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**Show Me the Money!  
Maximizing Monetary Recovery in Franchise Cases**

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# SHOW ME THE MONEY!

## MAXIMIZING MONETARY RECOVERY IN FRANCHISE CASES<sup>1</sup>

### I. INTRODUCTION

*Show Me The Money!* Is this the famous Rod Tidwell clarion call from the film *Jerry Maguire* or a shrill plea from your client after having just filed your latest franchise case? If it is the latter and you have not counseled your client about the reality of recovering monetary damages in a franchise action, you have overlooked an essential element of your case – the endgame!

Understanding the basis, scope and limitations for recovering money damages is an important first step. After all, winning the battle but losing the war may not be what your client had in mind. A proper damage analysis could be the difference between bringing an action and searching for other solutions. In other words, is commencing the action worth it? With the endgame in mind, how does counsel calculate, present, and prove the damage amounts the client should seek at trial or in arbitration, and what damage defenses and counter-arguments should counsel present or expect from the opponent?

This paper will outline and discuss the panoply of monetary damages available to franchisors and franchisees. Although equitable relief is an important tool on both sides of the franchise-equation, this paper generally limits the discussion to “legal” or money damages.<sup>2</sup> Monetary relief derives from many sources and comes in many varieties. Some of the areas highlighted include:

- contract damages – expectation damages, direct and consequential damages
- liquidated damages
- lost profits, lost future royalties and lost opportunity
- interest and currency issues
- contract limitations on damages
- nascent businesses and the new business rule
- tort damages and the economic loss rule
- rescission, restitution, and ancillary relief
- statutory relief –disclosure, registration, and relationship laws, business opportunity acts, Little Federal Trade Commission (“FTC”) Acts, The Defend Trade Secrets Act of 2016, and The Racketeering Influenced and Corrupt Organizations Act
- Lanham Act – 15 U.S.C. § 1117
- defenses in general, including mitigation and discounts

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<sup>1</sup> The authors would like to acknowledge the assistance of Wiggin and Dana associate John Foley.

<sup>2</sup> Resources discussing non-monetary relief include: Troy A. Bader, Patrick J. Carter and Deborah S. Coldwell, *Remedies: Damages, Injunctive Relief and Rescission*, ABA 22nd Annual Forum on Franchising, W5 (1999); Deborah S. Coldwell and Kay Lynn Brumbaugh, *Proving Entitlement to Preliminary Injunctions Against Franchisees*, 18 Franchise L.J. 87 (Winter 1999); Barbara A. Bagdon and Mary M. Kellerman, *When Will Courts Issue Preliminary Injunctions to Enforce Restrictive Covenants in Franchise Agreements?*, 28 Franchise L.J. 141, 149 (Winter 2009); Christina L. Fugate, Elizabeth N. Timme and Erin A. Webley, *Specific Performance: A Maverick Remedy Post-eBay and Winter*, 34 Franchise L.J. 2, 199 (Fall 2014); Michael D. Joblove and Peter C. Lagarias, *Franchise Law Remedies: What Do I Want and How Do I Get It*, ABA 36th Annual Forum on Franchising, W14 (2013).

- business fair market value
- punitive and consequential damages
- attorney fees, including the American Rule and exceptions
- Personal liability and guaranties

This paper will also discuss certain practice tips related to the types, methods, and mechanics of proof that focus on the use of expert witnesses.

## II. CONTRACTUAL DAMAGES

The franchise agreement is the obvious starting point for determining the parties' rights and obligations, including the potential entitlement to damages. Parties should consider the possibility of expectation, or "benefit of the bargain," lost profit, liquidated, and consequential damages, as well as damage caps and other limitations. Parties should also consider the availability of rescission and related remedies.

### A. Expectation Damages

A common, and somewhat simplistic, formulation is that a non-breaching party is entitled to the "benefit of the bargain" from the party in breach. Courts often use the term "expectation damages"<sup>3</sup> or "expectation interest"<sup>4</sup> to express this concept. The Restatement (Second) of Contracts defines a party's "expectation interest" as the "interest in having the benefit of [the party's] bargain by being put in as good a position as he would have been in had the contract been performed."<sup>5</sup> In other words, what did the non-breaching party expect to gain by entering into the contract? The Restatement (Second) further explains the appropriate, fairly straightforward sounding method of calculating expectation interest as:

- (a) [T]he loss in the value to [the party] of the other party's performance caused by its failure or deficiency, plus
- (b) any other loss, including incidental or consequential loss, caused by the breach, less
- (c) Any cost or other loss that he has avoided by not having to perform.<sup>6</sup>

As with many simple concepts, however, the devil is often in the details. For example, a franchisee claiming that a franchisor wrongfully refused to approve a proposed transfer (sale) of a franchise could claim that he or she lost the benefit of the bargain of the purchase price. But that would overstate the actual "benefit of the bargain" damages because, although the franchisee may have lost the benefit of a potentially lucrative sale, he or she still has a potentially valuable asset – the unsold franchise.

<sup>3</sup> See, e.g., *United States v. Qurashi*, 634 F.3d 699, 704 (2d Cir. 2011) ("Expectation damages strive to place an aggrieved party in the same economic position it would have been in had both parties fully performed their contractual obligations.") (internal citations and quotations omitted).

<sup>4</sup> See, e.g., *Merry Gentleman, LLC v. George & Leona Prods., Inc.*, 799 F.3d 827, 828 (7th Cir. 2015) ("[E]xpectation interest... involves obtaining the benefit of the bargain, or his reliance interest, which involves reimbursement for loss caused by reliance on a contract.") (internal citations and quotations omitted).

<sup>5</sup> Restatement (Second) Contracts § 344(a).

<sup>6</sup> Restatement (Second) Contracts § 347.

As another example, a franchisor whose franchisee abandoned the location could claim that it lost the benefit of royalties the franchisee would have paid for that location. But again, the calculation may not be as simple as it would first appear. Did the contract provide for liquidated damages (see discussion in Section I.E. below)? Was the franchisor able to take over the location, or did another franchisee begin operating there and paying royalties thereby reducing the franchisor's damages? In this last scenario, could the franchisor claim that it could have sold a new franchise to the successor franchisee, so that the successor's royalty payments should not reduce the damages that the abandoning franchisee should pay?<sup>7</sup>

## **B. Lost Profits and Fair Market Value**

No discussion of money damages would be complete without an exploration of lost profits. But what constitutes "lost profits" for franchisees and franchisors differs dramatically. That is because how franchisors and franchisees derive "profit" diverges: franchisor revenue derives from initial franchise fees, royalties, or licensing fees and sometimes the sale of goods and services to franchisees; while franchisee revenue generally ensues from profits earned by selling goods and services to third parties. Practitioners and courts therefore apply different analyses and methodologies to determine the proper measure of "lost profit" damages for franchisees and franchisors. Although "lost profits" may be easy to conceptualize, they can be difficult to explain and even more challenging to prove.

The disparity in revenue and profit sources requires different determinations of the proper mitigation of damages and may also compel courts to reach "creative" solutions to reach a fair result.<sup>8</sup> Generally speaking, most courts recognize that lost profits are recoverable if the losses are the natural and proximate result of a breach, can be determined with reasonable certainty, are not speculative or conjectural, and were within the parties' contemplation when the contract was formed.<sup>9</sup> Franchisees claiming lost profits will often request annually increasing profits through the remainder of the contractual franchise term, and sometimes even longer by assuming future renewals. Jurisdictions vary in their approaches, but many courts have held that seeking more than a few years of damages is too speculative for recovery.<sup>10</sup> Other courts

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<sup>7</sup> See Section IX.C. for a discussion of various mitigation issues.

<sup>8</sup> One example is *Postal Instant Press, Inc. v. Sealy*, 43 Cal. App. 4th 1704 (1996), discussed at length below. The California Court of Appeals reversed a trial court's award to franchisor Postal Instant Press, Inc. of "almost eight years" of future lost royalties/profits but let stand the award of unpaid past due royalties.

<sup>9</sup> See, e.g., *Burger King v. Weaver*, 169 F.3d 1310 (11th Cir. 1999); *H.J., Inc. v. Int'l Tel. & Tel. Corp.*, 867 F.2d 1531, 1550 (8th Cir. 1989) (awarding future lost profits for attempted monopolization where plaintiff "demonstrated its intent and some ability to market [its product] nationwide"); *T&S Distribs., L.L.C. v. Mich. Bell Tel. Co.*, No. 296257, 2012 WL 954274, at \*7 (Mich. Ct. App. March 20, 2012) ("Damages for lost profits must be amenable to establishment with some amount of certainty beyond pure speculation"); *In re Mid-America Corp.*, 159 B.R. 48, 53–55 (Bankr. M.D. Fla. 1993) (stating that the franchisor was entitled to lost, future royalties for the remaining term of the contract following the franchisee's abandonment of the franchise); *In re Montcastle*, No. 93-10465, Bus. Franchise Guide (CCH) ¶ 10,534, 1994 WL 16100200 (W.D.N.C. Sept. 2, 1994) (granting the franchisor lost future royalties for the remaining term of the contract after the franchisee stopped making royalty payments). Many courts require that the proof be sufficient to allow fact finders to reach a "reasonably certain determination of the amount of gains prevented." See *Glynn v. Impact Sci. & Tech., Inc.*, 807 F. Supp. 2d 391, 428 (D. Md. 2011) (applying New Hampshire law). Courts will often preclude recovery of lost profits damages, when the profit is uncertain or contingent. See, e.g., *Muir v. Navy Fed. Credit Union*, 744 F. Supp. 2d 145, 148–49 (D.D.C. 2010) (citing *Haywood v. Massie*, 188 Va. 176 (1948)).

<sup>10</sup> See *Meineke Car Care Ctrs., Inc. v. RLB Holdings, LLC*, 423 F. App'x 274, 284–85 (4th Cir. 2011) (upholding lost profits for franchisor for three-year period based on historical analysis of franchisee's revenues); *Precision Franchising, LLC v. Gatej*, No. 12-cv-158, 2012 WL 6161223, at \*9 (E.D. Va. Dec. 11, 2012) (finding lost profits

have had no difficulty awarding damages for the full contract term, including renewals.<sup>11</sup> This paper will also discuss fair market value damages when addressing the franchisee side-of-the-coin.

Whether a party in business litigation seeks fair market value or lost profits, it must adequately prove its damages, which cannot be speculative. The plaintiff generally has the burden to prove its damages to a “reasonable certainty”<sup>12</sup> and must, at a minimum, provide a reasonable basis for the damage claim calculation.<sup>13</sup> Jurisdictions vary in their approaches.<sup>14</sup> A franchisor defendant would do well to determine the stringency of proof required under applicable law and educate its damage rebuttal expert in preparation for direct and cross examination. As discussed in more detail in Section X below, both parties will generally use experts to establish and rebut damage theories and calculations.

### **C. Franchisor’s Lost Future Royalties – Lost Future Profits**

When a franchise relationship ends before the franchise agreement’s natural expiration, some franchisors pursue recovery of their lost future profits, typically measured by the loss of royalty payments for the balance of the term. As noted above, most courts agree that the future balance due is a reasonable basis for recovery of money damages provided lost royalty payments are reasonably certain and not speculative.

However, 20 years after the *Postal Instant Press, Inc. v. Sealy* decision,<sup>15</sup> held that a franchisor could not recover lost future royalties when it elected to terminate, a schism remains on two points: 1) what is the nature of the breach and 2) who actually terminated the agreement? This rift gives rise to different damage analyses: a “traditional contract” tack versus a “proximate cause” approach.<sup>16</sup> Although much has been written about the impact and demise

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damage award was reasonably calculated over four-year period); *but cf. Kiddie Acad. Domestic Franchising LLC v. Faith Enters. DC, LLC*, Civ. No. WDQ-07-0705, 2010 WL 673112, at \*5 (D. Md. Feb. 22, 2010) (“courts have been hesitant to award future royalties under a multi-year franchise agreement when there is possible double-recovery, uncertainty in the existence and amount of future royalties, and inability to determine what portion of lost royalties were actually lost profits and not costs attendant to maintaining the franchise relationship”).

<sup>11</sup> Diane Green-Kelly, Steven Kelley and Tamika Langley Tremaglio, *Nuts and Bolts of Damages Claims in Franchise Litigation*, ABA 28th Annual Forum on Franchising, W6 at 12–13 (2005); *see also FMS, Inc. v. Volvo Const. Equip. N. Am., Inc.*, No. 00-C-8143, 2007 WL 844899, at \*11 (N.D. Ill. Mar. 20, 2007) (approving damages calculation of year-to-year for 5 years followed by a terminal value analysis for contract without a termination date).

<sup>12</sup> *Beverly Hills Concepts v. Schatz & Schatz*, 247 Conn. 48, 70 (Conn. 1998); *see also City First Mortg. Corp. v. Barton*, 988 So. 2d 82, 86 (Fla. Dist. Ct. App. 2008) (reversing final judgment and award under FDUTPA because plaintiff-borrower’s speculative damage theory was “insufficient to establish damages under FDUTPA, which provides for recovery only of ‘actual damages.’”); *Himes v. Brown & Co. Sec. Corp.*, 518 So. 2d 937, 938 (Fla. Dist. Ct. App. 1987) (dismissing FDUTPA claim for failure to plead actual damages proximately caused by defendant, noting that “in Florida, unless the fact-finder is presented with evidence which will enable it to determine damages for lost profits with a reasonable degree of certainty, rather than by means of speculation and conjecture, the claimant may not recover such damages.”); *see also* Green-Kelly et al., *supra* note 11, at 5–6; Joblove et al., *supra* note 2, at 22–25.

<sup>13</sup> Christopher P. Bussert, Robert M. Einhorn and Christopher Martinez, *Calculating and Proving Damages in Franchise Termination Cases*, ABA 36th Annual Forum on Franchising, W3 at 12–14 (2008).

<sup>14</sup> *See* Joblove et al., *supra* note 2, at 22–25; Green-Kelly et al., *supra* note 11, at 5–6.

<sup>15</sup> 43 Cal. App. 4th 1704, 51 Cal. Rptr. 2d 365, 368–71 (Cal. Ct. App. 1996).

<sup>16</sup> *See* Rupert M. Barkoff and Christopher P. Bussert, *Can a Franchisor Recover Lost Future Royalties? The Debate Goes On*, 12 The Franchise Lawyer 2 (Spring 2009).

of the *Sealy* court's view<sup>17</sup>, along with considerable criticism,<sup>18</sup> the rationale remains an issue for franchisors seeking recovery of lost future royalties as lost profits. The case is therefore worth a thorough review by defaulting franchisees and their counsel.

