The Franchise Valuations Reporter

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Our Expertise

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

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

Have a Question About Succession Planning for Franchise Owners?

Call us for a free, confidential consultation. And we're always interested in your comments about the newsletter.

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We Write the Book

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

Joint Employer

IFA and Department of Labor Suffer Crushing Defeat as Judge Overturns DOL's Most Recent Joint Employer Rules as Arbitrary and Capricious

A Federal District Court has ruled that in enacting the Fair Labor Standards Act (FLSA), Congress adopted broad definitions of the terms "employ," "employee," and "employer". In a case where the International Franchise Association was granted Intervenor status, the Court found that the Department of Labor's interpretation for vertical joint employer liability conflicted with the FLSA and was arbitrary and capricious. The district court in New York City granted summary judgment in favor of a group of states that asked to overturn the DOL's Final Rule on joint employer status. The Court found that the Final Rule conflicts with FLSA because it ignores the statute's broad definitions. While the department reasoned that section "3(d) alone determines" if an employee has a joint employer, the court found that the FLSA's definition of "employer" cannot be read untethered from its related definitions of employee" and "employ" and that the DOL failed to adequately justify its departure from its prior interpretations. (*State of New York v. Scalia*, September 8, 2020, Woods, G.). The Judge wrote scathingly:

"The Department also cited zero cases holding that section 3(d) is the sole textual basis for joint employer liability. Even the Department did not argue that *Rutherford*, *Falk*, or *Bonnette* explicitly adopted the "textual delineation" it now claims to discern "clear[ly]" in the FLSA's text. 85 Fed. Reg. at 2825 (citation omitted). It has been *eight decades* since Congress passed the FLSA and the Department recognized joint employer liability. And the best the Department can do is to draw a negative inference from *Falk* and *Bonnette*. Because those courts did *not* cite sections 3(e)(1) and 3(g), the Department argued that

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

section 3(d) is separable from the FLSA's other statutory definitions.
"That is thin gruel. If the Department's interpretation were "clear" (or even permissible), some court would have probably adopted its rationale. But the Department has found not a one. Over eighty years later, this dog has yet to bark. *Cf.* A. Doyle, *Silver Blaze*, in *The Complete Sherlock Holmes* 335 (1927)."

Checkers Must Face Pregnancy Discrimination, Wage Claims of Franchisee Worker
Granting in part and denying in part Checkers' motion to dismiss, a federal district court in New York found that an employee of a Checkers franchisee pled sufficient facts to show that Checkers was her employer for purposes of her pregnancy discrimination and New York Labor Law claims. The record established that Checkers exercised sufficient control over the franchisees' management and operations and that the employee's work as a crew member was integral to Checkers' business operations (*Griffith v. Coney Food Corp. dba Checkers*, August 17, 2020, Garaufis, N.).

Expert Testimony

Attempted Supplementation of Upcoming Expert Testimony Not Allowed

The Trademark Trial and Appeal Board granted a motion by petitioner Empresa Cubana Del Tabaco to strike the supplemental expert report submitted by respondent General Cigar Co. The respondent's supplemental report, seeking to support the expert's original opinions with new examples and illustrations, were impermissible "bolstering," which amounted to an untimely disclosure of an expert opinion under Federal Rule 26(e). In narrow circumstances such an untimely supplementation could be allowed if it were deemed substantially justified or harmless under the five-part test of the *Great Seats* decision. Here, none of the five-part criteria of *Great Seats* were met and the respondent's supplemental expert report was stricken (*Empresa Cubana Del Tabaco v. General Cigar Co., Inc.*, August 26, 2020).

Valuations

Extensive Check List For Buying a Business

Edward Mendlowitz, CPA, PFS, ABV, CFF has put together a truly extensive list of considerations which practioners should consider when representing a potential buyer. It is well worth reviewing here.

Home Health and Hospice Enterprises
Quickread, a publication of the National Association of Valuators and Analysts, has published a very thorough first installment of the criteria and analysis for valuing home health and hospice enterprises – although it was put together before the pandemic. You can view the report here.

