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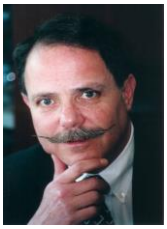
The Franchise Valuations Reporter

Our Expertise



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

- Valuations, Damages & Expert Testimony
- Finance, Accounting and Tax

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Franchise Regulation and Damages, the only treatise that covers valuations and damages in franchise disputes, 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

Valuations

Restaurant Research Assesses Impact of COVID-19 on Food Service Valuations

In a recent report, our well-respected friends Wally Butkus and Phil Mangieri of Restaurant Research LLC find declines in value of units of major chains ranging from less than 1% to more than 17% with an average decline of approximately 10%. You can access the full report by subscribing to their service here.

Subsequent Events Impact on Valuations

Valuation analysts must consider whether to factor in the impact of COVID-19 when the effective date of the valuation is prior to the outbreak. The AICPA has a rule for this. Its 2007 Standards on Valuation Services (SSVS sec 100, paragraph 43) states:

> The valuation date is the specific date at which the valuation analyst estimates the value of the subject interest and concludes on his or her estimation of value. Generally, the valuation analyst should consider only circumstances existing at the valuation date and events occurring up to the valuation date. An event that could affect the value may occur subsequent to the valuation date; such an occurrence is referred to as a ***subsequent event***. Subsequent events are indicative of conditions that were not known or knowable at the valuation date, including conditions that arose subsequent to the valuation date. The valuation would not be updated to reflect those events or conditions.
>
> Moreover, the valuation report would typically not include a discussion of those events or conditions because a valuation is performed as of a point in time - the valuation date - and the events described in this subparagraph, occurring subsequent to that date, are not relevant to the value determined as of that date. In situations in which a valuation is meaningful to the intended user beyond the valuation date, the events may be of such nature and significance as to warrant disclosure (at the option of the valuation analyst) in a separate section of the report in order to keep users informed (see paragraphs 52p, 71r, and 74). Such disclosure should clearly indicate that information regarding the events if provided for informational purposes only and does not affect the determination of value as of the specified valuation date.

Damages

Punitive Damages

In *The Orange Rabbit, Inc. v. FranChoice, Inc.*,[1] Two purchasers of an iLoveKickboxing (ILKB) business franchise were permitted to amend their complaint against franchise consultant FranChoice and one of its individual consultants to add a punitive damages claim to the extent of certain,

specifically alleged fraudulent representations, made by the defendants in order to induce the prospective franchisees to purchase their ILKB franchise, a district court in Minnesota has ruled. These allegations satisfied the requirements of Federal Rule of Civil Procedure 15 for amendment of a complaint because the representations were allegedly made by the defendants about ILKB without investigation or verification, when such representations were false and were known and should have been known to be false. However, amendment was denied as to certain allegations that did not satisfy Rule 15 because they were conclusory or otherwise did not put the defendants on notice of a claim for punitive damages. As an initial matter, the court determined that Rule 15, not Minnesota Statutes Section 549.191, governed the motion to amend. The court's order was representative of decisions announced the same day in 10 other suits brought by ILKB franchisees seeking to amend their complaints against FranChoice and one of its individual consultants.

Willfulness Showing Not Required To Recover Infringer's Profits Under Lanham Act

Resolving a circuit split, the US Supreme Court held that a mark owner should not have been denied a disgorgement remedy on the ground that the defendant acted only with "callous disregard" and did not infringe the mark willfully.[2] Thus, SCOTUS ruled that a plaintiff in a trademark infringement suit is not required to show that a defendant willfully infringed the plaintiff's trademark in order to recover an award of the defendant's profits under Section 35 of the Lanham Act. The Court vacated and remanded a decision of the U.S. Court of Appeals for the Federal Circuit, holding that magnetic fastener maker Romag Fasteners, Inc., was not entitled to an award of $6.8 million in profits derived from fashion accessories designer Fossil Group, Inc.'s use of counterfeit ROMAG-brand snaps on handbags because Fossil's infringement was not willful. Although mental state was a relevant factor in deciding whether to disgorge profits, the Court found no support in the statute or pre-Lanham Act common law for Fossil's suggested "inflexible precondition" of a willfulness showing.