In *Sealy*, the California Court of Appeals reversed a trial court's award to franchisor Postal Instant Press, Inc. (PIP) of "almost eight years"<sup>19</sup> of future lost royalties/profits but let stand the award of unpaid past due royalties. The agreement had a 20 year term. The total trial court award was \$432,510.35 (based on average sales for the prior two-years) plus interest, attorney fees, expenses and costs (this also included \$77,300 for past due unpaid royalties). The rationale was that the lost profits that PIP claimed did not arise from the franchisee's failure to pay royalties and advertising fees when due, but rather from PIP's *election* to terminate the franchise relationship. The court primarily used a "proximate cause" approach (further characterized as "natural and direct" cause<sup>20</sup>) and concluded that PIP's *election* to terminate was the proximate cause of the termination, not the franchisee's failure to pay; reasoning that the franchisor could have simply sued for the past due royalties without terminating the agreement, and the franchisee could have continued to operate and pay royalties. The court distinguished the cases that PIP cited to support full recovery because, in its view, in those cases there were "total failures to perform at all."<sup>21</sup> This has been interpreted to mean that even the *Sealy* court may have awarded the lost future royalties if the franchisee had repudiated the agreement or simply abandoned operations. Accordingly, the *Sealy* court indicated that it was not holding franchisors could never collect lost future royalties for a franchisee's breach, but that it depended on the nature of the breach and its impact on the franchisor's ability to receive those payments.<sup>22</sup>

However, the balance of the decision reveals that the court simply did not view the result at trial as fair – labeling it at one point as "unreasonable, unconscionable or grossly oppressive."<sup>23</sup> This was based on common law and California's Civil Code section 3359: "Damages must, in all cases, be reasonable, and where an obligation of any kind appears to create a right to unconscionable and grossly oppressive damages, contrary to substantial justice, no more than reasonable damages can be recovered."<sup>24</sup> The court further rejected

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<sup>17</sup> Douglas R. Hafer and Logan W. Simmons, *Lost Future Royalties: Lessons from Recent Decisions*, 31 Franchise L.J. 150 (Winter 2012); Barkoff et al., *supra* note 16; Robert L. Ebe, David L. Steinberg and Brett R. Waxdeck, *Radisson and the Potential Demise of Sealy, Barnes-Hilton Rule*, 27 Franchise L.J. 3 (Summer 2007); Robert M. Einhorn, *Burger King Corporation v. Hinton, Inc.: Are Lost Future Profits Disappearing?*, 22 Franchise L.J. 159 (Winter 2003).

<sup>18</sup> *Id.* Ebe et al., *supra* note 17; Joseph Schumacher and Kimberly Toomey, *Recovering Lost Future Royalties in a Franchise Termination Case*, 20 Franchise L.J. 116, 118–19 (Winter 2001); Ted P. Pearce, Leigh Reynolds King and J. Cary Tharrington, *The Enforcement of Post-Termination Remedies in the Franchise Contract*, 24 Okla. City U. L. Rev. 81, 106–08 (1999); Mary DeLeo, Note, *Emasculating Goliath: Did Postal Instant Press v. Sealy Strike an Unfair Blow at the Franchising Industry?*, 25 W. St. U. L. Rev. 117, 136–48 (1997).

<sup>19</sup> *Sealy*, 43 Cal. App. 4th at 1708.

<sup>20</sup> *Id.* at 1704.

<sup>21</sup> *Id.* at 1711.

<sup>22</sup> *Id.* at 1713.

<sup>23</sup> *Id.* at 1714.

<sup>24</sup> *Id.* at 1714–15.

PIP's argument based on its concern that to affirm the decision would allow franchisors to pursue lost royalties calculated over a lengthy term even for a very early payment default; the court envisioned a situation akin to economic enslavement.<sup>25</sup> When conceptually discussing mitigation, the court noted: "In our view, PIP's entitlement to recover its past unpaid royalties, along with attorney fees and costs, along with its right to immediately install a new franchisee in what formerly had been the Sealys' exclusive territory provides it with a full measure of 'reasonable' damages."<sup>26</sup> A number of courts have followed *Sealy*.<sup>27</sup>

Other courts have ignored *Sealy* or rejected its premise altogether.<sup>28</sup> *Meineke Car Care Centers, Inc. v. RLB Holdings, LLC*<sup>29</sup> is sometimes cited as a counterpunch to *Sealy*<sup>30</sup> but its facts are distinguishable in that the franchisee voluntarily abandoned operations. Although the decision contains a thorough analysis of general common law (North Carolina), it does not square-off against *Sealy* because it did not involve a termination based on failure to pay.

In *American Speedy Printing Centers, Inc. v. AM Marketing*,<sup>31</sup> however, the Sixth Circuit supplied the opposite view from *Sealy* when the franchisor's termination was based on a failure to pay. Applying Michigan law, the court affirmed the district court's award of lost future royalties to the franchisor. The Sixth Circuit did not mention *Sealy* and offered very little *Sealy*- or *Meineke*-like analysis. Rather, the court stated that "To create uncertainty as to the fact of future profits, therefore, [the franchisee] must provide evidence that [it] was likely to fail in some way, or become unprofitable, such that sales would end *but without any breach of the franchise agreement*. [The franchisee's] mere suggestion that the continued success of the business was difficult to predict, or even [the franchisee's] statement that the business had ceased operations, is not sufficient to create uncertainty as to the fact of future profits/royalties."<sup>32</sup> Thus, the only way to reach a *Sealy*-like result was for the franchisee to prove that there was a complete collapse of the business (no revenue) without a violation of the agreement, a very unlikely scenario.

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<sup>25</sup> *Id.* at 1718.

<sup>26</sup> *Id.* at 1715.

<sup>27</sup> *Medical Shoppe Int'l, Inc. v. TLC Pharmacy, Inc.*, No. 4-09-CV-00683-AGF, 2010 WL 2757328, at \*1 (E.D. Mo. July 12, 2010) (rejecting the franchisor's claim of \$748,029 for future lost license fees when finding that future license fees were neither expressly stated, nor meant to survive the termination); *Kissinger, Inc. v. Singh*, 304 F. Supp. 2d 944, 950–51 (W.D. Mich. 2003) (reaching the same conclusion as *Sealy*); *Burger King Corp. v. Hinton, Inc.*, 203 F. Supp. 2d 1357, 1366 (S.D. Fla. 2002) (reaching the same conclusion as *Sealy*); *I Can't Believe It's Yogurt v. Gunn*, No. Civ. A. 94-OK-2109-TL, 1997 WL 599391, at \*65 (D. Colo. Apr. 15, 1997) (loss of future royalties was proximately caused by the franchisor's election to terminate agreements); see also *Moran Indus., Inc. v. Mr. Transmission of Chattanooga, Inc.*, 725 F. Supp. 2d 712, 720–23 (E.D. Tenn. 2010) (collecting and discussing cases examining whether a franchisor can ever be entitled to recover lost profits after terminating a franchise agreement for the franchisee's breach of contract).

<sup>28</sup> See, e.g., *Progressive Child Care Sys., Inc. v. Kids 'R' Kids Int'l, Inc.*, No. 2-07-127-CV, 2008 WL 4831339 (Tex. App. Nov. 6, 2008).

<sup>29</sup> 423 F. App'x 274 (4th Cir. 2011).

<sup>30</sup> See Joblove at al., *supra* note 2, at 26–27.

<sup>31</sup> 69 F. App'x. 692 (6th Cir. 2003).

<sup>32</sup> *Id.* at 699 (emphasis added).

The 2011 decision in *Vino 100, LLC v. Smoke on the Water, LLC*<sup>33</sup> shows that the debate and uncertainty continue. The franchisor claimed \$289,940.00 in lost future royalties. The franchisee countered that breach of the franchise agreement, sublease, and the personal guaranty contracts did not cause the lost future royalties instead contending (à la *Sealy*) that the decision to terminate the franchise relationship was the proximate cause of any lost future royalties.

The district court cut to the quick in articulating the continuing divide:

In cases where a franchisor terminated the franchise relationship due to a franchisee's failure to pay royalties..., courts have generally found that the lost future royalties were caused by the franchisor's decision to end the relationship and not by the franchisee's prior failure to comply with the contract. See *Burger King Corp. v. Hinton, Inc.*, 203 F.Supp.2d 1357, 1366–67 (S.D.Fla.2002); \*286 *I Can't Believe It's Yogurt v. Gunn*, No. 94–2109, 1997 WL 599391, at \*22–25, 1997 U.S. Dist. LEXIS 14480, at \*60–\*65 (D.Colo. Apr. 15, 1997); *Postal Instant Press v. Sealy*, 43 Cal.App.4th 1704, 51 Cal.Rptr.2d 365, 368–71 (Cal.Ct.App.1996). These courts reason that the franchisor could allow the contractual relationship to continue and sue the franchisee to recover past-due amounts. In cases where a franchisee has voluntarily abandoned or terminated the franchised business, however, courts have held that the franchisee's decision to close the business caused the loss of future royalties to the franchisor notwithstanding that the franchisor may have subsequently terminated the contract. See *Meineke Car Care Ctrs., Inc. v. RLB Holdings, LLC*, 423 Fed.Appx. 274, 281–83, n. 8 (4th Cir.2011); *Lady of Am. Franchise Corp. v. Arcese*, No. 05–61306, 2006 U.S. Dist. LEXIS 68415, at \*13–17 (S.D. Fla. May 25, 2006); *Burger King Corp. v. Barnes*, 1 F. Supp. 2d 1367 (S.D. Fla.1998).<sup>34</sup>

The court resolved the matter by not resolving it, finding genuine issues of material fact on the crucial question of causation of lost future royalties.<sup>35</sup>

In November of 2014 in *Legacy Academy, Inc. v. JLK, Inc.*<sup>36</sup>, the Georgia Court of Appeals reversed a trial court decision and held that although franchisors were entitled to recover future lost royalties until the end of the term, the franchisor's proof of lost profits was insufficient because it failed to account for the expenses it would have incurred in realizing the profit. And the beat goes on.<sup>37</sup>

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<sup>33</sup> 864 F. Supp. 2d 269 (E.D. Pa. 2012).

<sup>34</sup> *Id.* at 285–86.

<sup>35</sup> See *id.* at 285.

<sup>36</sup> 765 S.E.2d 472 (Ga. Ct. App. 2014).

<sup>37</sup> See *Am. Outdoorsman, Inc. v. Shadow Beverages & Snacks, LLC*, No. 13-443, 2014 WL 7335027 (W.D. Pa. Dec. 19, 2014) (distinguishing *Sealy* due to the language of the license agreement and the guaranteed nature of the future royalty payments).



#### **D. Franchisee Lost Profits and Fair Market Value**

Franchisees often pursue lost profit damages as well. Causation is typically not at issue, at least when wrongful termination triggers the franchisee's claim. However, the damage analyses are far different than those applied to franchisors. Loss of revenue/profit is one starting point while fair market value of the business is another. As discussed later in this paper<sup>38</sup>, a franchisee cannot recover both, and determining a franchise's fair market value is particularly complicated when the business is new or of short duration.

Courts employ a variety of business valuation methods<sup>39</sup> and experts are usually at the core of the requisite proof. Historically, courts have held that franchisees are entitled to the future profits they would have earned had the franchise remained in effect.<sup>40</sup>

##### **1. Future Lost Profits - Franchisee**

Franchisees pursuing "lost profit" damages must meet a uniformly accepted threshold: lost profit evidence must be reasonably accurate, constitute a fair basis for future projection, take into account projected cost as well as projected revenue, and be adjusted for present value.<sup>41</sup> Although a number of evidentiary approaches are possible, the most straightforward is presenting well-maintained business records along with the testimony of the owner and accountant. While this alone should suffice,<sup>42</sup> most practitioners would likely take the further step of retaining an expert witness to discuss reasonable projections and the basis for future lost profits. Selecting the right expert with franchise-industry-specific-knowledge should be paramount.<sup>43</sup>

In addition to a franchisee's business records, data in possession of other franchisees and the franchisor should be a reliable and persuasive basis for calculating lost profits. Most franchisors routinely require gross sales reports, compare these reports from location to location, and employ these metrics to calculate royalties and counsel underperforming franchisees. Assuming the system is successful, no more compelling evidence than that secured from the franchisor and other franchisees would appear to exist; especially if that data support the franchisee's business record data.

It should be noted that an acceptable lost profits award cannot side-step the application of discount rates, discussed in Section IX.A. below.

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<sup>38</sup> See Section IX (discussing mitigation and double recovery).

<sup>39</sup> See Nicole Liguori Micklich, Michael W. Lynch and Ingrid C. Festin, *The Continuing Evolution of Franchise Valuation: Expanding Traditional Methods of Franchise Valuation*, 32 Franchise L.J. 223 (Spring 2013).

<sup>40</sup> *Martin Motor Sales v. Saab-Scania of Am., Inc.*, 452 F. Supp. 1047 (S.D.N.Y. 1978), *aff'd*, 595 F.2d 1209 (2d Cir. 1979); *Buono Sales, Inc. v. Chrysler Motors Corp.*, 449 F.2d 715 (3d Cir. 1971).

<sup>41</sup> *Century 21 Real Estate Corp. v. Meraj Int'l Inv. Corp.*, 315 F.3d 1271, 1282 (10th Cir. 2003).

<sup>42</sup> See *Pullman v. Land O'Lakes, Inc.*, 262 F.3d 759, 765 (8th Cir. 2001) (lay testimony from business owner was sufficient to establish a claim for lost profits); *Diesel Mach., Inc. v. B.R. Lee Indus.*, 328 F. Supp. 2d 1029, 1039-40 (D. S.D. 2003) (admitting opinion testimony from company president to establish evidence of lost profits).

<sup>43</sup> See Bruce S. Schaeffer and Susan Ogulnick, *Why Valuing Franchise Businesses Is Different from Valuing Other Businesses*, Bus. Appraisal Practice 37-41 (2008).

## 2. Fair Market Value (FMV)

Alternatively, franchisees may seek damages based on the then-FMV of the franchised business. Although it is difficult here to give full measure to all the intricacies of the FMV approach, we will review the high points and guide you to helpful resources.<sup>44</sup>

Pursuing a FMV approach may be far more complicated than a future lost profit line of attack. For this reason, it may be imperative to retain an expert witness. Issues related to the presentation of expert witnesses and their methodologies are addressed in Section X below. However, selecting an appropriate expert is essential. One prominent commentator has written "...considering that valuing a franchise business can be very different from valuing other businesses, valuation analysts, litigators and accountants need to familiarize themselves with some of the basic elements of franchising."<sup>45</sup> Familiarity with franchising is important because the franchise relationship is unique. "Management" of the business is more complex because of the franchise system controls and applicability of various franchise laws.<sup>46</sup>

Generally, FMV is an *estimate* of the value at a particular point in time of a business or asset based on what a knowledgeable and willing buyer would pay an unpressured and knowledgeable seller.<sup>47</sup> Because this is easier said than done, there are different ways to determine FMV. The most accepted and arguably reliable is comparable sales.<sup>48</sup> There may be a ready source from prior franchise transfer and sales, at least for established franchise systems. Both the franchisor and former franchisees may have past sales data, which franchisees can obtain through voluntary cooperation or discovery. This will be valuable information for testifying experts to consider. Indeed, having the expert assist in identifying information to obtain is a useful first step and another reason why it is important to retain an expert who has specialized franchise knowledge.

