The Franchise Valuations Reporter

June 2022 | Vol. 14 - Issue 6

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.

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

Valuations & Discounts

Discounts for Minority Interest (DMIN) and Lack of Marketability (DLOM) Upheld

In *Smaldino v. Comm'r*[1], the Tax Court, in valuing a 49% Class B interest in an LLC, noted that one expert applied a 38.43% combined discount for lack of control and lack of marketability while the other applied a similar combined discount rate of 36%. So, the Court held: "petitioner having advanced no other meaningful argument for [one expert's] slightly higher combined discount rate, we will apply [the other expert's] 36% combined discount rate." There was absolutely no dispute over whether or not the discounts were appropriate.

More Business Owners Deciding To Sell, Most Retiring

The long anticipated "Silver Tsunami" wave of retiring baby boomers appears to be arriving and is expected to supply the market with a steady stream of available businesses throughout the year, according to a report from BizBuySell. An increasing number of small business owners, many aging and no longer willing to wait on the sidelines, believe now is the time to exit. Of surveyed owners, over 63% say they are over 50 years old and 30% say they are over age 60. More than a third (37%) say they plan to sell within two years. Of owners recently surveyed, the majority (55%) cite retirement as their motivation for selling, while a substantial 31% say their business is doing well and feel they can currently receive a good price.[2] Active for-sale inventory has climbed 10% over the past year, the report says.

No Deduction For Built-In Taxes in Shareholder Buyout

As reported by BV Wire, in *Sproule v. Johnson*, 2022 ND 51; 2022 N.D. LEXIS 56; 971 N.W.2d 854; 2022 WL 803346, a North Dakota partnership dissolution case, the defendants argued on appeal that the district court erred

in its valuation. They asserted that the district court was required to consider potential capital gains taxes on liquidation in calculating the plaintiffs' buyout. The district court found that the agreement in principle called for a valuation without a discount. The accounting firm for the defendants provided an analysis of what would happen if the assets of the partnership were liquidated. However, the district court found this to be speculative because the plaintiffs indicated there was no intention currently to liquidate. The state Supreme Court affirmed the district court's decision.

"Tax Affecting" In Flux Again

In the case *In Re Cellular Tel. P'ship Litig.*; 2022 Del. Ch. LEXIS 56 (*Cellular)*, the court found there should be no tax affecting. As noted last month, the case is long and will be discussed in detail in a coming issue of this newsletter.

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[1] T.C. Memo 2021-127,| 2021 Tax Ct. Memo LEXIS 168, 122 T.C.M. (CCH) 298, 2021 WL 5232444
[2] This may no longer be current.

Punitive Damages

Requirements in New York Breach of Contract Claim Defined

In *Schlusselberg v New York Cent. Mut. Fire Ins. Co*., 2022 NY Slip Op 03539, Appellate Division, Second Department, the appeals court held that "the elements required to state a claim for punitive damages in New York when the claim arises from a breach of contract are: (1) the defendant's conduct must be actionable as an independent tort; (2) the tortious conduct must be of the egregious nature set forth in *Walker v Sheldon*; (3) the egregious conduct must be directed to the plaintiff; and (4) it must be part of a pattern directed at the public generally. Where a lawsuit has its genesis in the contractual relationship between the parties, the threshold task for a court considering a defendant's motion to dismiss a demand for punitive damages is to identify a tort independent of the contract (*see New York Univ. v Continental Ins. Co.*, 87 NY2d at 316; *Rocanova v Equitable Life Assur. Socy. of U.S.*, 83 NY2d at 613).

Expert Testimony

Daubert Challenge Leading To Exclusion "Not a Death Sentence"

In an article subtitled "End of Life or Another Day at the Office?", Allyn Needham, a partner at a Fort Worth-based expert services and economic research firm, claims being excluded is not a death sentence to being an expert – which he continues to be. He writes,

In my career, my testimony has been excluded three times. Never have I been excluded for not being qualified. . . In all three matters, the court found my analysis either did not have legal foundation or was not the analysis acceptable to the court. One assignment the court ruled a contract was not a contract. . . Because there was no breach of contract, there was no need for a lost profits analysis. Even though the fraud claim continued, my analysis could not be used because it was based on a false premise. The next challenge related to an assignment where I needed to develop one model for a class action suit and my model was too individualistic. The final matter involved my providing a valuation letter as opposed to a certified appraisal on a minority ownership. The judge would not accept testimony regarding a valuation letter as opposed to a certified valuation.

