



The Franchise Valuations Reporter



Our Expertise

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

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

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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 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](#).



Accounting Rule Change for Recognition of Franchise Fees

Two Sets of Books and a Tedious History

Special thanks to **David Oppenheim** of Greenberg Traurig for alerting me to an upcoming change in how franchisors account for the receipt of up-front franchise fees mandated by the Financial Accounting Standards Board (FASB). Franchisors' financial accounting for such up-front fees (as opposed to royalty payments) is in for a new and different method. But it continues the situation in which financial accounting is inconsistent with tax accounting. The history of the issue and its two sets of books requirement is [discussed in my BNA/Bloomberg Tax Management Portfolio](#).^[1]

In the old days, franchisors considered up-front franchise fees as revenue when they were received (which is basically how they are required to treat such payments for tax purposes - hence the need for two sets of books). Then FASB No. 45 said franchisors could not generally treat franchise fees as revenues until the franchised unit opened. This caused a success problem for new franchisors, to wit: they collect the franchise fee which results in an increase in their cash (for balance sheet purposes) but also requires them to record a liability for the deferred franchise fee which results in a wash for balance sheet purposes. But then they have to pay the tax on the franchise fee (and possibly a fee to a broker) which reduces their cash (asset).

The ultimate result is that each franchise sale and receipt of an up-front franchise fee results in a **reduction** in the franchisor's net worth for accounting purposes which can cause state regulators to demand an escrowing of fees resulting in a further reduction of the franchisor's cash (asset). This bizarre anomaly makes the entire System show a reduced net worth even though the truth is that they are quite successful and increasing their net worth. But as if that isn't bad enough, now they've changed the rules for financial accounting again in [ASC 606, Revenue From Contracts With Customers](#), which was issued jointly by the FASB and IASB on May 28, 2014. It changes the rules and says that the franchisor can't even book the franchise fee in full when the Unit opens but now has to take it into income ratably over the term of the franchise agreement.

The new rule was originally effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2016, for public entities but on August 12, 2015, the FASB issued an amendment which deferred for one year the effective date of the new revenue standard for public and nonpublic entities reporting under U.S. GAAP. Therefore, for **public business entities**, certain not-for-profit entities, and certain employee benefit plans, the effective date for ASC 606 is annual reporting periods (including interim reporting periods within those periods) **beginning after December 15, 2017**. The effective date for all other entities is annual reporting periods beginning after December 15, 2018, and interim reporting periods within annual reporting periods beginning after December 15, 2019.

[1] [Schaeffer, Bruce S., 559-3d Finance Accounting and Tax Aspects of](#)

DISCLAIMER

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Please visit our websites at www.FranchiseValuations.com and www.ftm.biz

[Franchising. pp. A8-A9.](#)

SBA Loans to Franchisees

An Excellent Review of Policies Past and Present

Samuel G. Wieczorek of the Cheng Cohen firm has written a comprehensive and very useful review of SBA lending to what is referred to as the "franchise industry." In his article, which is [available here](#), he explains the concept of "affiliation" as it has been applied by the SBA to decline lending to franchisees where the SBA considers that the franchisor has too much control over the franchisee. For those of us who have not kept up on the technicalities of SBA lending, he offers an explanation of the November 2016 modifications to the program (including the Franchise Registry formerly overseen by FranData), the SBA's newly required addenda and then the February 14, 2017 changes to the prior changes. It is a convoluted set of rules and Mr. Wieczorek explains them admirably. It is recommended reading.

Joint Employer Update

Franchisors Not "Employer" of Church's Chicken Employee Who Alleged FLSA Violations

An employee's assertion that two franchisors had a management role in a franchisee's restaurant operations did not render those entities her "employer" under the Fair Labor Standards Act, according to a federal district court in Birmingham, Alabama. [1] Although a franchise agreement required the franchisee to send its employees to attend a "manager training" program conducted by the franchisors, the training program alone did not turn the franchisors into the employee's employer. The employee did not allege any facts showing that the franchisors had the power to hire or fire, or make personnel decisions, supervise work schedules, determine pay rate, or maintain records of the franchisee's employees.

[1] *Rodriguez v. America's Favorite Chicken dba Church's Chicken* (USDC AL) (May 3, 2017, NO: 2:15-cv-1775-KOB)

Succession Planning for Franchisees

Many Owners Are Not Ready to Retire

Ten thousand people per day are turning 65. Many of them own franchises and it has been common wisdom that there will be an onslaught of baby boomers selling their businesses. But it may be a little later in coming than many people thought. A recent study by the Wells Fargo/Gallup Small Business Index finds that, if money were no object, over one-half (53%) of the nation's small-business owners would continue working in a full- or a part-time capacity. Only about one in four say they would retire completely.

Expert Testimony

Missouri Adopts Daubert

Last month Florida rejected a proposal to adopt the *Daubert* rule for admission of expert testimony. But more recently Missouri adopted the *Daubert* standard giving the Court a "gatekeeper" function, as applicable to expert witnesses. Previously, the admissibility of expert witness testimony in Missouri was guided by statute.[1] Before the adoption of the new law, Missouri was one of several states that followed neither the *Frye* standard nor the *Daubert* standard.

[1]The Missouri Code of State Regulations §490.065.3 required that the facts or data upon which an expert based an opinion "must be of a type reasonably relied upon by experts in the field in forming opinions or inferences upon the subject and must be otherwise reasonably reliable."

Wisdom from Warriors

Quotes from World War II Leaders

George C. Marshall: "No one ever had an original idea after 3 o'clock in the afternoon."

Dwight David Eisenhower: "I'm not one who finds it difficult to hate my enemies."