*Warren Distributing Co. v. InBev USA, LLC*<sup>49</sup> illustrates some of the complexities encountered when seeking FMV damages. This case concerned the New Jersey Malt Beverage Practice Act<sup>50</sup> and the valuation of a group of terminated beer distributorships. The statute required a FMV payment to the terminated distributors and defined FMV as "the price at which the asset would change hands between a willing seller and a willing buyer when neither is acting under compulsion and when both have knowledge of the relevant facts."<sup>51</sup>

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<sup>44</sup> Micklich et al., *supra* note 39.

<sup>45</sup> Schaeffer et al., *supra* note 43.

<sup>46</sup> State and federal franchise laws are discussed in Section III.D. below.

<sup>47</sup> See New Jersey Malt Beverage Practice Act, N.J. Stat. Ann. § 33:1-93:12 (2006), for a similar definition.

<sup>48</sup> Micklich et al., *supra* note 39, at 223.

<sup>49</sup> Civ. No. 07-1053, 2010 WL 2179167 (D. N.J. May 28, 2010).

<sup>50</sup> N.J. Stat. Ann. § 33:1-93:12 (2006).

<sup>51</sup> N.J. Stat. Ann. § 33:1-93:14(c).

The distributors had a different approach to determining FMV than the brewers involved (InBev USA and Anheuser). The difference resulted in a more than \$40 million gap. The brewers argued for a “market multiples valuation”—taking gross profits from the most recent year and multiplying those profits by multiples taken from comparative transactions with some added kickers. The distributors contended that the proper method was “discounted cash flow.” Although the court never explains this, in simple terms, discounted cash flow tries to determine the value of a company today based on projections of how much it is expected to make in the future. Under this analysis, a company is worth all of the cash that it could make available to investors in the future. It is called discounted cash flow because cash in the future is worth less than cash today.<sup>52</sup> The court noted that the “market multiples valuation” method had routinely been used in other transactions. (Discounting is discussed in more detail in Section IX.A. below)

The battle of the experts had mixed results. The *Warren* court denied the brewers’ *Daubert* motion,<sup>53</sup> allowing the distributor’s “discounted cash flow” method to go before the jury. However, the jury rejected the distributors’ methodology.<sup>54</sup> In permitting the competing methods, the court also allowed the experts to articulate the rationales for the different multiples applied. Clearly, the jury liked the method and multiples applied by the brewers’ expert. This resulted in a \$25,057,784 award to the distributors instead of the \$65,656,395 they sought.

Commentators have observed that, based on the *Warren* court’s discussion, the significance of this outcome is not due to the contrasting valuation *methods* but rather the *multipliers* that the experts used.<sup>55</sup> Another takeaway is that these valuation disputes may be decided by juries. Finally, *Warren* demonstrates that a \$40 million gap may be compelling motivation to select the right expert and submit the issue to a jury, even when the methodology may not be as widely accepted as your opponent’s approach.

### **3. New Business Rule and Lost Profits**

Seeking lost profit damages for a new business is challenging. As noted earlier, lost profit evidence must be reasonably accurate and, as some jurisdictions require, must be reasonably certain. See Section IX.

A common law doctrine known as the “new business rule” can bar certain lost profits claims as a matter of law. Some commentators have noted that, “In its strongest form, this rule prohibits a plaintiff from recovering any lost profits for a newly established enterprise: ‘[A] new business, or an existing business with a new product, cannot recover lost profits because the future profits of a new business cannot be ascertained with any degree of certainty.’”<sup>56</sup> The

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<sup>52</sup> See Ben McClure, *Discounted Cash Flow Analysis*, Investopedia (April 2016), available at <http://www.investopedia.com/university/dcf/>.

<sup>53</sup> *Daubert* motions are discussed in more detail in Section X below.

<sup>54</sup> No. 07-1053, 2011 WL 770005, at \*1 (D. N.J. Feb. 28, 2011).

<sup>55</sup> Micklich et al., *supra* note 39, at 232. The experts used different “multipliers” of gross profits for domestic and European brands from the year before termination. The brewers used 2.5 for domestic brands and 3.3 for European brands, and the distributors’ expert used 8.4. *Warren*, 2010 WL 2179167, at \*3–5.

<sup>56</sup> *Kinesoft Dev. Corp. v. Softbank Holdings, Inc.*, 139 F. Supp. 2d 869, 908 (N.D. Ill. 2001) (applying Illinois law) (citations omitted).

justification for the new business rule traditionally has been that the concerns regarding speculativeness of lost profits claims are even stronger when an enterprise has no history of revenue and profits.”<sup>57</sup>

Query whether this is true for a franchised business? After all, there is often an established system, typically a track record, many similar businesses offering the same product or service, sales reports and, in some cases, financial performance representations to call upon. Arguably, new franchised businesses are in a much better position than non-franchised businesses to demonstrate future lost profits with reasonable certainty. Further, there is a trend away from rigid enforcement of the “new business rule” and towards a reasonable proof standard that complements the favorable circumstance of new franchised businesses.<sup>58</sup> A number of cases bear this out:

- *No Ka Oi Corp. v. Nat'l 60 Minute Tune, Inc.*<sup>59</sup> – giving the green light to recovery for future lost profits when franchisee had yet to open single unit in the territory. “Proof of the nationwide character of the franchise business at issue provided an ample basis for computation of probable losses.”
- *613 Fairview Ave., L.L.C. v. Pong's Corp., Inc.*<sup>60</sup> – lost profits granted in delayed opening of new business caused by landlord. Expert relied on financial data from similar franchisees in the same system to overcome the “new business rule.” National franchise system attributes (uniform advertising, quality control, data collection) provided a “reasonable basis for estimating loss.”
- *Am.'s Favorite Chicken Co. v. Samaras*<sup>61</sup> – franchisor breach led to 20-year award of lost profits for a franchise that never opened. The court noted that: “It is the activity that is the enterprise, and if the activity is well-established, the fact that a newly formed entity is engaging in the activity will not preclude recovery[,]” and “[t]he historical data on the franchise operations provided an intelligent objective basis for [franchisee's] damage model, and we find the testimony of [franchisee's] expert provided more than a scintilla of evidence to support the jury's damage award.”<sup>62</sup>

Nevertheless, courts will reject a lost profit award to new franchised businesses when the brand and franchise system itself are new and unestablished.<sup>63</sup> Where the franchise system

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<sup>57</sup> Joseph Wylie and Christopher Fahy, *Proving and Defending Lost-Profits Claims*, ABA Bus. Torts J. 7 (Fall 2007).

<sup>58</sup> See David A. MacPherson and Stanley P. Stephenson, *Lost Profits Damages to New Businesses: Adjusting for Survival*, 1 J. of Bus. Valuation and Econ. Loss Analysis 1 (2006).

<sup>59</sup> 71 Wash. App. 844, 863 P.2d 79 (Wash Ct. App. 1993).

<sup>60</sup> 115 Wash. App. 1012, 2003 WL 14194 (Wash. App. Jan. 21, 2003).

<sup>61</sup> 929 S.W.2d 617 (Tex. Ct. App. 1996).

<sup>62</sup> *Id.* at 629.

<sup>63</sup> See *Otis v. Doctor's Assocs.*, No. 94-C-4227, 1998 WL 673595 (N.D. Ill. Sept. 14, 1998). Ms. Appleby's firm represented the defendant in that case.

is unestablished but similar to other systems in the marketplace, counsel should explore contacting industry sources and experienced experts to determine if there is a case for recovery. Moreover, with more start-up franchise systems being encouraged to offer Item 19 Financial Performance Representations under the relaxed FTC/NASAA-standards, "reasonable proof" may be there for the taking. Following the trend of focusing on reasonable proof may provide an opening where none was previously thought to exist.

#### **4. Interest and Currency Issues**

Plaintiffs should be sure to request the appropriate measure of prejudgment interest to bolster any potential award. Courts use various means to determine the appropriate interest rate to apply in a given case, including using an interest rate established by statute<sup>64</sup> or establishing an average interest rate for the years in which the damage being compensated was caused.<sup>65</sup> Absent a controlling statute, courts generally have the discretion to determine whether interest should be calculated as simple or compound.<sup>66</sup> Plaintiffs should request compound interest when possible because compounding can significantly increase the award.<sup>67</sup>

Post-judgment interest on an award should also be available. In state cases, courts generally award post-judgment interest pursuant to state law. Federal courts sitting in diversity determine awards pursuant to federal law.<sup>68</sup> The post-judgment interest rate is calculated at the time of the award, and runs until the judgment is paid. The rate is usually governed by state statute or, in federal cases, by the "weekly average 1-year constant maturity Treasury yield, as published by the Board of Governors of the Federal Reserve system, for the calendar week preceding the date of the judgment."<sup>69</sup>

Finally, franchise litigants engaged in international business disputes will need to petition the court or fact finder to determine the proper currency and currency conversion rates for their claims. Many states have adopted the Uniform Foreign-Money Claims Act,<sup>70</sup> which generally provides that the proper currency for a damage award is the currency the parties used in their normal dealings, the currency commonly used in international trade for the commodity or

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<sup>64</sup> See, e.g., *Alaska Rent-A-Car, Inc. v. Avis Budget Group, Inc.*, 738 F.3d 960, 975 (9th Cir. 2013) (applying a New York statutory interest rate of 9% per annum to lost profits awarded to the prevailing party).

<sup>65</sup> See, e.g., *Ecolab, Inc. v. Gardner Mfg. Co., Inc.*, No. Civ. 98-2294-MJDJGL, 2003 WL 1856434, at \*1 (D. Minn. Apr. 9, 2003) (using the average interest rate set by the U.S. Department of Treasury between 1995 and 2003 to calculate interest).

<sup>66</sup> See Mark A. Allen, Robert E. Hall and Victoria A. Lazear, *Reference Guide on Estimation of Economic Damages*, Reference Manual on Scientific Evidence 457–58 (The Nat'l Academies Press, 3d ed.).

<sup>67</sup> *Id.* at 491.

<sup>68</sup> 28 U.S.C. § 1961; see also *Eurodrip, USA, Inc. v. B & B Drip Irrigation, Inc.*, No. 1:09-cv-00716-AWI, 2009 WL 2365845, at \*7 (E.D. Cal. July 31, 2009).

<sup>69</sup> 28 U.S.C. § 1961(a); see also *Eurodrip*, 2009 WL 2365845, at \*7.

<sup>70</sup> See, e.g., Conn. Gen. Stat. § 50a-50, *et seq.*

service involved, or the currency in which the plaintiff incurred its loss.<sup>71</sup> Parties may submit expert evidence regarding applicable currency conversion rates or ask the court to take judicial notice of conversion rates and their potential changes over the life of the parties' claims.

### E. Liquidated Damages

Franchisors may be able to avoid much of the skirmishing over lost future royalties and profit by crafting a reasonable liquidated damages provision. As Barkoff and Bussert commented in their 2009 article in *The Franchise Lawyer* (which advocated for a more sensible approach to the prominent issues in the “Sealy debate”):

In fact, when informally asked what ‘should’ be a ‘fair’ settlement of a lost future royalties dispute, many attorneys suggest that two or three years would be an appropriate level of compensation. These opinions may be anecdotal in nature, but they do demonstrate to some level what is considered reasonable in the franchise community on this issue. In addition, when franchise agreements provide for *liquidated damages* if the franchisee improperly terminates, two to three years of royalties is often offered (and upheld by courts) as a reasonable compromise.<sup>72</sup>

As a practical matter, the reason “two to three years” seems to offer a “reasonable compromise” is that in a viable market, it should not take a franchisor much longer to find a replacement franchisee. And isn't that the point of awarding damages: to make the non-breaching party reasonably whole?

Indeed, according to The Restatement (Second) of Contracts, § 356(1), the enforceability of a liquidated damages provision largely depends on whether it constitutes a reasonable approximation of compensation to the non-breaching party.<sup>73</sup> This principal generally prevails throughout the American court system because the Restatement is adopted in most states, although what is “reasonable” varies from state to state. The same holds true whether liquidated damages will be perceived as a “penalty.”<sup>74</sup> In addition, validity of liquidated damages depends on (1) whether the amount fixed is a reasonable approximation of the loss anticipated *when the contract is made*, and (2) the difficulty of proof of loss.<sup>75</sup>

The 2010 *Franchise Law Journal* article *Liquidated Damages*, authored by Forum colleagues Deborah S. Coldwell, Altresha Q. Burchett-Williams, and Melissa L. Celeste, is extremely helpful in determining the state-by-state views and procedures on the enforceability of

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<sup>71</sup> See, e.g., Conn. Gen. Stat § 50a-54(a).

<sup>72</sup> Barkoff et al., *supra* note 16, at 10 (emphasis added).

<sup>73</sup> The Restatement (Second) of Contracts § 356(1), comment a.

<sup>74</sup> The Restatement (Second) of Contracts § 356(1) provides: “Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.”

<sup>75</sup> *Id.* at comment b.

liquidated damages.<sup>76</sup> Not only does the article offer an expanded discussion of this topic, the attached Appendix provides a 50-state survey of the various tests for enforceability. Most notable is that Minnesota<sup>77</sup> and North Dakota<sup>78</sup> prohibit liquidated damages clauses in franchise agreements. Because a reasonable liquidated damages provision may be more favorable to a franchisee than the recovery of full lost profits, one wonders whether these prohibitions do more harm than good from the franchisee's perspective.

A number of recent cases in the hotel and restaurant industries address the enforceability of liquidated damages:

- *Super 8 Worldwide, Inc. v. Windsor Real Estate, LLC*<sup>79</sup> – liquidated damages of over \$150,000, and \$175,000 in past due lost royalties granted by default judgment. Franchisee failed to provide proof of insurance coverage and stopped paying royalties.
- *Super 8 Worldwide, Inc. v. Anu, Inc.*<sup>80</sup> – court awarded liquidated damages when franchisee abandoned operation of hotel and did not respond to a summary judgment motion.
- *Shoney's North America, LLC v. Smith & Thaxton, Inc.*<sup>81</sup> – franchisee abandoned operation of two restaurants. Termination was conceded as proper but franchisee challenged validity of liquidated damage clause as a penalty and not a reasonable estimate of damages. After considering whether the damages were a reasonable estimate and if actual damages were indeterminable at the time of contracting, the court awarded liquidated damages. Marketing fund contributions were included in the calculation and permitted, despite franchisee's challenge.
- *HLT Existing Franchise Holding LLC v. Worchester Hospitality Group, LLC*<sup>82</sup> – the Second Circuit affirmed a lower court's finding<sup>83</sup> that liquidated damages were

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<sup>76</sup> Deborah S. Coldwell, Altresha Q. Burchett-Williams and Melissa L. Celeste, *Liquidated Damages*, 29 Franchise L.J. 211 (Spring 2010).

<sup>77</sup> *Id.* at 212, Appendix and n.51, stating: "Minn. R. 2860.4400; Minn. Stat. § 80C.01-22; *Nolan v. HairColorXpress Int'l, LLC*, No. 0:04-cv-03037-JNE-SRN, Bus. Franchise Guide (CCH) ¶ 13,049 (D. Minn. Mar. 8, 2005); *Holiday Hospitality Franchising, Inc. v. H-5, Inc.*, No. Civ. 99-1494-DWF-RLE, Bus. Franchise Guide (CCH) ¶ 12,215 (D. Minn. Mar. 26, 2001)."

