new first year allowances known as the 130% super-deduction and 50% Special Rate (SR) allowance were available for businesses to claim on plant and machinery investments. These allowances have now ceased and have been replaced with 100% full expensing and 50% first-year allowance for plant and machinery expenditure incurred after 1 April 2023. First year allowances are an alternative to writing down allowances - the normal expenditure on plant and machinery is claimed over time at 18% for main rate plant and machinery and 6% for special rate pool plant and machinery.

For example, a corporate tax-paying hotelier incurring annual building maintenance and furniture, fixtures, and equipment (FF&E) expenditure can claim 100% full expensing for expenditure on assets such as TVs, beds, wardrobes, carpeting, fire alarms and catering equipment (all being main rate plant and machinery), rather than claiming these at 18% per annum by writing down allowances. Special rate plant and machinery includes integral features to a building (i.e. lighting, electrical systems, heating, air conditioning, water systems, lifts, escalators, and solar shading) as well as solar panels. Expenditure incurred on such assets would qualify for the 50% first-year allowance rather than the 6% writing down allowance.

Full expensing and the 50% first-year allowance were initially introduced as temporary during the period 1 April 2023 to 31 March 2026, but an announcement in the Autumn Statement in 2023 confirmed the first-year allowances would be made permanent, providing businesses with greater certainty for investment decisions.

Any hoteliers and hotel investors that are considering carrying out building projects, be it refurbishments, new builds, or extensions, should carefully consider whether the first-year allowances claim could make investments more viable and ensure they are utilised whilst they are available.

In the 2024 Spring Budget, the Government announced the abolition of the Furnished Holiday Let (FHL) regime, which provided taxpayers with preferential tax treatment allowing lower capital gains tax rates, the full deduction of mortgage interest payments and the ability to claim capital allowances on the FHL property. It is expected that FHL businesses will instead be treated as normal property rental businesses, which will restrict interest deductibility and capital allowances claim on residential properties. The FHL regime will cease from April 2025, and as of the date of writing, there has been no detail shared from HMRC or the Government on how current FHL businesses, including those embedded within hotel groups, will be wound down or transferred to a property business and what will happen to capital allowances pools still within these businesses.

Data Protection Compliance

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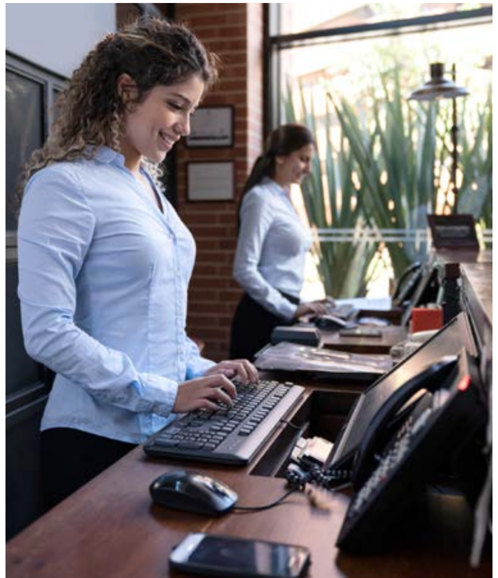
Since the UK data protection regulatory landscape changed in May 2018 with the introduction of the UK Data Protection Act 2018, hotel operators have had to grapple with the challenges of both meeting and evidencing compliance with data protection requirements.

2024 – the challenges facing the hotel industry

The Information Commissioner's Office (ICO) remains one of the most active regulators in Europe, publishing enforcement action on an almost daily basis, and has a range of powers at its disposal, including financial penalties (up to £17.5m or 4% of global turnover), reprimands, enforcement notices, and in some instances individual prosecutions.

ICO enforcement action is publicly available, and often picked up by media outlets. This can affect an organisation's reputation, reducing consumer trust and ultimately impacting the bottom line, especially in a market where consumers have the ability to move their purchasing power elsewhere. At a time when there are significant cost and inflationary pressures on hotel operators, and when margins can fluctuate - fines for data protection non-compliance could have a significant impact.

