



# The Franchise Valuations Reporter



## Recommended Reading

I recommend CCH's new daily electronic newsletter on intellectual property - ***IP Law Daily***.

This new service from Wolters Kluwer Law & Business provides the latest case law, statutory, and rulemaking developments in intellectual property law. This is very useful reading for franchise executives and attorneys representing franchisors, dealers or distributors.

It includes news stories on the most recent developments in copyright, trademark, patent, and technology/Internet law, along with links to the full text of cases, statutes, and regulatory materials.

For more information, check out the [IP Law Daily site](#).

## 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.



## Valuations

### ***In Oppressed Shareholder Case Delaware Court's "Fair Value" Appraisal Finding is \$6 Million Lower than the Merger Price***

Just Care, Inc. - a South Carolina-based prison healthcare services company - was acquired for \$40 million in cash. Shortly thereafter, a group of shareholders filed a petition for appraisal with the Delaware Court of Chancery, claiming that the \$40 million price was too low. The petitioners included the company's CEO and CFO who contended that the company was worth \$55.2 million; the company responded that its fair value was only \$33.6 million. After a trial, Vice Chancellor Parsons found the company's value to be only \$34.2 million (*Gearreald v. Just Care, Inc.*, C. A. No. 5233-VCP (Del. Ch. Apr. 30, 2012) ) because the court did not adopt either expert's growth or discount rate assumptions.

### ***Valuation Expert Need Not Know the Law Before Taking a Case***

In one recent case, after purchasing a company for \$45 million the acquirer failed to register the stock with the SEC. A class of shareholders filed suit, claiming \$14.5 million in damages, as calculated by their expert which was followed by a defendant's filing of a motion to dismiss, arguing that the expert failed to apply the controlling law on damages. After losing that motion, it filed a *Daubert* motion claiming the expert should be excluded because he hadn't even heard of the controlling case before taking on this engagement. According to the defendant this proved that he could not be considered an "expert on damages."

But to no avail as apparently the expert learned of the controlling case law and the federal district court confirmed that the proper measure of damages for a breach of promise to register stock is controlled by *Duncan v. TheraTX Inc.*, 775 A.2d 1019 (Del. 2001). Thus, the court ruled that not only did the plaintiff's expert correctly apply the law, but "this court does not expect scientific, technical, or financial experts to know of particular cases that recite methods by which damages can be calculated, since the law is not their area of expertise." Rather, the court emphasized in dismissing the *Daubert* motion, "It is the quantification of inputs into the *Duncan* formula that fall into [the expert's] expertise."

### ***Business Valuation Credentials: What Do They Mean?***

Many experts providing damages and valuation reports have entire alphabets of credentials after their names. But do they mean anything? First of all, it's worth noting that the IBA (Institute of Business Appraisers) and NACVA (National Association of Certified Valuators and Analysts) have become one organization after a four-year partnership so there may be fewer letters in the future.

Furthermore, a well-recognized authority in the discipline, Mel Abraham, told the 2012 NACVA Consultants' Conference "Your qualifications are critical," but since all appraisers must have credentials to practice, he said, "your particular qualifications don't matter to the marketplace or your position within it. . . It's the experience you have and the results you get that matter."

Furthermore, in a recent Dunkin' Donuts case from Canada, the judge made a point of highlighting the litany of letters that follow experts' names on damages and valuation reports, noting for example the credentials of certain

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## Franchise Technology Risk Management



Our franchise law and computer forensics experts provide consulting and implementation of all aspects of cyber security, ESI management and e-discovery for franchise systems - from preparation of cyber security and ESI-related policies and procedures manuals through collection, preservation, processing, production and presentation.

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[www.ftm.biz](http://www.ftm.biz)

of the experts as follows [the underlining and the footnotes are quoted directly from the court's opinion]:

- Mr. Douglas Fisher, BAS, MSc, FCMC, CFE, FCSI[1] an expert for ADRCIC, the Dunkin' master franchisee;
- Mr. Francois Filion, CA, CA-EJC, EEE[2] who prepared a report provided for the franchisees;
- and Mr. Steve Harrar, CFE, CBV, CMA, CA,[3] another of Dunkin's experts.

[1] Bachelor of Aministrative Studies, Master of Science, Fellow Certified Management Consultant, Certified Foodservice Executive, Foodservice Consultants Society International

[2] Comptable Agréé, Comptable Agréé - Excellence in JurComptabilité de L'Institut canadien des Comptables Agréés du Quebec, Institut canadien des Experts en Evaluation d'Entreprises

[3] Certified Fraud Examiner, Chartered Business Valuator, Certified Management Accountant, Chartered Accountant

Could it be that the court was engaged more in ridicule of the after-name appellations than in a showing of respect? The court seemed to show the greatest deference to the opinion of one of the franchisees' experts, described simply as "Mr. Francois Desrosiers, MBA."

## Valuations: Impairment

### *Update of Duff & Phelps Goodwill Impairment Study Out*

As we have noted previously in our newsletters (see [January 2009](#) and [February 2009](#) and [August 2009](#)) goodwill impairment is an issue that is confronting many entities that made franchise acquisitions in the past decade and the amount of asset reductions because of goodwill impairment continues to climb. The 2011 study by Duff & Phelps and the Financial Executives Research Foundation (FERF) found that the total amount of goodwill impaired in calendar year 2010 increased from \$26B in 2009 to \$30B. This is an issue that the franchise community may be ignoring.