<sup>78</sup> Coldwell et al., *supra* note 76, at 212, Appendix and n.75, stating: "Securities Commissioner Policy Regarding Conduct That Is Unfair, Unjust, or Inequitable to North Dakota Franchisees, Bus. Franchise Guide (CCH) ¶ 5,340.05; N.D. Cent. Code § 51-19-09 (authorizing the Commissioner to deny the effectiveness of any registration if the Commissioner finds that the offer, sale, or purchase of the franchise would constitute misrepresentation or deceit to purchases, or that the offeror is engaging in fraudulent or deceptive practices in connection with the offer). Note that there is an ongoing debate regarding the ability of the Securities Commissioner to set substantive terms of the parties' agreement in the absence of direct authority from the state legislature or courts."

<sup>79</sup> No. 13-5620, 2014 WL 5475217 (D. N.J. Oct. 28, 2014).

<sup>80</sup> No. 13-4852, 2015 WL 1969138 (D. N.J. Apr. 29, 2015).

<sup>81</sup> No. 3:12-cv-00625, 2015 WL 5139304 (M.D. Tenn. Sept. 1, 2014).

<sup>82</sup> 609 F. App'x 669 (2d Cir. 2015).

reasonable; three years' worth of royalty and program fee payments, based on average fees over last two years, were awarded. The lower court found that the liquidated amount bore a reasonable relationship to the probable loss and that the actual loss could not be determined. The Second Circuit rejected the argument that the lower court ignored franchisee's expert witness's view that only one year was needed to construct a new hotel, noting that expert failed to opine on the length of time to find a substitute franchisee.

- *Days Inn Worldwide, Inc. v. Yamuma Kunj, LLC*<sup>84</sup> – although the court awarded attorney fees and \$114,477.30 in “outstanding Recurring Fees” on a default judgment, it denied enforcement of an “eight year” liquidated damages period. The court viewed the operation of the provision as “a penalty rather than a *bona fide* estimate of damages.” The interesting twist in this case is that the liquidated damages provision in the standard franchise agreement providing for a two-year period of calculation was superseded by an Indiana Addendum that could allow for a larger recovery than Days Inn's standard clause. (“...you covenant to pay to us within 10 days after demand compensation for all damages, losses, costs and expenses (including reasonable attorney's fees) incurred by us and/or amounts which would otherwise be payable for and *during the remainder of the unexpired Term of the License Agreement* but for such termination.”(emphasis added)). The decision does not indicate whether the State of Indiana required the Addendum but no other reason is apparent from the ruling. Based on the Addendum language, Days Inn requested \$199,808.15, which included \$135,517.69 characterized as “actual damages” plus \$64,290.46 interest; but, the court called it “an unenforceable liquidated damages clause.” The court noted that enforcing the Addendum provision would result in eight years' worth of Recurring Fees, instead of the two years' worth that was superseded. Further, Days Inn also inappropriately did not discount the \$135,517.69 to present value and sought interest on the amount as well.

## **F. Limiting Claims and Time to Initiate**

In order to gain certainty and limit exposure, franchisors commonly insert clauses seeking to limit the time frame for asserting a claim, the type or amount of damages, or all of the above. These types of provisions are commonly, although not universally, judicially enforced.<sup>85</sup>

### **1. Limiting time frames for asserting claims**

A clause limiting the time frames in which to assert a claim could be as simple as: “To the maximum extent permitted by law, no claim arising out of or relating to this agreement may be brought more than a year after the occurrence of the event giving rise to the claim.” Some may be more elaborate and also incorporate particular notice requirements and or mediation before commencing litigation or arbitration. It may also be prudent to consider clarifying application of this time limitation to particular claims. For example, a franchisor might want to

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<sup>83</sup> No. 12 CIV. 8295 (PAE), Bus. Franchise Guide (CCH) ¶15,215 (S.D.N.Y. Jan. 28, 2014).

<sup>84</sup> No. 13-cv-6053-KM, 2015 WL 2194507 (D. N.J. May 11, 2015).

<sup>85</sup> *Chin v. Advanced Fresh Concepts Franchise Corp.*, 194 Cal. App. 4th 704, 708, 123 Cal. Rptr. 3d 547, 551–52 (Cal. App. 4th 2011); *Saey v. Xerox Corp.*, 31 F. Supp. 2d 692, 701 (E.D. Mo. 1998).



include that, “Claims brought pursuant to this Agreement’s obligation to indemnify will be considered timely if brought within one year after any final award or judgment giving rise to the obligation to indemnify, but such claims may be asserted earlier to recover any amounts for which indemnity is owed.”

Some jurisdictions routinely enforce these time limitations and notice provisions, which effectively shorten the statute of limitations period that would otherwise apply to the claim.<sup>86</sup> When enforcing a one-year time limitation, one Ohio appellate court commented: “In construing the terms of a written contract, our primary objective is to give effect to the intent of the parties, which is presumed to rest in the language they have chosen to employ.”<sup>87</sup> Other states frown on them.<sup>88</sup> Some jurisdictions will review the provisions and enforce them only if they are reasonable,<sup>89</sup> and some might refuse to enforce them if they find them to be “unconscionable.”<sup>90</sup> Some jurisdictions will enforce them for some claims but not for others, such as “non-waivable” statutory rights.<sup>91</sup> Jurisdictions also vary on how, or if, they will apply

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<sup>86</sup> See, e.g., *Air Brake Sys., Inc. v. TUV Rheinland of N. Am., Inc.*, 699 F. Supp. 2d 462, 470 (D. Conn. 2010) (collecting cases for the proposition that Connecticut and federal “jurisprudence has recognized that parties to a contract may require a specific period of time within which to assert their respective claims, and that longer statutes of limitation do not prevent such agreements as a matter of principle”); see also *Deming v. Nationwide Mut. Ins. Co.*, 279 Conn. 745, 753, 905 A.2d 623, 629–30, n. 9 (2006) (recognizing that the contractual three-year time limitation applied to the claims, rather than the six-year limitation imposed by Connecticut General Statutes § 52-576); *Voris v. Middlesex Mut. Assur. Co.*, 297 Conn. 589, 595–96, 999 A.2d 741, 745–46 (2010) (parties bound by time limitation in policy even if it was a contract of adhesion); see also *MedValUSA Health Programs, Inc. v. Memberworks, Inc.*, 273 Conn. 634, 657, 872 A.2d 423, 438, n.14 (2005) (noting that parties “negotiate whatever limits they deem appropriate on the scope of the arbitrators’ powers,” including “opt[ing] to include in arbitration clauses language that either caps or precludes punitive damages altogether”); *Joseph Schott, LLC v. Medrea*, No. 106007153, 2011 WL 5842774, at \*14 (Conn. Super. Ct. Nov. 1, 2011) (plaintiff not entitled to lost profits where contract provided that he “waive[d] claims for consequential damages . . . including but not limited to . . . loss of profit”); *Amica Mut. Ins. Co. v. S. Cent. CT Reg.*, No. CV085020379S, 2009 WL 5511282, at \*2 (Conn. Super. Ct. Dec. 16, 2009) (denying claim for consequential damages where contract expressly excluded such damages); *Pai v. DRX Urgent Care, LLC*, No. 13-4333, 2014 WL 837158, at \*9 (D. N.J. Mar. 4, 2014) (holding that contractual limitation periods are enforceable under both New Jersey and Maryland law provided that the limitations period is reasonable and does not violate public policy); *Storto Enters., Inc. v. Exxonmobil Oil Corp.*, Civil No. WDC-10-1630, 2011 WL 231877, at \*5 (D. Md. Jan. 24, 2011) (recognizing parties’ ability to agree to reasonable, shorter periods of limitation in contracts, including a one-year contractual limitation period).

<sup>87</sup> *Buffalo Wings & Rings, L.L.C. v. M3 Restaurant Group, L.L.C.*, No. 14AP-980 2015-Ohio-3843, at ¶ 13, 2015 WL 5555158, at \*3 (Ohio Ct. App. Sept. 22, 2015). In this matter, it was the franchisor’s claim that ended up being time-restricted.

<sup>88</sup> See, e.g., Fla. Stat. § 95.03 (“Any provision in a contract fixing the period of time within which an action arising out of the contract may be begun at a time less than that provided by the applicable statute of limitations is void.”); *Maxcess, Inc. v. Lucent Techs., Inc.*, 433 F.3d 1337 (11th Cir. 2005) (noting that Florida does not allow parties to shorten limitations periods); *City of Picayune v. Landmark Am. Ins. Co.*, Civ. No. 11-cv-00435, 2013 WL 392484, at \*3 (S.D. Miss. Jan. 31, 2013) (Mississippi “will not enforce contractually created time limitation on suits”).

<sup>89</sup> See, e.g., *Trzeciak v. State Farm Fire & Cas. Co.*, 809 F. Supp. 2d 900, 910 (contractual limitation period is enforceable if a reasonable time is afforded).

<sup>90</sup> See *Jackson v. S.A.W. Entm’t Ltd.*, 629 F. Supp. 2d 1018, 1028 (N.D. Cal. 2009) (“Contractual agreements to shorten the statute of limitations period are generally disfavored... [but] are not necessarily unenforceable. The critical question is whether the period fixed is so unreasonable so as to show imposition or undue advantage in some way.”) (internal quotations omitted); *Aull v. McKeon-Grano Assocs., Inc.*, Civ. Action No. 06-2752, 2007 WL 655484, at \*7 (D. N.J. Feb. 26, 2007) (conducting an analysis of whether a contractual statute of limitations provision was unconscionable).

<sup>91</sup> See, e.g., *Wineman v. Durkee Lakes Hunting & Fishing Club, Inc.*, 352 F. Supp. 2d 815 (E.D. Mich. 2005) (contractual limitation periods are enforceable for common-law claims but not claims under the Fair Labor Standards

the “discovery rule” for when claims begin to accrue. For example, some jurisdictions will not start the limitations clock until the resulting damage actually occurs,<sup>92</sup> some will look to when the offending act was, or reasonably should have been, discovered,<sup>93</sup> and some will start the clock ticking when the offending act occurred, regardless of when it was discovered<sup>94</sup>

## **2. Limiting the type of damages recoverable**

Franchise agreements similarly often limit the type of damages recoverable. For example, a franchisor might insert the following clause in its standard franchise agreement:

EACH PARTY HEREBY WAIVES, WITHOUT LIMITATION, ANY RIGHT IT MIGHT OTHERWISE HAVE TO ASSERT A CLAIM FOR AND/OR TO RECOVER LOST PROFITS AND OTHER FORMS OF CONSEQUENTIAL, INCIDENTAL, CONTINGENT, PUNITIVE AND EXEMPLARY DAMAGES FROM THE OTHER EXCEPT AS EXPLICITLY PROVIDED IN THIS AGREEMENT. EACH PARTY'S LIABILITY SHALL BE LIMITED TO ACTUAL COMPENSATORY DAMAGES. EACH PARTY ACKNOWLEDGES THAT IT HAS HAD A FULL OPPORTUNITY TO CONSULT WITH COUNSEL CONCERNING THIS WAIVER, AND THAT THIS WAIVER IS INFORMED, VOLUNTARY, INTENTIONAL, AND NOT THE RESULT OF UNEQUAL BARGAINING POWER.

As with contractual time limitations, jurisdictions vary in their enforcement of these types of clauses. Some jurisdictions will rigorously enforce them.<sup>95</sup> Some jurisdictions also perform an

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Act). In *Wineman*, the court noted that claims with public policy implications, such as employee's statutory enforcement rights, that may affect individuals beyond the parties to a particular lawsuit should not be capable of restriction by contract. *Id.* at 821.

<sup>92</sup> See, e.g., *Aviall Servs., Inc. v. Cooper Indus., LLC*, 694 F. Supp. 2d 567, 576 (N.D. Tex. 2010) (a cause of action accrues when “the wrongful act effects an injury, regardless of when the plaintiff learned of such injury.”); *Doe v. Linam*, 225 F. Supp. 2d 731, 734 (S.D. Tex. 2002) (“In Texas, a plaintiff's cause of action accrues and the applicable limitations period starts to run when a wrongful act causes some legal injury, even if the fact of injury is not discovered until later, and even if all resulting damages have not yet occurred.”) (internal quotations omitted).

<sup>93</sup> See, e.g., *Shovah v. Mercure*, 44 F. Supp. 3d 504, 510–11 (D. Vt. 2014) (sexual abuse victims claims accrued at the time of the sexual action causing the injury, not years later when the plaintiffs connected the conduct to an injury); *Singleton v. Clash*, 951 F. Supp. 2d 578, 587 (S.D.N.Y. 2013) (same).

<sup>94</sup> *Belinda K. v. County of Alameda*, No. 10-CV-05797, 2011 WL 2690356, at \*6 (N.D. Cal. July 8, 2011) (“An injury from an illegal search and seizure accrues when the act occurs.”); Conn Gen. Stat. § 52-585 (three year statute of repose on ‘injury to person or property caused by negligence, misconduct or malpractice,’ timed from the date of the act or omission complained of,” regardless of when the effects are discovered or felt).

<sup>95</sup> *Int'l Marine Holdings, Inc. v. Stauff*, 44 Conn. App. 664, 676, 691 A.2d 1117, 1124 (Conn. App. 1997) (If the language of the agreement discloses that the parties intended to limit the remedies to those stated, the agreement will be enforced and the party will be limited to the exclusive remedies outlined in the agreement.”) (internal quotation marks omitted); *Michelin N. Am., Inc. v. Inter City Tire & Auto Ctr., Inc.*, Nos. 6:13-1067-HMH, 6:13-2752-HMH, and 6:14-1254, Bus. Franchise Guide (CCH) ¶ 15,428 (D. S.C. Dec. 22, 2014) (rejecting an argument that a South Carolina wrongful termination statute superseded a contractual bar to damage claims resulting solely from agreement termination and holding that South Carolina law enforced limitation of damages clause unless they are unconscionable or violate public policy, neither of which was found to exist); *Philips-Van Heusen Corp. v. Mitsui O.S.K. Lines Ltd.*, No. CV-00-0665, 2002 WL 32348263, at \*13 (M.D. Pa. Aug. 14, 2002) (“under Pennsylvania contract law, parties of equal bargaining power may contractually limit their liability for special, indirect, or consequential damages); see also Green-Kelly et al., *supra* note 11, at 40–43.

unconscionability analysis based on public policy to determine if a contractual damages limitation is enforceable.<sup>96</sup>

Recent franchise cases demonstrate the effectiveness and enforceability of contractual waivers. In *Yumilicious Franchise, LLC v. Barrie*,<sup>97</sup> the franchisee (individual guarantors) pursued consequential and punitive damages following the failure of its franchise locations based on fraudulent inducement, among other claims. The franchise agreement contained a “waiver of punitive damages” provision that also limited each party to the “recovery of any actual damages it sustains.” The trial court enforced the waiver and granted summary judgment to the franchisor. The Fifth Circuit affirmed.<sup>98</sup> The court also rejected a related negligent misrepresentation claim based on the economic loss rule.<sup>99</sup>

The franchisee in *Coraud LLC v Kidville Franchise Co., LLC*<sup>100</sup> sought punitive damages in the face of a contractual waiver asserting that the waiver was ineffective under the New York State Franchise Sales Act.<sup>101</sup> After analyzing Section 687(5) of New York State Franchise Sales Act, the court found that although the Act contemplated actual damages and rescission, it did not provide for punitive damages. Thus, “[f]rom this, the Court conclude[d] that the NYSFA does not permit recovery of punitive and exemplary damages and that, as a result, enforcement of the contractual waiver of such damages does not offend Section 687(5).”<sup>102</sup>

#### **a. Limiting the Amount of Damages Claimed**

Franchisors also often seek to cap the amount of damages, regardless of type or source. A limiting clause may state, for example:

ACTUAL COMPENSATORY DAMAGES REFERENCED [IN THE DAMAGE TYPE LIMITATION PROVISION] SHALL NOT EXCEED THE GREATER OF (1) \$100,000.00 OR (2) AT YOUR SOLE OPTION, ALL AMOUNTS PAID TO US FOR FRANCHISE FEES AND ROYALTIES FOR THIS AGREEMENT FOR UP TO THREE YEARS PRECEDING THE DATE OF ANY AWARD HEREIN.