It's also worth noting that the ICO has been active in the sector, following a high-profile data breach which affected millions of guest records and resulted in the ICO issuing an £18.4m penalty to an international hotel operator.



How should hotel operators respond to these challenges?

1. **Tone at the top** – ensure that key decision makers are aware of the risks of non-compliance and allocate sufficient time and resources to implementation and continued compliance efforts.
2. **On-going employee awareness** – Embedding data protection training in the employee lifecycle is a key control to ensure that employees understand and follow key data protection processes, particularly in relation to data breach reporting and managing data subject rights requests, where key time limits apply.
3. **In-house expertise** – Our experience has shown that often, the responsibilities of the data protection lead are often 'bolted-on' to an existing role (i.e. CFO or Head of Compliance), when in reality, the individual lacks the time, resource and expertise to maintain data protection compliance effectively. Hotel operators should therefore consider whether there is sufficient expertise in-house or whether it would be prudent to seek support from a third party in an outsourced capacity.
4. **Oversight of data processing and third-party exposure** – Hotel operators often struggle to maintain a documented oversight of data processing activities which have an exposure to third-party data transfers. This is crucial to ensure that existing contracts are in place with each third party which include relevant data sharing and international data transfer clauses.
5. **Consent processes** – Hotel operators often actively promote marketing content to guests but should be aware of the requirement to evidence the time and date any guest consent was obtained, and to ensure that robust consent management processes are in place, if an individual was to subsequently withdraw their consent.

Corporate Criminal Offences

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In 2017, the UK government introduced a pivotal piece of legislation that has significant implications for all businesses, including those operating in the hospitality sector: the Corporate Criminal Offences (CCO) legislation.

This legislation comprises two offences: one for the facilitation of UK tax evasion ('the domestic offence') and another for overseas tax evasion ('the overseas offence'). It is designed to hold businesses accountable if they do not take steps to prevent their 'associated persons', such as employees or third-party service providers, from facilitating tax evasion and there is a clear legal obligation to implement 'reasonable prevention procedures' to defend against potential prosecution.

Responding to the legislation

HMRC have published guidance on what 'reasonable prevention procedures' look like. The starting point for any hotel business is to undertake a CCO Risk Assessment to identify areas where there is potential for the facilitation of tax evasion to occur. There are common risks for all businesses, e.g. supply chain, financial controls and HR matters. However, for hospitality businesses there may be additional considerations, including policies and controls around tips and troncs, and the use of off-payroll workers or staffing intermediaries.

Following the risk assessment, it is crucial to develop a comprehensive CCO policy documentation and provide training for staff, particularly those who handle financial transactions. Like the Bribery Act, businesses have an ongoing obligation to monitor and review these procedures to ensure they remain effective.

HMRC Activity

HMRC publish bi-annual statistics on the number of live CCO investigations and opportunities under review. On 1 January 2024 there were 11 live CCO investigations spanning several different business sectors across organisations of all sizes.

In addition to this investigative activity, HMRC is also incorporating CCO-related questions into broader discussions with businesses, such as during Business Risk Reviews and Governance Audits. . This indicates that HMRC is not only vigilant in investigating potential offences but is also proactively seeking to understand how businesses are managing their CCO risks

Commercial Impact

HMRC's objective to embed a culture of prevention against tax evasion seems to be taking hold, as CCO compliance is now a factor in commercial decisions. For instance, as part of transaction due diligence, the steps a business has taken to respond to CCO can influence its attractiveness to potential buyers.

A lack of compliance could lead to less favourable terms due to the risks of prosecution, which include unlimited financial penalties, public record of conviction, and reputational damage.

Financial institutions, such as banks and insurance companies, may consider a business's CCO compliance when making lending or coverage decisions. This underscores the importance of having a formal CCO framework in place, the development of which should not be an onerous task for most businesses as it could impact your hotels lending ability later down the line.

