



# The Franchise Valuations Reporter



## Have a Damages or Valuation Question?

Call us for a free, confidential consultation. Here are some of the questions we have been asked recently:

- What kinds of damages can I claim?
- How can the damages be proven?
- What's the difference between lost future profits and lost business value?

And we're always interested in your comments about the newsletter.

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## Our Expertise

Within the franchise, distribution and dealership context, we are experts in:

- Damages, Valuations & Expert Testimony
- Finance, Accounting and Tax
- Cyber Security and E-discovery of Electronically Stored Information

We offer a free initial consultation. If any readers have questions, you are welcome to email or phone us and we will provide our best answer as quickly as possible.

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## Lost Profits: The Theory

### *The Difference Between "Expectation" Damages and "Reliance" Damages*

Lost Profits are regularly claimed in breach of contract cases and in actionable tort cases such as intentional interference with economic interest. "Damages suffered by a party are generally recoverable under one of two legal remedies, depending on the type of claim asserted [footnote omitted]. In a claim brought under tort law, the plaintiff may seek restitution or reliance damages. A plaintiff in a breach of contract claim may seek to recover expectation damages." [1] Restatement Second §344, which has been around since 1981, offers the following rationale:

#### §344. PURPOSES OF REMEDIES

**Judicial remedies under the rules stated in this Restatement serve to protect one or more of the following interests of a promisee:**

**(a) his "expectation interest," which is his interest in having the benefit of his bargain by being put in as good a position as he would have been in had the contract been performed,**

**(b) his "reliance interest," which is his interest in being reimbursed for loss caused by reliance on the contract by being put in as good a position as he would have been in had the contract not been made,**

And the Restatement makes the distinction with its two illustrations:

#### Illustrations:

1. A contracts to build a building for B on B's land for \$100,000. B repudiates the contract before either party has done anything in reliance on it. It would have cost A \$90,000 to build the building. A has an expectation interest of \$10,000, the difference between the \$100,000 price and his savings of \$90,000 in not having to do the work. Since A has done nothing in reliance, A's reliance interest is zero. Since A has conferred no benefit on B, A's restitution interest is zero.

2. The facts being otherwise as stated in Illustration 1, B does not repudiate until A has spent \$60,000 of the \$90,000. A has been paid nothing and can salvage nothing from the \$60,000 that he has spent. A now has an expectation interest of \$70,000, the difference between the \$100,000 price and his saving of \$30,000 in not having to do the work. A also has a reliance interest of \$60,000, the amount that he has spent. If the benefit to B of the partly finished building is \$40,000, A has a restitution interest of \$40,000.

[1] Nancy Fannon and Jonathan M. Dunitz, Esq. Editors, *The Comprehensive Guide to Lost Profits and Other Commercial Damages*, Chapter 13. "Lost Profits Versus Lost Business Value." [www.bvresources.com](http://www.bvresources.com)

## We Write the Book

**Franchise Regulation and Damages**, the only treatise that covers damages in franchise disputes and valuations of franchises, is updated 3 times a year.

For more details, to see a Table of Contents or to place an order, go to the Wolters Kluwer Law & Business web page [here](#).

## DISCLAIMER

The information provided in this newsletter is for informational purposes only and should not be construed as legal or expert advice which can only be obtained from appropriate professionals. Franchise Valuations, Ltd. and Franchise Technology Risk Management provide such expert advice on the topics addressed herein.

Please visit our websites at [www.FranchiseValuations.com](http://www.FranchiseValuations.com) and [www.ftm.biz](http://www.ftm.biz)

## Damages

### *Calculation Whoops*

In a breach of distribution agreement case the Court of Appeals for the Sixth Circuit has ruled that a federal district court was in error when it granted summary judgement to a distributor and allowed it to calculate damages using a 50% profit margin when the distributor's own sales data and tax returns showed only a 25% profit margin. Although the grant of partial summary judgment was correct, the Court of Appeals vacated the damages award and remanded for recalculation. *Elite International Enterprise, Inc. v. Norwall Group, Inc.*, CA-6, Business Franchise Guide ¶15,640.