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<sup>96</sup> See *Captain Bounce, Inc. v. Bus. Fin. Servs., Inc.*, No.11-CV-858, 2012 WL 928412 (S.D. Cal. Mar. 19, 2012) (“limitation on punitive damages was not unconscionable where the plaintiff had failed to assert a claim for which punitive damages were recoverable.”); *Irwin Seating Co. v. Int’l Bus. Mach. Corp.*, No. 1:04-CV-568, 2005 WL 1475390, at \*14 (W.D. Mich. June 22, 2005) (“Colorado courts will enforce a clause limiting damages unless the clause is unconscionable.”); *Trent Partners & Assocs., Inc. v. Digital Equip. Corp.*, 120 F. Supp. 2d 84, n. 19 (D. Mass. 1999) (“damage limitation clauses are enforceable unless they are unconscionable or against public policy.”).

<sup>97</sup> No. 3:13-CV-4841-L, 2015 U.S. Dist. LEXIS 53144 (N.D. Tex. Apr. 23, 2015), *aff’d*, United States Court of Appeals, Fifth Circuit No. 15-10508, 2016 WL 1375871 (5th Cir. Apr. 6, 2016).

<sup>98</sup> *Id.*

<sup>99</sup> *Id.* “In Texas, the economic loss rule ‘generally precludes recovery in tort for economic losses resulting from the failure of a party to perform under a contract.’ *Lamar Homes, Inc. v. Mid-Continent Cas. Co.*, No. 05-0832, 242 S.W.3d 1, 12 (Tex. 2007). Section IV further discusses the rule.

<sup>100</sup> 109 F. Supp. 3d 615 (S.D.N.Y. June 12, 2015).

<sup>101</sup> N.Y. Gen. Bus. Law § 687.

<sup>102</sup> *Coraud*, 109 F. Supp. 3d at 625.

Again, enforcement will vary by jurisdiction. For example, one court enforced a clause in a fire alarm system installation and service agreement limiting damages to the \$250 installation cost after fire destroyed the property.<sup>103</sup> Another court held that a damage limitation provision did not bar a claim for fire damages stemming from the alleged negligent installation of smoke detectors.<sup>104</sup> In that case, an Ohio court determined that such caps on damages can act as a penalty and are unrelated to the anticipated damages that might stem from the parties' contract.<sup>105</sup> In many jurisdictions, various formulations of "reasonableness" or "unconscionability" will apply.<sup>106</sup> Courts will also often refuse to enforce damage caps for particular types of statutory claims.<sup>107</sup> For example, an Indiana federal district court found that a limitation of remedies clause would not bar a price discrimination claim under the Indiana Deceptive Franchise Practices Act.<sup>108</sup> The case has a lengthy and complex procedural history but the court refused to enforce the limitation because the discriminatory conduct was intentional and the provision at issue did not specifically supplant the dealer's statutory rights.<sup>109</sup>

### **G. Issues of Mutuality and Competing Provisions**

In some jurisdictions, issues of "lack of mutuality" may hinder enforcement of claim limitations. Though unequal bargaining power is a frequent reality some courts are reluctant to allow well-positioned parties to contract so as to slant dispute resolution or damage limitation provisions too far in their favor. In *Armendariz v. Found. Health Psychcare Servs., Inc.*,<sup>110</sup> the Supreme Court of California deemed a contract provision, including a requirement to arbitrate and a damage limitation clause, unconscionable for lack of mutuality. The damages provision limited only one party's damages in the event of a dispute and allowed the better-positioned party to opt out of arbitration at its choice, whereas the weaker bargaining party was compelled to resolve dispute by arbitration.<sup>111</sup> The court determined that the lack of mutuality in substantive contract terms was so pervasive that it could not simply strike unconscionable

<sup>103</sup> *U.S. Fid. & Guar. Co. v. Sonitrol Servs. Corp.*, CV-93-0134267S0, 1996 WL 456327 (Conn. Super. Ct. July 29, 1996).

<sup>104</sup> *Braden v. Honeywell, Inc.*, 8 F. Supp. 2d 724 (S.D. Ohio 1998).

<sup>105</sup> *Id.* at 728–29; see also *Jacada (Europe), Ltd. v. Int'l Mktg. Strategies, Inc.*, 401 F.3d 701 (6th Cir. 2005) (finding no "manifest disregard of law" where arbitrator refused to enforce damage limitation), *abrogated for other reasons by Hall St. Associates, L.L.C. v. Mattel, Inc.*, 552 U.S. 576 (2008).

<sup>106</sup> See, e.g., *Galaxy Prod. & Servs., Inc. v. AMI Entm't Network, Inc.*, Civ. Action No. 12-6963, 2015 WL 4630058, at \*3 (E.D. Pa. Aug. 4, 2015) ("If the limitation is reasonable and not so drastic as to remove the incentive to perform with due care, Pennsylvania courts uphold the limitation"); *Hoang v. Amazon.com, Inc.*, No. C11-1709-MJP, 2013 WL 11319007, at \*5 (W.D. Wash. Mar. 18, 2013); *Michelin N. Am., Inc. v. Inter City Tire & Auto Ctr., Inc.*, Nos. 6:13-1067-HMH, 6:13-2752-HMH, and 6:14-1254, Bus. Franchise Guide (CCH) ¶ 15,428 (D. S.C. Dec. 22, 2014) (holding that South Carolina law enforced damage limitation clauses unless they are unconscionable or violate public policy).

<sup>107</sup> See, e.g., *Milgard Tempering, Inc. v. Selas Corp. Am.*, 902 F.2d 703, 708–09 (9th Cir. 1990) (concluding that a contractual damages cap was unenforceable where a party's failure was not part of the bargained for allocation of risk under a limited repair clause pursuant to U.C.C. 2-719(2)).

<sup>108</sup> *Andy Mohr Truck Ctr., Inc. v. Volvo Trucks N. Am.* No. 1:12-cv-448-WTL-DKL, 2015 WL 2124994 (S.D. Ind. May 6, 2015).

<sup>109</sup> *Id.* at \*4.

<sup>110</sup> 24 Cal. 4th 83, 115-20, 6 P.3d 669, 691–94 (Cal. 2000).

<sup>111</sup> See *id.*

clauses and compel arbitration.<sup>112</sup> Including non-mutual provisions could risk a finding that an entire contract is void. When drafting, franchisors may want to ensure that both parties are bound by any limitations. It is also important to make sure that any limitation paragraphs coordinate and do not conflict with other provisions, such as prevailing party attorney fee provisions and other provisions establishing liability for particular acts or breaches. Including a severability clause may also help preserve non-offending contract provisions.

## **H. Consequential Damages**

Expectation or benefit of the bargain damages are often referred to as “direct” damages.<sup>113</sup> Consequential damages are damages suffered by a non-breaching party that are indirect but are foreseeably caused by another party’s breach.<sup>114</sup> “The difference between direct and consequential damages depend[s] on whether the damages represent (1) a loss in value of the other party’s performance, in which case the damages are direct, or (2) collateral losses following the breach, in which case the damages are consequential.”<sup>115</sup> Lost profits may be recovered as either or both direct and consequential damages.<sup>116</sup> Consequential damages are recoverable only when the losses incurred by the non-breaching party are foreseeable. However, courts have taken different approaches to determining what damages are ‘foreseeable’ to the parties. The Restatement (Second) of Contracts § 351 states that losses are foreseeable where damages result from: (1) the ‘ordinary course of events’ or (2) special circumstances of which a breaching party had reason to know.<sup>117</sup> In applying the Restatement, some courts have determined that foreseeable damages include both damages that the breaching party knew or should have known could occur.<sup>118</sup> Other courts have determined that when there is no evidence of actual knowledge at the time of contracting regarding the loss claimed as consequential damages, that loss is not foreseeable.<sup>119</sup> As noted above, in Section II.F., parties often seek to limit the availability of consequential damages contractually. This

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<sup>112</sup> See *id.*

<sup>113</sup> See *BCC Merchant Solutions, Inc. v. Jet Pay, LLC*, 129 F. Supp. 3d 440 (N.D. Tex. 2015) (holding that lost profits constitute “direct damages” where a buyer’s expectation to recover the cost of the purchased goods, minus the contract price, was expressly provided in the contract); *Carolee, LLC v. eFashion Solutions, LLC*, No. 2:12-cv-02630-WHW, 2013 WL 5574594, at \*6 (D. N.J. Oct. 9, 2013); Restatement (Second) of Contracts § 347(a) (“the injured party has a right to damages based on his expectation interest as measure by (a) the loss in the value to him of the other party’s performance caused by its failure or deficiency”).

<sup>114</sup> See *Carolee, LLC*, 2013 WL 5574594 at \*6.

<sup>115</sup> *Atl. City Assocs., LLC v. Carter & Burgess Consultants, Inc.*, 453 F. App’x 174, 179 (3d Cir. 2011).

<sup>116</sup> *Penncro Assocs., Inc. v. Sprint Spectrum, L.P.*, 499 F.3d 1151, 1156 (10th Cir. 2007).

<sup>117</sup> Restatement (Second) of Contracts § 351 (1981).

<sup>118</sup> See, e.g., *O’Toole v. Northrop Grumman Corp.*, 305 F.3d 1222, 1226 (10th Cir. 2002) (holding that even when there is no evidence of actual knowledge that the non-breaching party would suffer particular damages, such losses are still recoverable under New York law as consequential damages if the breaching party should have known about them).

<sup>119</sup> See, e.g., *Marine Rubber Intern. v. Environ. Mgmt. Group, Inc.*, 324 F. Supp. 2d 32, 35–36 (D. Maine 2004) (holding that lost profits were not foreseeable when the parties never discussed the potential loss at the time of contracting).

effort often leads to disputes about whether lost profits in a particular case are “direct” or “consequential” damages.<sup>120</sup>

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<sup>120</sup> See *Pennco Assocs., Inc. v. Sprint Spectrum, L.P.*, 499 F.3d 1151, 1155–56 (10th Cir. 2007) (holding that contract provision prohibiting recovery of lost profits as a component of consequential damages did not restrict party from seeking recovery of lost profits as *direct damages*); but see *Optimal Interiors, LLC v. HON Co.*, 774 F. Supp. 2d 993, 1012–13 (S.D. Iowa 2011) (holding that contract restriction on consequential damages eliminated possibility of recovery for lost profits because lost profits are regarded as consequential damages under Iowa law).

## **I. Prevailing Party Damages**

Franchise agreements often contain “prevailing party” clauses that require the losing party to pay the winner’s costs and attorney fees. A typical clause might say: “If any Party brings litigation or other proceedings to enforce this Agreement, or for breach of this Agreement, the prevailing Party shall be awarded from the other Party its reasonable costs, disbursements, arbitration filing and administrative fees, arbitrators’ fees, and attorney fees incurred, including, but not limited to, pre-suit or pre-arbitration costs and attorney fees related to the breach and/or efforts to enforce.”

When mutual, these clauses are generally enforceable.<sup>121</sup> However, some jurisdictions have determined that a party that successfully moves to dismiss based on grounds not relating to the merits of the case (e.g., jurisdiction, venue) is not entitled to attorney fees as a “prevailing party” unless the “prevailing party” clause specifically provides an “incontrovertible prevailing party provision for enforcement of any aspect of the agreement.”<sup>122</sup> Additionally, references in an agreement to the recovery of “costs” and “expenses” do not necessarily require courts to award attorney fees and all “prevailing party” provisions therefore should specifically include the recovery of attorney fees.<sup>123</sup> Courts may also limit or prohibit attorney fees in cases where a party prevails on only non-contractual claims<sup>124</sup> but generally a party will be deemed the “prevailing party” and recover proportionally reduced attorney fees even when some of its claims fail, so long as the successful claim is based on a breach of the contract in question.<sup>125</sup>

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<sup>121</sup> Some jurisdictions will impose mutuality for prevailing party provisions even if they are drafted unilaterally. See, e.g., Cal. Civil Code § 1717; Fla. Stat. ch. § 57.105.

<sup>122</sup> *Tradex Global Master Fund SPC Ltd. v. Palm Beach Capital Mgmt., LLC*, No. 09-21622-CIV, 2010 WL 3323750, \*2–3 (S.D. Fla. July 13, 2010); see also *Buckhannon Bd. & Care Home, Inc. v. W. Virginia Dep’t of Health & Human Res.*, 532 U.S. 598, 603–09 (2001) (defining ‘prevailing party’ with respect to a statutory fee-shifting provision under the Fair Housing Amendments Act); *Am. Guard Servs., Inc. v. Mgmt. Info. Tech. Corp.*, No. CV-11-3525, 2011 WL 2940407, at \*4 (C.D. Cal. July 21, 2011) (relying on the Supreme Court’s interpretation of “prevailing party” in *Buckhannon* while performing objective interpretation of “prevailing party” in contract language).

<sup>123</sup> See *Sammi Line Co., Ltd. v. Altamar Navegacion S.A.*, 605 F. Supp. 72, 73 (S.D.N.Y. 1985) (noting that ‘costs’ and ‘expenses’ “are not generally used to encompass attorneys’ fees”).

<sup>124</sup> See *625 3rd Street Assocs., L.P. v. Bd. of Nat. Credit Union Admin.*, No. C-09-00564, 2010 WL 5185498, at \*2–3 (N.D. Cal. Dec. 7, 2010) (holding that a party was restricted from collecting attorney fees under ‘prevailing party’ clause where it failed on its breach of contract claims but succeeded on a related fraud claim that was only partially based upon the underlying contract).