Taking some straightforward steps to demonstrate compliance can provide assurance over the integrity of your business partners and signal strong tax governance within your organisation. Importantly for hospitality businesses, where reputation is critical to long-term success, taking a strong stance on CCO (along with Anti-Bribery and Modern Slavery) should be viewed as a means to protect this reputation and ensure that the business is seen as a trustworthy and responsible operator in the sector.

The challenges facing the hotel industry

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Hotels have continued to demonstrate their resilience in 2023, with RevPAR and ADR increasing across the market. At opposite ends of the market, budget and luxury hotels are in the strongest position, with the mid-market hotels most at risk.

In the post-Covid-19 environment, hotel revenue has remained strong due to price increases and is now back at 2019 levels, but profits have been severely impacted due to increased costs. Hotel valuations have largely remained stable compared to pre-Covid-19, but with reduced profits, will they fall and put pressure on loan covenants and business valuations?

Government contracts issued to house asylum seekers have provided a relative safety blanket to some hotels. As these contracts end, management must carefully plan their return to being open to the public. Hotels may require refurbishment and without recent customer data due to Covid-19 and government contracts, management will need to assess if they have sufficient cash reserves to re-open and generate a profit immediately or whether there will be a lag whilst they build customer numbers back up.

There are some key challenges that the entire hotel industry will continue to face:

Continued restrictions on consumes discretionary spend – Although inflation fell to 3.8% in March 2024 compared to 8.9% in March 2023, there has not yet been a material drop in prices that consumers are paying. The Bank of England base rate is not expected to drop significantly in 2024, with smaller drops towards the end of the year, meaning consumers will continue to face high mortgage rates.

Labour costs - The recent National Living Wage increase in April 2024 is a direct hit to profitability, and pressure to offer attractive salaries will remain. The ability to pass on these costs will be more challenging as consumers become less willing to accept price rises with reduced discretionary spend.

Debt service costs – As already discussed, the Bank of England base rate is not expected to fall significantly this year, meaning that the cost of servicing debt, ie interest payments, will be a major cost to businesses, particularly to those who have not reduced their debt levels post-Covid-19.

Continued focus on ESG – Regulators, lenders, investors, employees, and customers are requiring more and more sustainability credentials and higher ethical standards from the industry.

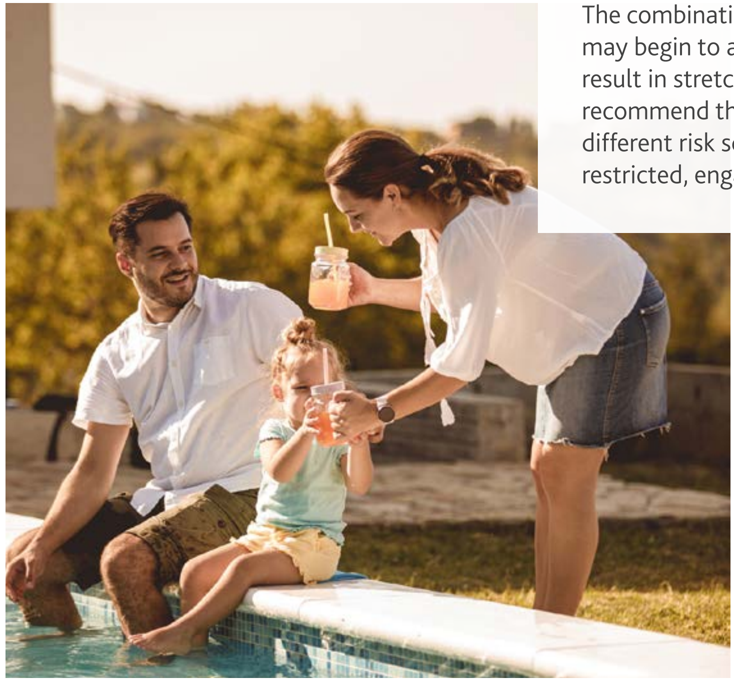
There is scope for management to negotiate these challenges and continue to grow their businesses in this reliant market. Management teams can navigate this successfully with:

Quality financial information – Having access to timely and high-quality financial information, including robust financial forecasts, will allow businesses to make swift and decisive decisions. An accurate and detailed cash-flow forecast will highlight potential pinch points, model scenarios and support management in implementing mitigating procedures.