### ***GM May Take Impairment Write Down of Peugeot Stake if Europe Worsens***

In an example of a possible impairment situation, General Motors Co said it may have to write down the value of its 7 percent stake in French automaker Peugeot SA owing to the deepening fiscal crisis in Europe that has hurt vehicle sales in the region and stock prices. GM paid 320 million Euros, or \$423 million, for its stake, according to a March regulatory filing. Based on Peugeot's current market value, a 7 percent share of the company is worth 146 million Euros (\$180.16 million).

## Cyber-Security

### ***Small Businesses Increasingly Targeted***

According to data from security technology firm Symantec Corp., in the first half of 2012, the total number of targeted cyber-attacks on organizations rose to an average of 151 a day during May and June. The proportion of those attacks that were explicitly focused on small business rose to more than 30%, compared with 18% at the end of December 2011, Symantec reported, defining small businesses as those with 250 employees or fewer.

### ***E-Mail Scammers Target Law Firms***

According to [The Wall Street Journal](#), law firms present juicy targets for e-mail scammers who exploit lawyers' eagerness to take on new clients through the Internet. The thieves come up with often elaborate stories usually claiming monies owed from errant spouses or deadbeat clients. When

the lawyers succeed in getting satisfaction of the supposed obligation, they deposit what appear to be legitimate checks. Then the con men ask the lawyers to wire the funds to bank accounts overseas, after taking a cut as fees for their services. The problem is the checks that the lawyers deposit bounce and the firm is left out in the cold to the extent that they wired the net proceeds to the crooks.

### ***Courts Extend Legal Protection to Small Firms Whose Accounts Were Hacked***

[The Wall Street Journal also reported](#) that small-business owners whose bank accounts have been plundered by cyber-thieves until recently had no one to blame but themselves because the laws generally have treated individuals and companies differently, reasoning that companies should be more sophisticated than individuals and have their own online security measures in place.

But two recent court rulings are giving those business owners new hope that banks may be held liable for funds stolen by hackers who increasingly have focused on attacking small businesses. In one case, the Boston-based First Circuit Court of Appeals ruled that Ocean Bank in Maine lacked reasonable safeguards against hackers who siphoned nearly \$600,000 from an account held by Patco Construction Company Inc., a Maine contractor and builder. It is believed that hackers gained access to Patco's accounts through a program that recorded employees' keystrokes, allowing the thieves to answer security questions posed by Ocean's system.

In another case, a federal district judge in Detroit last year ruled that a bank owned by Dallas-based Comerica was on the hook for \$561,399 in funds stolen from accounts held by Experi-Metal Inc., a custom metals shop in Sterling Heights, Mich. Experi-Metal was the victim of a phishing scheme that lured an employee into providing account access information, according to court documents. Richard B. Tomlinson, a lawyer who represented Experi-Metal, said he believes the courts are simply recognizing that small businesses need some of the protections extended to individual customers. "In the past, they often would just tell the customer, 'too bad,'" he said. But that may not be the case any longer.

## **Tax Nexus**

### ***IFA Pushes BATSA But Are Supporters' Claims True?***

The International Franchise Association is lobbying for passage of a federal law, the Business Activity Tax Simplification Act, to prevent the income taxation of any businesses that do not have a "physical presence" in the jurisdiction seeking to collect the tax. To the IFA, the idea of "economic tax nexus" - upheld repeatedly for twenty years and most recently in the Iowa decision concerning KFC - is a heinous burden and should be unconstitutional.

Supporters of the bill are vociferous: in a recent letter provided to the IFA by Virginia Congressmen Bob Goodlatte and Robert C. "Bobby" Scott, the Congressmen wrote:

A company in our state had their delivery trucks confiscated and held by another state's tax enforcement agency until the company paid that jurisdiction's income taxes all because the company had to travel through that particular state to deliver goods to another state.

On the face of it, this assertion seems dubious. We wrote to the offices of both Congressmen for substantiation of the claim and, to date, have received no response. Obviously, driving through a state - with no other connections - should not yield tax nexus and we know of no case with such a holding. Is it true?

**Alabama ~ Sales and Use Tax: Department Adopts Nexus Rule**

The Alabama Department of Revenue has adopted a new rule which requires certain out-of-state sellers to register with the department for a sales tax license and collect and remit sales tax on all sales of tangible personal property made within the state. The rule also provides that a seller may have substantial nexus with the state due to the business activities conducted in the state by the seller's affiliates as set forth in Ala. Code §40-23-190. A seller has substantial nexus with the state for the collection of use tax if *inter alia*:

- the seller and the in-state business use an identical or substantially similar name, trade name, trademark, or goodwill, to develop, promote, or maintain sales, or the in-state business and the seller pay for each other's services in whole or in part contingent upon the volume or value of sales, or the in-state business and the seller share a common business plan or substantially coordinate their business plans, or the in-state business provides services to, or that inure to the benefit of, the business related to developing, promoting, or maintaining the in-state market.

Rule 810-6-2-.90.01, Alabama Department of Revenue, effective August 24, 2012

**New Jersey ~ Sales and Use Tax: City's Tax on Car Rentals Upheld**

The New Jersey Superior Court, Appellate Division, held that an ordinance enacted by the city of Newark levying a rental tax on all car rental transactions within specified industrial zones of the city, including Newark Airport, was not a discriminatory tax or otherwise in violation of the federal Anti-Head Tax Act (AHTA) or the dormant Commerce Clause and was a valid exercise of municipal authority.

Avis Budget Group, Inc. v. City of Newark, New Jersey Superior Court, Appellate Division, No. A-3801-10T4, August 1, 2012, ¶401-663