<sup>125</sup> See *First Commodity Traders, Inc. v. Heinold Commodities, Inc.*, 766 F.2d 1007, 1015 (7th Cir. 1985) (upholding proportionally reduced attorney fee award where party was successful on only one of seven claims); but see *Telewizja Polska USA, Inc. v. Echostar Satellite Corp.*, No. 02-C-3293, 2007 WL 3232498, at \*4 (N.D. Ill. Oct. 30, 2007) (enforcing a “prevailing party” provision and awarding full attorney fees where the plaintiff succeeded solely on its breach of contract claim and the remaining four claims were ‘in the alternative’). Courts exercise a great degree of discretion in determining an appropriate recovery of attorney fees when a party prevails on some claims but not others. See *Telewizja Polska*, 2007 WL 3232498 at \*4 (“Ultimately, this Court has wide discretion to determine whether, and to what extent, to award fees and costs.”).

## J. Rescission and Restitution

Money damages are called “legal remedies,” while others are called “equitable remedies.” This distinction stems from procedural and venue separation in federal and state courts for courts sitting in equity as opposed to those sitting in law.<sup>126</sup>

Most jurisdictions that had separate courts for plaintiffs seeking legal or equitable remedies have since abolished them, but the distinctions relating to remedies have remained in various forms in many jurisdictions.<sup>127</sup> As a recent law review article explains:

The equitable remedies still used regularly in the United States are the injunction, specific performance, reformation, quiet title, and a cluster of restitutionary remedies: accounting for profits, constructive trust, equitable lien, subrogation, and equitable rescission. The legal remedies in regular use are damages, mandamus, habeas, replevin, ejectment, and certain restitutionary remedies. There are also more obscure remedies that are legal or equitable. One other remedy, the declaratory judgment, though not easy to classify, should typically be seen as a non-equitable remedy.<sup>128</sup>

From a contract perspective, the most common equitable remedies in franchise cases are injunctive relief, which is beyond the scope of this paper,<sup>129</sup> and rescission.

Rescission is a common law and sometimes statutory remedy for a franchisee who has claims against a franchisor, regrets entering into a franchise agreement, and would like to undo the effects of contracting. “Rescission ‘means undoing an exchange, with each side returning what it has received.’ The exchange at issue might have been made under a voidable contract or under a contract that has been breached.”<sup>130</sup> It “is the unmaking of a contract. It is a renouncement of the contract and any property obtained pursuant to the contract, and places the parties, as nearly as possible, in the same situation as existed just prior to the execution of

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<sup>126</sup> See, e.g., *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 327 U.S. 308, 318, 119 S. Ct. 1961 (1999) (“The Judiciary Act of 1789 conferred on the federal courts jurisdiction over ‘all suits ... in equity.’ § 11, 1 Stat. 78. We have long held that ‘[t]he ‘jurisdiction’ thus conferred ... is an authority to administer in equity suits the principles of the system of judicial remedies which had been devised and was being administered by the English Court of Chancery at the time of the separation of the two countries.”) (citations and internal quotations omitted); *Lyons P’ship, L.P. v. Morris Costumes, Inc.*, 243 F.3d 789, 798 (4th Cir. 2001) (noting the merger of law and equity in federal courts, at least for procedural purposes).

<sup>127</sup> Samuel L. Bray, *The System of Equitable Remedies*, 63 UCLA L. Rev. 530, 538 (March 2016).

<sup>128</sup> *Id.* at 542.

<sup>129</sup> For helpful discussions of injunctive relief in franchise cases, see Arthur M. Kaufmann, Peter Silverman and Christina Fugate, *Stop the Bleeding: Affirmative Injunctive Relief and Other Non-traditional Remedies*, ABA 38th Annual Forum on Franchising, W3 (2015); C. Griffith Towle and Justin M. Klein, *Fundamentals 201: Stop That Right Now – Preparing for, and Winning, Injunctions*, ABA 33rd Annual Forum on Franchising, W20 (2010). For a discussion of specific performance, see Fugate et al., *supra* note 2.

<sup>130</sup> Bray, *supra* note 127, at 538 (quoting Ward Farnsworth, *Restitution: Civil Liability for Unjust Enrichment* 121 (2014) and citing Restatement (Third) of Restitution & Unjust Enrichment § 54 (Am. L. Inst. 2011)); Farnsworth at 133–34.



the contract. A condition precedent to rescission is the offer to restore the other party to its former condition as nearly as possible."<sup>131</sup>

Franchisees generally request "restitution" as monetary relief in connection with their rescission claim. Restitution is "a restoration of the status quo and is the amount [that] would put plaintiff in as good a position as he would have been if no contract had been made."<sup>132</sup> In quantifying their restitution claims, franchisees sometimes misguidedly simply add up what they paid to the franchisor and other expenses and related losses. They often ignore that the franchisees' claims must be offset by the benefits they received from the contract, which in some cases may exceed the franchisees' recoverable costs.<sup>133</sup> For example, franchisors may receive an offset to franchisees' claimed restitution of profits, including all gross income derived, from operating the franchise.<sup>134</sup> In most cases, however, the franchisee is the party awarded restitution calculated by determining the amounts paid to a franchisor, including advertising fees, royalty fees, and amounts required to be paid under the franchise agreement (e.g., required purchases of supplies/equipment and required payments to third parties).<sup>135</sup>

Similarly, a franchisee may also be able to seek "reliance" damages to reimburse it for the amounts invested in the business or otherwise spent in furtherance of the enterprise. A plaintiff generally cannot seek both reliance damages and expectation damages, because that could overcompensate the plaintiff.<sup>136</sup> In some cases, judges have noted that damages could be categorized as either restitution or reliance damages.<sup>137</sup> Courts have also held that reliance damages are an alternative to recovery for lost profits, not an additional measure of damages.<sup>138</sup>

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<sup>131</sup> *Paul Revere Life Ins. Co. v. Pastena*, 52 Conn. App. 318, 325, 725 A.2d 996, 1000 (Conn. App. Ct. 1999) (internal quotation marks omitted).

<sup>132</sup> *Marwell Louisiana, Inc. v. Harris*, Civ. A. No. 95-0041-C, 1996 WL 335380, at \*5 (W.D. Va. May 29, 1996); see also Black's Law Dictionary 1313 (6th ed. 1990) ("an equitable remedy under which a person is restored to his or her original position prior to loss or injury, or placed in the position he or she would have been, had the breach not occurred.").

<sup>133</sup> See *Ambassador Hotel Co. v. Wei-Chuan Inv.*, 189 F.3d 1017, 1031 (9th Cir. 1999) ("Rescission reverses the fraudulent transaction and returns the parties to the position they occupied prior to the fraud. It restores the status quo ante. . . . the plaintiff returns to the defendant the subject of the transaction, plus any other benefit received under the contract, and the defendant returns to the plaintiff the consideration furnished, plus interest. If true rescission is no longer possible (perhaps because the plaintiff no longer owns the subject of the sale), the court may order its monetary equivalent. This remedy entitles the plaintiff to the return of the consideration paid *less any value received on the investment.*") (internal citations omitted) (emphasis added); *Dorsey v. Mancuso*, 23 Conn. App. 629, 635, 583 A.2d 646, 650 (Conn. App. 1990).

<sup>134</sup> See *Dollar Sys., Inc. v. Avcar Leasing Sys., Inc.*, 890 F.2d 165 (9th Cir. 1989) (suggesting that trial court's refusal to award profits earned by franchisee to franchisor in restitution award needed to be revisited because it rewarded, rather than punished, the franchisee for its misconduct under the franchise agreement).

<sup>135</sup> See *Little Caesar Enters., Inc. v. OPPCO, LLC*, 219 F.3d 547, 553-54 (6th Cir. 2000); *In re DeRosa*, 98 B.R. 644, (D. R.I. 1989) ("Restitution damages consist of: (1)... franchise fee; (2)... equipment...; (3)... 'improvements and operation of the business'").

<sup>136</sup> Green-Kelly et al., *supra* note 11, at 16-18.

<sup>137</sup> See *DeRosa*, 98 B.R. at 649. In *DeRosa*, the court avoided the issue of counting the damages twice by enumerating what damages amounts were due for each particular loss alleged by the franchisee. *Id.* at 649 ("\$8,542.24 spent on improvements and operation of the business (these might also fall into the category of reliance damages.)").

<sup>138</sup> See *Nat'l Controls Corp. v. Nat'l Semiconductor Corp.*, 833 F.2d 491, 499 (3d Cir. 1987).

Reliance damages were previously addressed in the Restatement (First) of Contracts section on measure of restitution damages<sup>139</sup> but have since been removed from the Restatement's Measure of Damages in General section, which now focuses on calculation of expectation damages.<sup>140</sup> "Recoupment" may also be available for relationships that are terminable at-will to allow a plaintiff to recover sunk costs in certain circumstances.<sup>141</sup>

### III. STATUTORY DAMAGES

Franchising is, of course, a regulated industry.<sup>142</sup> Many states have enacted disclosure, relationship, and business opportunity laws protecting franchisees and providing causes of action and remedies that might not otherwise be available. In addition, some state "Little FTC Acts" may also provide a vehicle for damages and other relief based on violations of federal law for which there is no federal private right of action.

#### A. Disclosure and Registration Laws

Federally, the FTC Rule<sup>143</sup> requires franchisors, among other things, to provide an FDD to "prospective franchisees"<sup>144</sup> at least fourteen days before they sign the agreement or pay money to the franchisor or its affiliate.<sup>145</sup> The information in the FDD must be accurate and strictly comply with the FTC Rule's regulatory requirements.<sup>146</sup> It is well-established that there is no private right of action for violation of the FTC Rule.<sup>147</sup> State disclosure laws are another matter.

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<sup>139</sup> Restatement (First) of Contracts § 347 ("For the total breach of contract, the injured party can get judgment for the reasonable value of a performance rendered by him... if the performance so rendered was... (B) rendered in reliance upon the other party's promise.").

<sup>140</sup> Restatement (Second) of Contracts § 347.

<sup>141</sup> Green-Kelly et al., *supra* note 11, at 36–37.

<sup>142</sup> See generally Leonard D. Vines, Gina D. Bishop and Rupert M. Barkoff, *Damage Control for Violations of Registration and Disclosure Obligations*, 24 Franchise L.J. 191 (Winter 2005).

<sup>143</sup> 16 C.F.R. § 436.1, *et seq.*

<sup>144</sup> The FTC Rule defines "prospective franchisee" as "any person (including any agent, representative, or employee) who approaches or is approached by a franchise seller to discuss the possible establishment of a franchise relationship.

<sup>145</sup> 16 C.F.R. § 436.2(a).

<sup>146</sup> See *Hanley v. Doctors Exp. Franchising, LLC*, No. ELH-12-795, 2013 WL 690521, at \*2 (D. Md. Feb. 25, 2013) ("A 'Franchise Disclosure Document,' or 'FDD,' is a document containing certain specified disclosure that a franchisor must furnish to a prospective franchisee... under regulations issued by the Federal Trade Commission ('FTC')").

<sup>147</sup> See, e.g., *Yumilicious Franchise, LLC v. Barrie*, Civ. Action No. 3:13-CV-4841-L, 2015 WL 2359504 (N.D. Tex. May 18, 2015), *aff'd*, No. 15-10508, 2016 WL 1375871 (5th Cir. Apr. 6, 2016) (no private right of action is available to franchisee for franchisor's failure to furnish required information under Franchise Rule); *A Love of Food I, LLC v. Maoz Vegetarian USA, Inc.*, 70 F. Supp. 3d 376, 382 (D. D.C. 2014) (same); *Robinson v. Wingate Inns Int'l, Inc.*, Civ. Action No. 13-cv-2468-CCC, 2013 WL 6860723, at \*2 (D. N.J. Dec. 20, 2013) ("It is well-settled that there is no private cause of action for violation of the FTC franchise disclosure rules."); *Hidden Values, Inc. v. Wade*, Civ. Action No. 3:11-CV-1917-L, 2012 WL 1836087, at \*7 (N.D. Tex. 2012) (Lindsay, J.) (collecting cases); *Vino 100, LLC v. Smoke on the Water, LLC*, 864 F. Supp. 2d 269, 281 (E.D. Pa. 2012) (same).

Fifteen states currently have their own laws requiring franchisors doing business in those states to register with the state and provide pre-sale disclosures.<sup>148</sup> Available relief for violation is wide-ranging and can include rescission, actual, and multiple damages, as well as costs and attorney fees.<sup>149</sup>

## **B. Relationship Laws**

Although state registration and disclosure laws cover pre-sale activities, some states (even those without registration and disclosure laws) have “relationship laws” that cover various aspects of the franchise relationship, such as termination and renewal.<sup>150</sup> Special industries are sometimes covered by industry-specific protections.<sup>151</sup> Relief may include actual and punitive damages, cost, attorney fees, and other remedies.<sup>152</sup>

## **C. Business Opportunity Laws**

There is a federal Business Opportunity Rule.<sup>153</sup> The FTC has separated its Business Opportunity Rule from the FTC Rule relating to the FDD discussed above.<sup>154</sup> However, like the FTC Rule, there is no independent private right of action for violation of the federal Business Opportunity Rule.<sup>155</sup>

Again, analogous state law is more plaintiff-friendly. Twenty-six states regulate business opportunities.<sup>156</sup> A recent Forum presentation explained:

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<sup>148</sup> The fifteen states are California, Hawaii, Illinois, Indiana, Maryland, Michigan, Minnesota, New York, North Dakota, Wisconsin, Rhode Island, South Dakota, Virginia, Washington, and Oregon. Oregon's disclosure requirement differs from the fourteen other states with disclosure laws in that Oregon has no franchise registration requirement. Or. Admin. R. 441-325-0020; see also Keith Kanouse, Dawn Newton and Michelle Webster, *Fundamentals 201: Drafting the Six Most Challenging Items in the FDD*, ABA 38th Annual Forum on Franchising, W16 at 2 (2015); Green-Kelly et al., *supra* note 11, at 31–32; Ellen R. Lokker and Dennis R. LaFiura, *Damages in Franchise Cases: Contract, Tort, and Statutory*, ABA 25th Annual Forum on Franchising, W7 at 24–26 (2002).

<sup>149</sup> Joblove et al., *supra* note 2, at 15–20; Green-Kelly et al., *supra* note 11, at 31–32; Lokker et al., *supra* note 148, at 24–26.

<sup>150</sup> Susan Grueneberg and Jonathan Solish, *Franchising 101: Key Issues in the Law of Franchising*, 19 Am. Bar Assoc. Bus. L. Today (March/April 2010); Lokker et al., *supra* note 148, at 27–29.

<sup>151</sup> Green-Kelly et al., *supra* note 11, at 33–34.

<sup>152</sup> Karen Marchiano, Glenn Plattner and Leonard Vines, *Roadmap for the Default and Termination Process*, ABA 35th Annual Forum on Franchising, W13 at 11–18 (2012); Green-Kelly et al., *supra* note 11, at 32–33; Lokker et al., *supra* note 148, at 27–29.

<sup>153</sup> 16 CFR Part 437.

<sup>154</sup> See Beata Krakus and Alexander Tuneski, *Caught in the Web of Federal and State Business Opportunity Laws: Managing and Avoiding the Entanglement of Regulations*, ABA 36th Annual Forum on Franchising, W7 at 1–2 (2013); Keith J. Kanouse, *FTC's New Business Opportunity Rule: Reduced Disclosure But Increased Coverage*, 86 Fla. Bar J. 4 (April 2012).