Damage Award For Copying Competitor's Business Information Database Upheld On Appeal

Copyright in a factual compilation protects the selection and arrangement of facts as long as they are made independently by the compiler and involve a minimal degree of creativity. Thus, a company that compiles a database of factual business information could recover $11.2 million in damages for copyright infringement from a competitor started by the first company's founder because the selection and arrangement of these facts were copyrightable, the U.S. Court of Appeals for the Eighth Circuit ruled in affirming the jury's verdict and denying the motion for a new trial. It also upheld the $10 million judgment against the founder for breach of his separation agreement with the company.[3]

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[1]May 6, 2020, Wright, E.

[2]*Romag Fasteners, Inc.v. Fossil Group, Inc.*, April 23, 2020, Gorsuch, N.

[3]*Infogroup, Inc. v. Database LLC*, April 27, 2020, Benton, W.

Payroll Protection Program

PPP Loan Forgiveness Results in Non-Deductible Expenses

The IRS has released guidance about the deductibility of expenses for

taxpayers who receive loans under the Paycheck Protection Program (PPP). While the CARES Act (P.L. 116-136) provided for tax-exempt treatment of the amount of loans forgiven, it did not address whether deductions for expenses associated with the loan forgiveness would still be allowed. IRS Notice 2020-32 provides a reminder that the Internal Revenue Code does not allow for a deduction of the amount of expenses that are allocable to tax-exempt income. This also applies to tax-exempt income that is earmarked for a specific purpose and the deductions that are incurred in carrying out that purpose. The interrelation between the amount of tax-exempt income from forgiveness of a PPP loan and the amounts paid for eligible expenses is sufficient to disallow deduction of these expenses according to the IRS Notice. Effectively then, the Cancellation of Indebtedness will result in taxable income. The right hand giveth and the left hand taketh away.

Joint Employer, Independent Contractor, Vicarious Liability

California Sues Uber and Lyft, Claiming Workers Are Misclassified

California's attorney general and a coalition of city attorneys in the state sued Uber and Lyft on May 5, claiming the companies wrongfully classified their drivers as independent contractors in violation of a state law that makes them employees. The law, known as Assembly Bill 5 (AB 5), requires companies to treat their workers as employees instead of contractors if they control how workers perform tasks or if the work is a routine part of a company's business.

Attorneys' Fees

Attorney Fees Greater Than Award

As we reported recently, in *Fh Krear Co v. Nineteen Named Trustees*[1], the Court wrote (at Para.70) "Although the district judge found that the services of its attorneys 'secured a substantial benefit for Krear,' it does not appear that she gave appropriate consideration to what is apparently the general rule in New York, i.e., that it is rarely proper to award fees in an amount that exceeds the amount involved in the litigation." But that was then. In the more recent case of *AFC Franchising, LLC v. Fairfax Family Practice, Inc.*[2], an urgent care center franchisor prevailed in a fee award against a former franchisee and was awarded attorney's fees greater than the damages award. The Court found, the award was appropriate given the franchisor's success in obtaining injunctive relief.

Attorney Fees Denied To Defendant Following Favorable PTAB Unpatentability Ruling

An award of attorney fees to a prevailing party in a patent case is within court discretion but will not be considered unless the case is "exceptional." Thus, on remand, a federal district court in Texas declined to award attorney fees to the prevailing party, defendant Alcatel-Lucent Enterprises ("ALE"). Although the district court vacated an earlier judgment in favor of plaintiff Chrimar Systems following the PTAB's ruling that the patent claims were unpatentable, the court held that Chrimar's conduct in pursuing its claim did not make the case "exceptional" under 35 U.S.C. § 285. Accordingly, ALE's motion for an award of attorney fees against Chrimar was denied.[3]

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[1] 810 F. 2d 1250

[2] May 8, 2020, Brinkema, L.

[3] *Chrimar Systems, Inc. v. Alcatel-Lucent Enterprise USA Inc.*, April 21, 2020, Love, J.

Quotations from Joseph Stalin

"A single death is a tragedy; a million deaths is a statistic."

"There is no God"

"I trust no one, not even myself."

"*Those who vote decide nothing*. Those who count the vote *decide* everything."