Experts In, Lay Witnesses Out In Damages Case

In *Auto Konnect, LLC. v BMW of North America*, LLC, 2022 U.S. Dist. LEXIS 42345, a Michigan case, there were a number of motions to exclude expert witnesses in a damages case that involved employee poaching in the automotive industry. The motions were granted with respect to lay witnesses but denied (or partially granted) with respect to damages experts, as follows:

- The defendants' motion to exclude the plaintiff's industry expert was denied (the expert had over 40 years of experience in the industry and would testify as to industry customs and practices);
- The plaintiff's motion (in limine) to preclude the defendant from presenting expert testimony from lay witnesses was granted (they were employees of the defendant);
- The defendants' motion to exclude testimony of the plaintiff's owner as an expert was granted (he can testify as to his own personal experiences but not as to industry customs and practices);
- The defendants' motion to exclude the plaintiff's damages expert was denied (he was not a CPA nor did he have business valuation credentials, but he was a JD/MBA who had testified in a number of damages cases); and
- The plaintiff's *Daubert* motion to exclude specific expert testimony from the defendant's expert was granted in part (he had valuation certifications and would be a rebuttal expert to the plaintiff's damages expert).

Husband Shuns Valuation Expert, Loses Case

In *Snyder v. Snyder*, 2022 Pa. Super. LEXIS 175; 2022 PA Super 72, a Pennsylvania divorce case reported by BV Wire involving a restaurant, neither the husband nor the wife submitted formal business appraisals. But the wife had an accounting degree and had worked as an auditor, so she herself did a valuation using the "gross sales method," and she prevailed in the trial court. On appeal, the husband argued that she was not competent to testify as to the valuation and that the method she used was not appropriate. But the appellate court disagreed, finding she was competent and that prior experts had used the gross sales method, so it was appropriate.

Joint Employer/Independent Contractor

Uber and Lyft Hit a Red Light in Massachusetts

As reported by Andrew Ross Sorkin in his DealBook newsletter, Gig companies like Uber and Lyft suffered a a major and expensive setback when a court in Massachusetts this week rejected a proposed ballot measure that would have classified drivers as independent contractors rather than employees. The unanimous ruling by a seven-judge panel halted the

companies' $17.8 million campaign to put the issue to voters. The measure would have given drivers some limited benefits but absolved the companies of the need to pay for full health care coverage, time off or other benefits that employees enjoy. The fight in Massachusetts came after a similar initiative in California in 2020 in which gig companies spent more than $200 million on a state ballot proposition. In that case, voters passed the measure, but a judge later found it unconstitutional. Still, the decision in Massachusetts is another sign that gig companies' business models may not remain viable. The ballot initiative might have succeeded had it not overreached. It contained a provision buried in obscure language that seemed to try to shield businesses from liability for accidents or crimes involving their drivers. This section was unrelated to the rest of the proposal, the court said, violating a state requirement that all sections of a ballot measure be related.

And Another Gig-Economy Problem in New York

An entity similar to Uber and Lyft by the name of Groundanywhere LLC operates a digital platform on a smartphone app that provides transportation services to clients seeking rides in New York City. *Matter of Hossain (Groundanywhere LLC--Commissioner of Labor)*, 2022 NY Slip Op 03424, Appellate Division, Third Department is a case where the Claimant worked as a driver for Groundanywhere from July 2016 through July 2017, when he applied for unemployment insurance benefits after he ceased driving for that platform. The Department of Labor issued an initial determination that claimant was an employee of Groundanywhere and, after a hearing, an Administrative Law Judge upheld that determination. The Unemployment Insurance Appeal Board affirmed, finding that Groundanywhere was liable for additional unemployment insurance contributions on remuneration paid to claimant and other similarly situated drivers. Groundanywhere appealed.

The Appellate Division affirmed holding "whether an employment relationship exists within the meaning of the unemployment insurance law is a question of fact, no one factor is determinative and the determination of the . . . [B]oard, if supported by substantial evidence on the record as a whole, is beyond further judicial review even though there is evidence in the record that would have supported a contrary decision" (*Matter of Empire State Towing & Recovery Assn., Inc. [Commissioner of Labor], 15 NY3d 433*, 437 [2010]). This analysis requires that "the touchstone of the analysis is whether the employer exercised control over the results produced by the worker or the means used to achieve the results" (*Matter of Vega [Postmates Inc.-Commissioner of Labor], 35 NY3d 131*, 137 [2020]. The Court found "Groundanywhere sets and calculates the fares, keeps a set percent as a fee, charges the client a processing fee, adds a gratuity which, if disputed by the client, results in the driver getting a higher percent of the fare in lieu of a gratuity, collects the charges from the client and pays a percent of the base charge to the drivers, who are paid even if the client fails to show up for the trip or disputes the charges. Although drivers use and maintain their own vehicles and pay all vehicle expenses, they display a Groundanywhere logo and are reimbursed for tolls and parking costs." Thus the relationship was employer-employee rather than independent contractor.

Quotations From Russia With Love

"I like to praise and reward loudly, to blame quietly." - Catherine the Great

"A great wind is blowing, and that gives you either imagination or a headache." - Catherine the Great

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