<sup>155</sup> See Krakus et al., *supra* note 154, at 1–2; Kanouse, *supra* note 154.

<sup>156</sup> Krakus et al., *supra* note 154, at 1–2.

A “business opportunity” is defined differently in federal and state laws and regulations, but the definition under the Indiana business opportunity law fairly well represents how the concept is defined in most state laws:

“Business opportunity means an investment that:

- (1) Involves the sale or lease or offer to sell or lease any goods or services to an investor that are to be used by the investor in beginning or operating a business;
- (2) Involves an initial payment by the investor of more than five hundred dollars (\$500) and an initial cash payment of less than fifty thousand dollars (\$50,000); and
- (3) Involves a solicitation of investors in which the seller represents that:
  - (A) the investor may or will earn an amount in excess of the initial investment;
  - (B) a market exists for any goods to be made or services to be rendered by the investor;
  - (C) the seller may buy from the investor any goods to be made or services to be rendered by the investor;
  - (D) the seller or a person referred by the seller to the investor may or will sell, lease, or distribute the goods made or services rendered by the investor; or
  - (E) the seller may or will pay to the investor the difference between the initial payment and the investor's earnings from the investment.<sup>157</sup>

Although this definition could apply to many franchise and franchise-like relationships, these state statutes generally provide exemptions for businesses involving federally registered trademarks.<sup>158</sup>

Remedies available for state business opportunity law plaintiffs can include rescission, actual and multiple damages as well as costs and attorney fees.<sup>159</sup> At least one state provides for punitive damages awards as well.<sup>160</sup>

#### **D. Little FTC Acts**

As noted above, there is no private right of action for violation of the FTC Rule or the FTC Business Opportunity Rule. Accordingly, parties seeking to sue based on violation of

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<sup>157</sup> *Id.* at 1–2. Appendix A to this paper provides a helpful “complete list of state business opportunity statutes, including statutory references.” *Id.* at 2.

<sup>158</sup> *Id.* at 2.

<sup>159</sup> *Id.* at 27.

<sup>160</sup> See, e.g., Cal. Civ. Code § 1812.218.

these Rules must shoehorn their claim into another law. If false disclosures are provided, then the plaintiff may assert a claim for fraud in the inducement or other related common law claim, irrespective of the FTC Rule.<sup>161</sup> The most common vehicle for asserting an FTC Rule violation is through an applicable state “Little FTC Act” by claiming that FTC Rule violation is the “predicate” for Little FTC Act violation.<sup>162</sup> Plaintiffs may further seek to rescind or otherwise avoid their contractual obligations by arguing that the agreement is “illegal” because of an alleged FTC Rule violation.<sup>163</sup> Franchisees also base Little FTC Act claims on alleged unfair or deceptive practices unrelated to violation of the FTC Franchise Rule.<sup>164</sup>

State Little FTC Acts vary widely.<sup>165</sup> Some protect only consumers or apply to households or other goods and services and do not apply to the franchise relationship or alleged FTC Rule violations.<sup>166</sup> Others go so far as to conclude that an FTC Rule violation is a *per se* violation of the Little FTC Act.<sup>167</sup> Because of their often remedial nature,<sup>168</sup> Little FTC

<sup>161</sup> See *A Love of Food I, LLC v. Maoz Vegetarian USA, Inc.*, 70 F. Supp. 3d 376, 414–15 (D. D.C. 2014) (permitting a common law claim of fraud in the inducement where the plaintiff argued that the defendant “provided false estimated start-up expenses in the offering prospectus”); *Bans Pasta, LC v. Mirko Franchising, LLC*, No. 7:13-cv-00360-JCT, 2014 WL 637762, at \*2, \*11 (W.D. Va. Feb. 12, 2014) (allowing claims of fraud in the inducement and misrepresentation where plaintiff claims defendant misrepresented the financial strength of defendant’s franchises and provided a cost schedule that failed to include “several essential operating costs”).

<sup>162</sup> For a discussion of common predicates frequently argued pursuant to state Little FTC Acts, see Dennis LaFiura, Peter Lagarias and Victor Vital, *Comparison of the Trilogy: Common Law Fraud, Franchise Investment Laws, and Little FTC Laws Remedies for the Misrepresentations and Omissions in the offer and Sale of Franchises*, ABA 34th Annual Forum on Franchising, W24 at 10–14 (2011). Other commentators have noted that “[w]hile the [FTC Rule] does not provide for a private right of action, most states have implemented their own ‘Little FTC Acts’ or Deceptive Trade practice Acts, which generally mimic the FTC Rule, but importantly may provide for a private right of action.” John G. Parker and Angela M. Fifelski, *Claims Under Little FTC Acts*, ABA 28th Annual Forum on Franchising, W4 at 1 (2005).

<sup>163</sup> See, e.g., *Mercy Health Sys. of S.E. Penn. V. Metro. Partners Realty LLC*, No. Civ. A. 02-1015, 2002 WL 1774060, at \*2 (E.D. Pa. July 29, 2002) (dismissing for lack of federal question jurisdiction where plaintiff alleged “because defendants’ failure to make the disclosures required by the Franchise Rule is an illegal act contaminating the formation of the parties’ contract, [plaintiff] is suing for relief from the illegal contract.”).

<sup>164</sup> LaFiura et al., *supra* note 162; Altresha Q. Burchett-Williams, Robert M. Einhorn and Paula J. Morency, *Claims Under the “Little FTC Acts”: The High States of Risk and Reward*, ABA 33rd Annual Forum on Franchising, W6 (2010).

<sup>165</sup> See, e.g., Burchett-Williams et al., *supra* note 164, at 5–11.

<sup>166</sup> See *859 Boutique Fitness LLC v. Cyclebar Franchising, LLC*, No. 5:16-CV-018-KKC, 2016 WL 2599112, at \*3 (E.D. Ky. May 5, 2016) (Kentucky Consumer Protection Act “only provides a private cause of action for an individual ‘who purchases or leases goods or services primarily for personal, family or household purposes’”); *W. Coast Franchising Co. v. WCV Corp.*, 30 F. Supp. 2d 498, 500 (E.D. Pa. 1998) (franchises do not constitute ‘goods or services primarily for personal, family or household purposes’ under the Pennsylvania Unfair Trade Practice and Consumer Protection Law); see also *Family Wireless #1, LLC v. Automotive Techs., Inc.*, No. 15-CV-1310-JCH, 2016 WL 183475, n.17 (D. Conn. Jan. 14, 2016) (noting that neither the Pennsylvania Unfair Trade Practices and Consumer Protection Law nor the West Virginia Consumer Credit and Protection Act “apply to the sale of franchises, but only to the sale of goods or services”); see also *A.H. Meyers & Co. v. CAN Ins. Co.*, 88 F. App’x. 495, 500 (3d Cir. 2004) (“franchises are not covered by the [New Jersey] Consumer Fraud Act because they are businesses, not consumer goods or services.”); but cf. *Kavky v. Herbalife Int. Am.*, 359 N.J. Super. 497, 499, 820 A.2d 677, 678 (N.J. App. Div. 2003) (carving out a limited exception providing that the New Jersey Consumer Fraud Act does apply to franchises where the franchise is so insubstantial that it is offered to the general public in mass marketing).

<sup>167</sup> See LaFiura et al., *supra* note 162, at 8.

Acts can provide valuable and wide-ranging remedies, including actual, multiple, and punitive damages, and can allow for rescission, injunctions, and other relief.<sup>169</sup>

#### **E. Defend Trade Secrets Act of 2016**

The Defend Trade Secrets Act of 2016 (“DTSA”) was signed into law in May 2016 and provides a federal private cause of action to pursue parties that misappropriate trade secrets.<sup>170</sup> The DTSA is largely consistent with existing state trade secret laws but, importantly, allows litigants the power to pursue claims in both federal and state court. Remedies available include injunctive relief as well as damages for injuries from misappropriation and, in instances of willful or malicious misappropriation, exemplary damages double the actual damages or restitution available.<sup>171</sup> Reasonable attorney fees may also be awarded where a defendant’s misappropriation has been willful or malicious.<sup>172</sup>

#### **F. The Racketeer Influenced and Corrupt Organizations Act (RICO)**

RICO<sup>173</sup> violations can entitle a plaintiff to treble damages, attorney fees, costs, and other relief.<sup>174</sup>

#### **G. Lanham Act Monetary Damages – Holdover Franchisees**

When the franchise relationship has a contentious ending or franchisees find themselves in desperate circumstances, franchisees are often tempted to continue to use the franchisor’s trademark after termination or expiration of the franchise agreement. These so-called “holdover franchisees” take great risk when following this course of action, and this decision often leads to a Lanham Act (Trademark Act of 1946) lawsuit.<sup>175</sup> Although securing injunctive relief may be the most expedient Lanham Act violation remedy,<sup>176</sup> this paper focuses on monetary relief permitted under the Act in actions involving holdover franchisees.

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<sup>168</sup> See, e.g., Conn. Gen. Stat. § 42-110b(d) (“It is the intention of the legislature that this chapter be remedial and be so construed”); Idaho Code § 48-601 (“It is the intention of the legislature that [the Idaho Consumer Protection Act] be remedial and be so construed”).

<sup>169</sup> For a discussion of remedies available under Little FTC Acts, see Burchett-Williams, et al., *supra* note 164, at 18–20. Note, however, that defendants may be able to take advantage of prevailing party fee-shifting provisions. See, e.g., Fla Stat. § 501.2105(1); *Humane Soc. of Broward Cnty., Inc. v. Florida Humane Soc.*, 951 So. 2d 966, 969 (Fla. Dist. Ct. App. 2007) (finding that § 501.2105(1) allows for the “award [of] prevailing party attorney fees to both plaintiffs and defendants under the same standards”).

<sup>170</sup> 18 U.S.C. § 1836, *et seq.*

<sup>171</sup> *Id.*

<sup>172</sup> *Id.*

<sup>173</sup> 18 U.S.C. § 1962, *et seq.*

<sup>174</sup> 18 U.S.C. § 1964. For further discussion of RICO claims in the franchise context, see W. Michael Garner, *Current Status of Civil RICO and Franchising*, 6 Franchise L.J. 1 (1986); Michael J. Walter, *Civil RICO: An End to Franchise Fraud*, 2 Franchise L.J. 26 (1982).

<sup>175</sup> 15 U.S.C. § 1051, *et seq.*

<sup>176</sup> 15 U.S.C. § 1116; 15 U.S.C. § 1125(c).

15 U.S.C. § 1117(a) provides for the following monetary remedies “subject to the principles of equity”: (1) defendant’s profits, (2) any damages the plaintiff sustained (in some cases multiplied up to three times), and (3) the costs of the action.<sup>177</sup> A plaintiff may recover both defendant’s profits and damages so long as it will not result in a duplicate recovery. Prevailing parties may obtain an award of reasonable attorney fees only in “exceptional cases.”<sup>178</sup>

When researching and briefing Lanham Act claims in franchise cases, counsel should be aware that courts often treat “holdover franchisees” differently from third party infringers when determining whether infringement was “willful” because a former franchisee would have “[f]ull knowledge of the proprietary nature of a mark and the infringement and misuse of the mark.”<sup>179</sup> For example, in *American Dairy Queen Corp. v. YS&J Enterprises, Inc.*,<sup>180</sup> the holdover franchisee refused to stop operating a Dairy Queen®/Orange Julius® restaurant in Fayetteville, North Carolina. Dairy Queen, among other claims, asserted “trademark infringement pursuant to 15 U.S.C. § 1114 [and] false designation of origin pursuant to 15 U.S.C. §1125.”<sup>181</sup> The court noted that “[I]t is well established that a franchisee’s post-termination use of franchise marks may constitute trademark infringement warranting an award of treble damages under the Lanham Act, 15 U.S.C. §1117.”<sup>182</sup> It then found that defendants engaged in “intentional and willful infringement”<sup>183</sup> and trebled the “actual damages,” which the court characterized as “the fees defendants would have paid it under the parties’ agreement” during the infringement period.<sup>184</sup>

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<sup>177</sup> 15 U.S.C. § 1117(a); see also *Babbitt Elecs., Inc. v. Dynascan Corp.*, 38 F.3d 1161, 1182 (11th Cir. 1994); *Sands, Taylor & Wood v. The Quaker Oats Co.*, 34 F.3d 1340, 1347 (7th Cir. 1994); *Luxottica Retail N.A., Inc. v. Haffner Enter., Inc.*, No. 8:11-CV-2433-T-23TBM, 2012 WL 1405704, at \*1 (M.D. Fla. Apr. 23, 2012) (holding that the Lanham Act entitles a successful plaintiff to a cumulative recovery of the defendant’s profits, any damages sustained by the plaintiff, and the costs of the action); *Buffalo Wild Wings, Inc. v. Buffalo Wings & Rings*, No. 09-1426 JRT/SER, 2011 WL 4537970, at \*4 (D. Minn. Sept. 29, 2011).

<sup>178</sup> 15 U.S.C. § 1117(a).

<sup>179</sup> *Holiday Inns, Inc. v. Airport Holiday Corp.*, 493 F. Supp. 1025, 1028 (N.D. Tex. 1980), *aff’d sub nom.*, *Holiday Inns, Inc. v. Alberding*, 683 F.2d 931 (5th Cir. 1982) (trebling of profits and damages awarded to motel franchisor for “flagrant” and “willful” infringement by holdover franchisee).

<sup>180</sup> No. 5:14-CV-151-BR, 2014 U.S. Dist. LEXIS 112977 (E.D.N.C. Aug. 14, 2014).

<sup>181</sup> *Id.* at 1.

<sup>182</sup> *Id.* at 4 (quoting *McDonald’s Corp. v. Do*, No. Civ. A. 00-1592-A, 2001 WL 34042640, at \*4 (E.D. Va. Apr. 30, 2001), *aff’d*, 20 F. App’x 194 (4th Cir. 2001); see also *Gorenstein Enterprises v. Quality Care—USA*, 874 F.2d 431, 435–36 (7th Cir. 1989) (awarding treble damages for post-termination use of trademarks); *Ramada Inns, Inc. v. Gadsden Motel Co.*, 804 F.2d 1562, 1568 (11th Cir. 1986) (awarding treble damages, attorney fees and prelitigation interest where the franchisee illegally held over after its franchise was terminated); *KFC Corp. v. Lilleoren*, 821 F. Supp. 1191, 1193–94 (W.D. Ky. 1993) (same). In such cases, the total franchise service fees which the defendant would have owed under the terminated franchise agreement during the period of post-termination use of the franchise marks provides an appropriate measure of base damages. See *Ramada Inns Inc.*, 804 F.2d at 1565; *Holiday Inns v. Airport Holiday Corp.*, 491 F. Supp. 1025, 1028 (N.D. Tex. 1980).

<sup>183</sup> *Id.* at 5 (citing *Vanwyk Textile Sys., B.V. v. Zimmer Mach. Am., Inc.*, 994 F. Supp. 350, 380 (W.D.N.C. 1997)).