Delaware Court Adopts DCF Model as Fair Value
In *Kruse v. Synapse Wireless, Inc.,* 2020 Del. Ch. LEXIS 238 (July 14, 2020), a statutory appraisal action disputing the 2016 buyout of minority shareholders, the Delaware Court of Chancery recently found there was no meaningful market-based evidence of fair value and neither expert opinion, based on standard valuation methods, was "wholly reliable." Forced to decide, the court adopted one expert's discounted cash flow analysis.

IRS Deals With Triple Whammy As It Reviews Valuations
The government shutdown, budget cutbacks—and now the pandemic—have impacted the IRS and how it selects and reviews tax returns that include valuations. Unlike the 2008 economic downturn, the IRS now has much less staff doing valuation work—about half of what it had back then. Therefore, staffing is a concern that may impact the quality of the review process. According to Michael Gregory (Michael Gregory Consulting LLC) a former IRS official, as the IRS did back in 2008, it will give more attention to certain elements of valuations. "They focused on the low-hanging fruit because that was the easiest to do," he says. The first and foremost red flag is a discount for lack of marketability (DLOM), especially if DLOMs are being increased without adequate explanation. Second on the IRS radar screen has been S corporations because this is related to the issue of tax affecting, although it is not as prominent anymore due to tax law changes and recent court cases, Gregory notes. The third red flag is reasonable compensation. These three areas will continue to be targeted as the most likely areas of noncompliance the IRS will scrutinize while it has less resources to work with.

Damages

Max Rack Loses Bid To Alter Ruling Vacating Jury's $1M Compensatory Damages Award

Max Rack, Inc. failed to persuade the federal district court in Columbus, Ohio, to retract or alter its decision to reduce a jury's damages award from $1.25 million to $500,000 stemming from a former licensee's failure to remove references to a fitness equipment company's trademark MAX RACK on the former licensee's website. Max Rack failed to present any newly discovered evidence or intervening change in law required for reconsideration. The Supreme Court's recent decision in *Romag Fasteners* (which we discussed in a prior newsletter) clarifying that willfulness is not required to receive an award of an infringer's profits—did not abrogate Sixth Circuit precedent requiring proof of actual confusion to receive compensatory damages in trademark infringement cases (*Max Rack, Inc. v. Core Health & Fitness, LLC*, August 24, 2020, Marbley, A.).

Punitive Damages Judgment of $420M Vacated
The Seventh Circuit affirmed a judgment of $140 million in compensatory damages for stolen medical records and misappropriation of trade secrets owned by Epic Systems Corporation, but vacated a punitive damages award of $280 million that they held exceeds the outermost limit of constitutional due process. The Seventh Circuit agreed with the district court, that the conduct of India-based medical records provider Tata accessing the web portal of Epic without authorization and misappropriating confidential information warrants punishment, but the conduct was not reprehensible to an extreme degree. The appellate court remanded the case to the district court to reduce the punitive damages and not exceed a 1:1 ratio of the $140 million compensatory award (*Epic Systems Corp. v. Tata Consultancy Services Ltd.*, August 20, 2020, Kanne, M.).

Attorneys' Fees

Former Employee's Willful Misconduct Leads To $2.2M Attorney Fee Award

Medical device manufacturers Stryker Corp. and Howmedica Osteonics Corp. can recover over $2.2 million in attorney fees against a former employee for willful and malicious misappropriation of trade secrets. The Fifth Circuit held that the judge alone may decide whether to award attorney fees for willful misappropriation of trade secrets and also held that the bankruptcy court did not

abuse its discretion in sanctioning the former employee for raising objections to attorney fees under the Common Core doctrine where prevailing on a trade secrets claim entitles a party to attorney fees related to all of its other claims (*Ridgeway v. Stryker Corp.*, No. 19-30791 September 2, 2020, Oldham, A.).

Quotations

"The Post Office has been stolen and the mailbox is locked." – *Bob Dylan (Stuck Inside of Mobile with the Memphis Blues Again)*

"The riot squad is restless, they need some place to go, as lady and I look out tonight from Desolation Row." – *Bob Dylan (Desolation Row)*

"Each of us is more than the worst thing we've ever done." – *Defense Attorney Bryan Stevenson who created the National Memorial for Peace and Justice in Montgomery, Ala.*

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