



The Franchise Valuations Reporter

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Welcome to our newsletter focusing on issues unique to our practice that we don't think are addressed anywhere else with respect to franchising: valuation and damages, cyber crime, expert testimony and tax nexus –the issues we know best, that matter to our clients - franchise executives and the consultants, attorneys and other professionals who advise them. We hope you find information that warns, informs and benefits you.

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Best Practices

Franchisor Claim for Royalties vs. IRS Claim for Taxes – Winner IRS on a Technicality

In a recent decision Cold Stone Creamery brought a declarative action against the IRS to determine the priority of their lien under a UCC filing vs. the IRS lien under a tax lien filing against a defaulting franchisee. The IRS won (allowing it to seize the franchisee's assets) because the franchisor's UCC lien had not been renewed even though it was originally filed first in time. (See Janet Sparks's coverage in *Franchise Times* (Nov/Dec 2009) p. 54) The moral: check UCC liens to make sure they are current and valid.

“Constructive” Wrongful Termination, Attorneys Fees and Expert Fees

A new headline issue under wrongful termination statutes is “constructive” wrongful termination. In the recent New Jersey case, *Maintainco, Inc. v. Mitsubishi Caterpillar Forklift*, (New Jersey Superior Court, Appellate Division (Filed July 30, 2009). CCH Business Franchise Guide ¶14,195) a forklift manufacturer's actions forcing out an authorized dealer, was held to have amounted to “constructive” termination in violation of the New Jersey Franchise Practices Act (NJFPA). The manufacturer argued that the NJFPA prohibited only

Damages Decisions

actual terminations and, because the dealer was never terminated, there was no violation.

However, the record established that the manufacturer's officers were well aware that the NJFPA prohibited them from terminating the dealer unless they could establish "good cause", and its assertion that the dealer breached a best efforts provision in the parties' agreement failed. The court

held that a dealer's loss of an exclusive territory, in and of itself, could qualify as a constructive termination. Therefore, the trial court's ruling and its award of compensatory damages for lost profits to the dealer in the amount of \$679,414 were affirmed.

Additionally, the trial court's substantial award of attorney fees to the dealer in the amount of \$3,533,642 was also upheld, but an award of \$477,611 in expert witness fees was reversed.

Cf. Not "Constructive" Termination

Under the Vermont motor vehicle dealer law, a manufacturer did not violate its provision by terminating a dealer without "good cause" when they discontinued production of a line of trucks, which they had the right to do under their agreement. The dealer was allowed to continue selling parts; thus the court ruled there was no "termination", wrongful or otherwise, and therefore, no "wrongful termination". (*L&B Truck Services, Inc. v. Daimler Trucks N.A. LLC*, DC Vt., CCH Business Franchise Guide ¶14,249) Accordingly, no damages were available.

U.S. Supreme Court

The issue of "constructive" wrongful termination is now before the U.S. Supreme

Court in the case of *Marcoux v. Shell Oil Products* (CCH Business Franchise Guide ¶13,703) where the First Circuit upheld a jury finding of "constructive wrongful termination" under the PMPA when the gas station franchisor assigned the leases of eight dealers to an affiliate that breached the agreements.

Vicarious Liability and Punitive Damages

A Kentucky Appeals court upheld a \$400,000 punitive damages award against a female McDonald's manager and a \$5 million punitive damages award against the franchisor, where the manager was duped into making a female employee go through a strip search. The court held that McDonald's could have foreseen and prevented the incident with proper training which was under their control. ("Appeals Court OKs \$5M in Punitives for Victim of Phone Hoax Strip Search", <http://www.abajournal.com/weekly/article/appeals-court-oks-5m-in-punitives-for-victim-of-phone-hoax-strip-search>)

Nexus Notes

The Georgia Department of Revenue has issued a new corporate and personal income tax rule regarding the addback adjustment for certain captive real estate investment trust (REIT) expenses and costs. (Reg. Sec. 560-7-3-.04, Georgia Department of Revenue, effective November 4, 2009)

The Illinois Department of Revenue has ruled that sales in Illinois once or twice a year from a mobile sales unit were not merely *de minimus*. They were sufficient to yield nexus for income tax purposes. (*General Information Letter IT 09-0039-*

GIL, Illinois Department of Revenue,
October 19, 2009)

CyberCrime

Red Flags Rule Enforcement Delayed – Again

Enforcement of the Federal Trade Commission's "Red Flags" Rule, which was supposed to begin November 1, 2009, has been postponed until June 1, 2010. This is the fourth time enforcement has been delayed. As we reported in previous editions of this newsletter ([Issue No. 8](#), [Issue No. 9](#)), the Rule requires certain entities to develop and implement written identity theft prevention programs to enable employees to spot warning signs that an identity thief is trying to use stolen information.

Organizations representing medical practices, lawyers and franchisors had appealed to the FTC for exemptions on behalf of their members. On October 30, 2009, the American Bar Association succeeded in obtaining a ruling from the U.S. District Court for the District of Columbia saying that the FTC may not apply the Red Flags rule to attorneys. Whether or not the FTC will ever enforce

the Rule against franchisors and franchisees remains anyone's guess.

MORE REASONS TO BE FRIGHTENED! **Links to Recent Articles on Cyber-Crime**

DHS: PhoneSnoop app bugs BlackBerrys

http://voices.washingtonpost.com/securityfix/2009/10/dhs_warns_of_blackberry_snoopi.html?hpid=news-col-blog

Hackers Indicted in Widespread ATM Heist

http://online.wsj.com/article/SB125786711092441245.html?mod=WSJ_hps_LEFTWhatsNews

LAW FIRMS BE PARTICULARLY ALERT!

FBI: Hackers targeting law and PR firms

http://www.msnbc.msn.com/id/33991440/ns/technology_and_science-security/

More Hackers Target Law Firms, Often 'Spear Fishing' in Spam E-Mail

http://www.abajournal.com/news/article/more_hackers_target_law_firms_often_spear-fishing_in_spam_e-mail

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