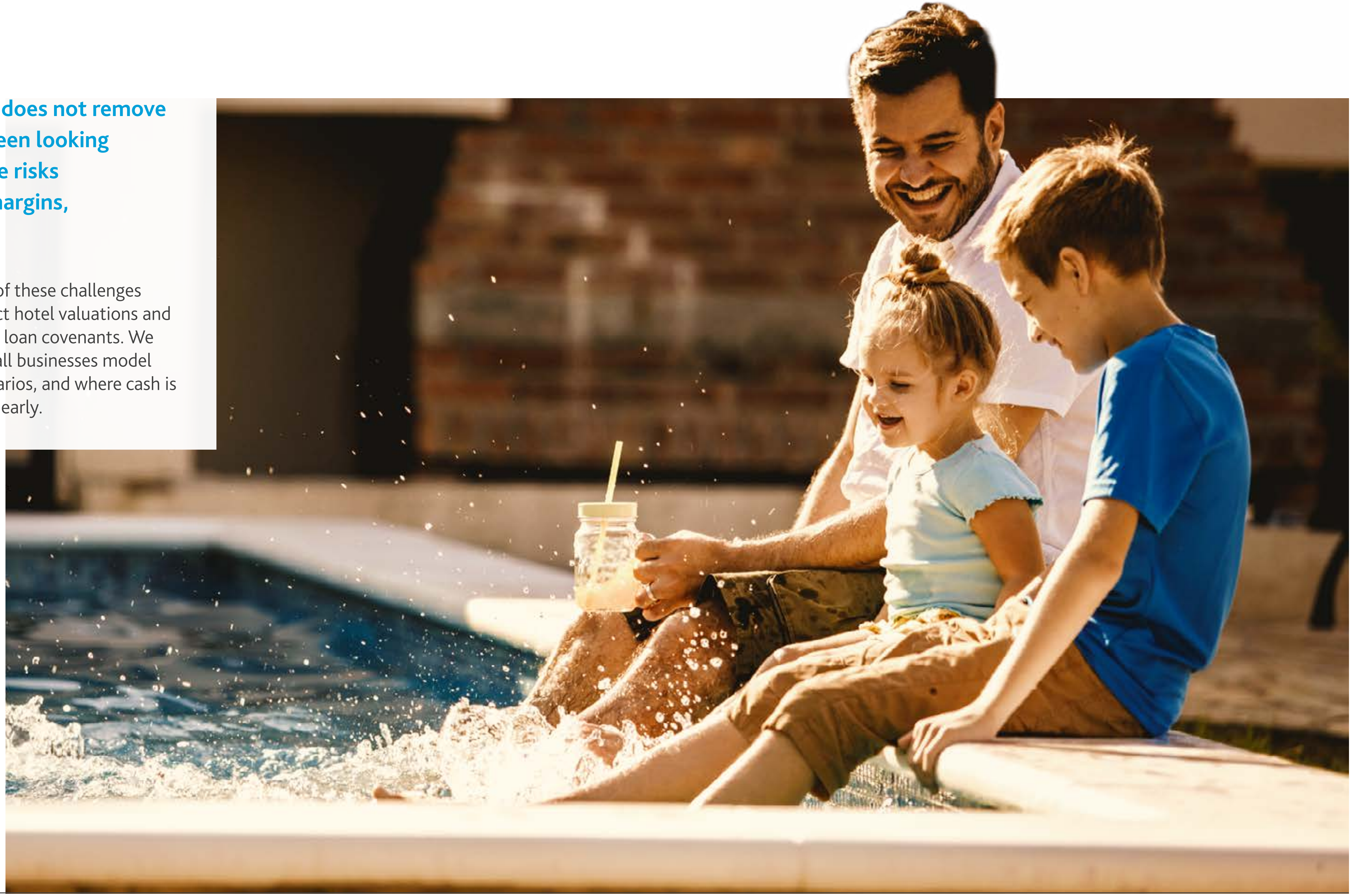
Implementation of mitigation strategies – Should they be required, management should consider and act accordingly and, if required, seek expert help. It is recommended that early engagement in every case is beneficial, whether this be with lenders, key suppliers, or experts.