## Valuation Discounts

### *Perhaps the IRS Is Not Going To Kill Minority Discounts in Estate Planning*

There is a lot of scuttlebutt that the long-awaited proposed regulations under Internal Revenue Code Section 2704(b) to limit the ability of family-owned businesses to apply minority discounts under certain circumstances may not be as bad as some predicted, according to a BNA news item that quoted an IRS official.

## Warning To Officers of Failing Franchises

### *Liability For Sales and Withholding Tax May Extend To Officers*

Several opinions have come down recently concerning the personal liability of corporate officers and managers of LLCs. What this means for the franchise community is that a corporate structure may not fully protect an owner/operator from personal liability in all circumstances.

1) **Illinois:** An Administrative Hearing[1] held that a company's president was personally liable for the company's Illinois sales tax because the president had retained the final authority and oversight responsibility over the company's affairs and willfully failed to pay the taxes. Although the president had delegated his overall responsibilities to manage the company's affairs, including filing of returns and making sales tax payment, to an outside corporation, the president did not provide sufficient documentation to show that he ceased to be a responsible officer of the company. In addition, the president failed to investigate and correct mismanagement of the company's business after he was aware that the business was failing, and that taxes were not being paid.

2) **Illinois:** In another Illinois case, a taxpayer who was an officer of a corporation was not personally liable for the corporation's Illinois sales tax because the taxpayer had no authority over the financial affairs of the corporation for the tax periods at issue. According to statute, personal liability is imposed on a person who has control or responsibility for filing corporate tax returns and making the tax payments and who willfully fails to file returns or make tax payments. In this case, a new business license was issued to the taxpayer before the corporation's tax periods at issue, and the taxpayer left the corporation before the tax periods at issue.[2]

3) In a **New Mexico** case<sup>[3]</sup> a taxpayer who was listed as an agent and manager of a limited liability company (LLC) registered in New Mexico was not liable for withholding tax owed by the LLC, because he was not an "employer" for withholding tax purposes. The taxpayer's son-in-law opened and operated a restaurant under the LLC in New Mexico, but the application for a business tax identification number identified the taxpayer as one of the managers of the LLC. The taxpayer, however, was unaware of any business or tax registrations that were done in New Mexico, and he did not consent to the use of his information on any applications. The taxpayer did not work in the restaurant or LLC, did not have any control over or knowledge about their employees or wages, and did not participate in any aspects of their business. Under New Mexico law, the key for an individual to be held liable for withholding tax is whether the individual had control of the payment of wages. In this case, the taxpayer was not an "employer" for withholding tax purposes since he did not control the payment of wages.

4) **Washington:** Under the Washington statute, in order for a responsible person to be held personally liable for collected and unpaid sales tax: (i) The tax must be the liability of a corporate or limited liability business; (ii) The corporation must be terminated, dissolved or abandoned; (iii) The failure to pay must be willful; and (iv) The department must not have a reasonable means of collecting the tax from the corporation. In this recent case the Chief Executive Officer was held personally liable.<sup>[4]</sup>

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[1] Administrative Hearing Decision No. ST 15-07, Illinois Department of Revenue, August 6, 2015, released October 2015 CCH ¶403-016.

[2] Illinois State Tax Reporter, Administrative Hearing Decision No. ST 15-09 - CCH ¶403-015. Administrative Hearing Decision No. ST 15-09, Illinois Department of Revenue, August 17, 2015.

[3] *In the Matter of the Protest of Andrew Winston*, CCH ¶401-680. New Mexico Taxation and Revenue Department, No. 15-32, September 29, 2015

[4] Det. No. 14-0350, 34 WTD 474 (Oct. 30, 2015)

## Cybersecurity

If you stayed at a Starwood hotel between Nov. 5, 2014 and April 13, 2015, you'd better check your credit card bills.

[Starwood Reports Payment-Information Data Breach](#)

KrebsOnSecurity is reporting that the Dept. of Homeland Security "has been quietly launching stealthy cyber attacks against a range of U.S. private businesses."

[DHS Giving Firms Free Penetration Tests](#)