Understanding your market – Specific markets are seeing a decline in corporate and event-led demand, and some are experiencing changing supply in government contracts. As we reported in 2023, mid-market hotels were most at risk. Identifying your market and offering accordingly is essential.

Overall, the UK hotel market is performing well, but this does not remove risk. After the recent wet weather, UK consumers have been looking overseas for more reliable weather - this coupled with the risks discussed above will keep pressure on hotel businesses margins, and their cash position.



The combination of these challenges may begin to affect hotel valuations and result in stretched loan covenants. We recommend that all businesses model different risk scenarios, and where cash is restricted, engage early.



BDO Sector Expertise

Leisure and Hospitality

Our team works with international businesses across the leisure industries, including hotels, restaurants and bars, travel and tourism, betting and gaming, professional sports and fitness. We provide assurance, tax, and advisory services to our clients, who range from small owner-managed businesses to large corporations in both the private and public sectors, many of whom are market leaders.

Hotel Expertise

Our hotel industry experience goes back nearly a century. Today, we are at the forefront of the field, working with the industry's market leaders. Our experienced and passionate partners and staff find and help implement actionable insights that make a difference to our clients' businesses. We take the time to understand the business and the people behind the numbers so that we can use our expertise to maximum effect.

We can keep you up to speed with the latest issues and movements of the market, both nationally and internationally, presenting our findings through our comprehensive publication, Hotel Britain. In an industry which can be volatile and heavily affected by world events, we can give our clients vital insights into what they can do to improve their relative performance and market position. In short, if you are active in the hotel industry then you should be talking to us.

Driving Growth

Driving the growth of your business is always a priority. This is a challenge in the very competitive leisure and hospitality sector. We will work with you to develop or adjust your strategy, fine tune your business model and overcome the barriers to growth. Our focus is to provide the actionable ideas and insights that will make a tangible difference to your business. Whether it is improving working capital management or improving tax efficiency, we will use our experience and expertise to deliver value to you. We always invest the time to understand you and your business so that we can help you achieve your goals.

Regulatory Advice for Leisure and Hospitality Businesses

The leisure and hospitality sector is faced with an ever-changing burden of regulation, ranging from accounting standards to the Apprenticeship Levy and National Living Wage. We can provide practical guidance and help you navigate the challenges your business is facing. We can help you whether you are thinking of tackling the transition to IFRS accounting, wondering where you currently stand on troncs, trying to establish how the national living wage may affect your business or debating whether you should be converting to a REIT.

Our Hotels Team

Taking Leisure and Hospitality International

You may be ready to expand your leisure and hospitality business overseas – but you may not be ready for the challenges of succeeding internationally. You will need to navigate local regulations and tax regimes, local labour markets and any number of other issues. We will help you from the first step by identifying the best options for expansion, and the markets that are easier to break into. We can help you to work through the options available to you whether that be a joint venture, opening a branch, franchise or an acquisition. When you do make the leap, we will ensure you have the most efficient tax structures and all the necessary local knowledge. As part of the BDO international network, we draw on the leisure and hospitality expertise of colleagues across the globe - we have a presence and local leisure and hospitality expertise in every market you might want to expand into, and we understand that each area of leisure and hospitality faces its unique challenges and opportunities.

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