<sup>184</sup> *Id.*

When a violation involves use of a counterfeit mark (i.e., a mark that is “identical with or substantially indistinguishable” from a federally registered mark) and the mark is used in connection with goods and/or services encompassed by the federal registration, courts are *required* to assess treble damages on the “profits or damages, whichever amount is greater, together with a reasonable attorney’s fee” absent “extenuating circumstances.”<sup>185</sup> A plaintiff may also elect to recover statutory damages in lieu of actual damages or profits for the use of a counterfeit mark.<sup>186</sup> Accordingly, a claim under 15 U.S.C. § 1117(c) - intentionally using a mark knowing that it is a counterfeit mark – could be a significant tool for franchisors, which should be of great concern to holdover franchisees. Although a holding that a holdover franchisee’s use of a franchisor’s federally registered mark constitutes counterfeiting has gained only limited acceptance to date, a 2012 *The Franchise Lawyer* article examined the evolution of this potential claim in cases involving holdover franchisees.<sup>187</sup> For example, a franchisor successfully asserted a counterfeiting claim against a holdover franchisee in *Century 21 Real Estate, LLC v. Destiny Real Estate Props.*<sup>188</sup> There, after determining that a holdover franchisee’s continued use of the franchisor’s mark after termination of the franchise agreement constituted counterfeiting under the Lanham Act, the court awarded treble damages and attorney fees.<sup>189</sup> The clear advantage to franchisors is that counterfeit-based claims can if sufficiently proven, dramatically increase the monetary remedies that are available. That is because, absent “extenuating circumstances,” the court **must** award treble damages on the franchisee’s profit or franchisor’s damages, whichever is greater, or allow statutory damages up to \$2 million (at the franchisor’s election) and reasonable attorney fees.<sup>190</sup> The article also noted, “In light of the dire consequences former franchisees face in having their post-termination trademark use of a franchisor’s federally registered mark held to constitute counterfeiting, they would do well to consider carefully this issue in developing and executing a plan for leaving the franchisor’s system.”<sup>191</sup>

#### IV. TORT DAMAGES – ECONOMIC LOSS RULE

Courts generally will not grant or base damages on tort theories in contract disputes. In essence, where there is a breach of contract, there cannot be a tort. Known as the “economic loss rule,” two of our Forum colleagues articulated it this way in 2008: “Generally speaking, this rule prohibits recovery of damages in tort when the subject injury is unaccompanied by either

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<sup>185</sup> 15 U.S.C. § 1117(b).

<sup>186</sup> 15 U.S.C. § 1117(c).

<sup>187</sup> Christopher P. Bussert, *Trademark Counterfeiting: A New Danger that Lurks for Holdover Franchisees*, 15 *The Franchise Lawyer* 4 (Fall 2012).

<sup>188</sup> No. 4:11-CV-38 JD, 2011 WL 6736060 (N.D. Ind. Dec. 19, 2011).

<sup>189</sup> *Id.* at \*5–6.

<sup>190</sup> 15 U.S.C. § 1117(b) and (c).

<sup>191</sup> Bussert, *supra* note 187, at 5.



property damage or personal injury.”<sup>192</sup> Different jurisdictions also have different nomenclatures for related doctrines, such as “contort”<sup>193</sup> and “gist of the action.”<sup>194</sup>

But still, there is an “injury,” so what does this mean in practical application? Confusion in grasping the true meaning and application is apparently common. One commentator opined that the economic loss rule “is one of the most confusing doctrines in tort law.”<sup>195</sup> Reviewing three variations or strains of the rule may offer some clarity:

- prohibiting recovery for economic loss in tort where there is *no personal injury or property damage*, without regard to contract.
- prohibiting recovery for economic loss in tort *where the loss is also compensable by a breach of contract claim*.
- prohibiting recovery for economic loss on both contract and tort theories, *unless the tort is separate and independent from the claimed contract breach*.<sup>196</sup>

It is the second and third variations that most concern franchise lawyers. It is the search for the boundary between tort and contract law. Here is another way of looking at it: commercial parties define, allocate, and in some instances limit damage arising from known or predictable risks or disputes. Contract law seeks to limit recovery to the parties’ expectations based on the anticipated contract fulfillment whereas tort law deals with the happenstance of events, known and unknown, and allows damage for injury based on the failure of certain duties owed and the proximate cause of injuries related to those events. Thus, a contract involves commercially-related parties who have the opportunity to plan for outcomes; while a tort, such as an automobile accident, involves strangers with no common plan. Yet confusion remains when contracts are involved, and are coupled with tort-based claims like fraud.

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<sup>192</sup> Christian C. Burden and Sean Trende, *The Economic Loss Rule and Franchise Attorneys*, 27 Franchise L.J. 192 (Winter 2008) (citing Stewart I. Edelstein, *Beware the Economic Loss Rule*, 42 Trial 42, 42 (2006)).

<sup>193</sup> See *Berkel & Co. Contractors, Inc. v. ConocoPhillips Co.*, Civ. Action No. G-05-589, 2006 WL 2037566, at \*2–3 (S.D. Tex. July 17, 2006) (recognizing that in some circumstances there may be “tortious liability for the negligent performance of contracts,” referred to as a ‘contort’ that requires a two-step inquiry analyzing: “(1) whether the conduct violated duties imposed by the contract or bylaw, and (2) an examination of the nature of the loss, i.e., whether the loss or damages go to the subject matter of the contract”); see also *Best Buy Stores, L.P. v. Devs. Diversified Realty Corp.*, Civ. No. 05-2310, 2007 WL 4191717, at \*3 (D. Minn. Nov. 21, 2007) (“the law of contorts is a muddy area, devoid of bright line rules or easy answers as to what conduct constitutes a tort, and what a breach of contract”) (internal quotation omitted); *Erlach v. Menezes*, 21 Cal. 4th 543, 551 (Cal. 1999) (describing the differing goals of tort and contract law and disapproving of the rise of contorts).

<sup>194</sup> See *Am. Home Assur. Co. v. Major Tool & Mach., Inc.*, 767 F.2d 446, 448 (8th Cir. 1985) (“where the gist of the action is the breach of contract, either by misfeasance or nonfeasance... the foundation of the action is in contract.”) (internal quotations omitted); *Stanley Black & Decker, Inc. v. Gulian*, 70 F. Supp. 3d 719, n.4 (D. Del. 2014) (noting the distinctions between comparable doctrines: Pennsylvania’s gist of the action doctrine and Connecticut’s economic loss rule); *eToll, Inc. v. Elias/Savion Advertising, Inc.*, 811 A.2d 10, 14–15, 2002 PA Super 347 (Pa. Sup. Ct. 2002) (holding that unless the breach of contract gives rise to an actionable tort, it must be dismissed pursuant to the gist of the action doctrine to avoid confusion between well-settled forms of actions: contract and tort).

<sup>195</sup> R. Joseph Barton, *Drowning in a Sea of Contract: Application of the Economic Loss Rule to Fraud and Negligent Misrepresentation Claims*, 41 W. & M. L. Rev. 1789, n.3 (2000).

<sup>196</sup> F. Malcolm Cunningham, Jr. and Amy L. Fischer, *The Economic Loss Rule: Deconstructing the Mixed Metaphor in Construction Cases*, 33 Tort & Ins. L.J. 147, 155 nn. 37–38 (1997).

Nevertheless, this judge-made rule, with an extensive evolutionary history too long to discuss here,<sup>197</sup> has survived a nearly half century of debate, discussion, and dissent. And, it has become nearly universally accepted.<sup>198</sup>

The rule landed on the franchise doorstep in *Broussard v. Meineke Discount Muffler Shops, Inc.*<sup>199</sup> After awarding one of the highest damage amounts in franchising history, the Fourth Circuit reversed the lower court's judgment, thanks to the economic loss rule. The Fourth Circuit court put it this way: "This is a straightforward contract dispute, yet it somehow managed to become a massive tort action in the end."<sup>200</sup> On remand, the lower court was instructed to limit the award to contractual damages without imposing punitive damages.<sup>201</sup>

The 2012 case *Beaver v. Inkmart, LLC*<sup>202</sup> was discussed by Michael Joblove and Peter Lagarias at the 2013 Forum on Franchising<sup>203</sup> but the distinctions drawn are worth revisiting. Applying the economic loss rule, the district court dismissed the franchisee's claim of fraudulent misrepresentation and inducement when the terms of the franchise agreement contradicted the alleged misrepresentations. Nevertheless, the court left standing claims for fraudulent and negligent *omissions* or concealment; in particular, that the franchisee's consultant (hired to find the franchise opportunity) was an officer of the franchisor.<sup>204</sup> The *Beaver* court distinguished these claims from the fraudulent inducement claim by noting that they were "different from the accusations based on representations of the [franchisor's] performance or services available" under the franchise agreement and that the franchisor had a duty to disclose its relationship with the franchisee's consultant under the Florida Deceptive and Unfair Trade Practices Act and the FTC Rule. Essentially, the economic loss rule did not bar claims relating to the duty to disclose required information *before* execution of the contract because they did not involve the performance of or contradict the terms of the contract.<sup>205</sup>

The recent case *Yumilicious Franchise, LLC v. Barrie*<sup>206</sup> illustrates that the economic loss rule has wide application. The Fifth Circuit rejected the franchisee's claim of negligent misrepresentation because the franchisee:

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<sup>197</sup> See *id.* at 192–194 for an extended discussion.

<sup>198</sup> Amanda K. Esquibel, *The Economic Loss Rule and Fiduciary Duty Claims: Nothing Stricter Than the Morals of the Marketplace?* 42 Vill. L. Rev. 789 (1997); also see *Clemens v. Nelson Fin. Grp., Inc.*, No. 10CVA-01-1221, 2015-Ohio-1232, ¶ 34 (Ohio Ct. App. May 31, 2015) where acceptance of and support for the rule is solidly embedded in Ohio common law – "Absent tangible physical harm to persons or tangible things, there is generally no duty to exercise reasonable care to avoid economic losses to others."

<sup>199</sup> 155 F.3d 331 (4th Cir. 1998).

<sup>200</sup> *Id.* at 345.

<sup>201</sup> *Id.* at 347.

<sup>202</sup> No. 12-60028, 2012 WL 3822264 (S.D. Fla. Sept. 4, 2012).

<sup>203</sup> Joblove et al., *supra* note 2, at 17.

<sup>204</sup> *Beaver*, 2012 WL 3822264, at \*4–5.

<sup>205</sup> *Id.*

<sup>206</sup> No. 15-10508, 2016 WL 1375871 (5th Cir. Apr. 6, 2016).

introduced no evidence that Yumilicious's actions caused injury and in part because it was barred by the economic loss rule. In Texas, the economic loss rule generally precludes recovery in tort for economic losses resulting from the failure of a party to perform under a contract. In operation, the rule restricts contracting parties to contractual remedies for those economic losses associated with the relationship, even when the breach might reasonably be viewed as a consequence of a contracting party's negligence..... As the district court [had] concluded [at the trial court level], "[d]efendants' fraud and negligent misrepresentation claims are tied directly to the Franchise Agreements and arise solely from the contractual relationship between the parties." Therefore, the economic loss rule dictates that any losses [franchisee] suffered as a result of the franchise agreements give rise to claims sounding in contract, not tort.<sup>207</sup>

Despite the language above, the court noted that the economic loss rule's application was limited to the claim of negligent misrepresentation, not the fraud or fraudulent inducement claims. However, those claims met similar fates for different reasons: lack of evidence and contractual disclaimers and waivers.<sup>208</sup>

## V. PUNITIVE AND EXEMPLARY DAMAGES UNDER STATUTORY AND COMMON LAW

Hand in hand with the discussion above of damage limitations and the economic loss rule is the recovery of punitive damages. First, many contemporary franchise agreements waive recovery of punitive and exemplary damages. Second, to sustain a claim for punitive damages, a tort claim is essential. If the "injury" is compensable by way of a breach of contract claim, no tort will lie in most jurisdictions. Thus, in the franchise context, recovery of punitive damages or exemplary damages generally can be constrained by the contract.

Recovery of punitive damages is determined by state law. Although the criteria for recovery differs in each state, one fundamental precept prevails: "Punitive damages are not recoverable for a breach of contract unless the conduct constituting the breach is also a tort for which punitive damages are recoverable."<sup>209</sup> Some states have embodied this tenet in statutes and jury instructions.<sup>210</sup> Under New York law, as restated in a 2015 decision involving a dispute over the sale of two Dunkin' Donuts restaurants, the New York Supreme Court reported: "It is

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<sup>207</sup> *Id.* at \*5 (internal quotations and citations omitted).

<sup>208</sup> *Yumilicious Franchise, L.L.C.*, 2016 WL 1375871, at \*6.

<sup>209</sup> Restatement (Second) of Contracts § 355, comment A (1981).

<sup>210</sup> When instructing when punitive damages may be considered, Ohio Revised Code § 2315.21(A)(1) (Punitive or exemplary damages) provides: "'Tort action' means a civil action for damages for injury or loss to person or property. 'Tort action' includes a product liability claim for damages for injury or loss to person or property that is subject to sections 2307.71 to 2307.80 of the Revised Code, *but does not include a civil action for damages for a breach of contract or another agreement between persons.*" (emphasis added); also see, Ohio Jury Instructions, CV 315.37 Punitive damages: certain tort actions (claims arising on and after 4/7/05) [Rev. 12-5-09]; California Civil Code section 3294, subdivision (a) permits an award of punitive damages "for the breach of an obligation *not arising from contract*, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice." (emphasis added).

well established that punitive damages are not available for a private wrong, breach of contract, and ordinary fraud (citations omitted).<sup>211</sup>

Nevertheless, there are instances when punitive damages, exemplary damages or enhanced statutory damages can be recovered.

In *Powerhouse Motorsports Group, Inc. v. Yamaha Motor Corporation, U.S.A.*<sup>212</sup>, the court affirmed an award of \$200,000 in punitive damages. Yamaha argued that it was improper to grant punitive damages to the terminated franchisee. Yamaha's actions disrupted a planned sale of the dealership to a third party upon a breach of contract. The appellate court found no error in the award because it was not based on a breach of contract but rather on the tort of intentional interference with contractual relations.<sup>213</sup> Hence, as we noted above, to sustain a viable claim for punitive damages, a tort claim is essential. The court also found that a "willful" violation of California Vehicle Code Section 11713.3 supplied an additional ground for "tort" liability<sup>214</sup> and awarded \$533,350 under Section 11726 of the California Vehicle Code.<sup>215</sup>

State franchise laws and business opportunity acts may provide authority for recovery of "exemplary" or statutory-enhanced damages. Trebling damages is not uncommon. Hawaii's franchise laws allow courts to "increase the award of damages to an amount not to exceed three times the actual damages sustained."<sup>216</sup> South Dakota and Washington also offer similar damage enhancements.<sup>217</sup> A violation of Ohio's Business Opportunity Purchaser's Protection Act allows a purchaser to "recover up to three times the amount of actual damages or ten thousand dollars, whichever is greater."<sup>218</sup> As discussed in Section III.D., state Little FTC Acts may also provide for the recovery of punitive damages.

## VI. ATTORNEY FEES

Any discussion of the recovery of attorney fees must begin with the so-called "American Rule." As one court explained:

A majority of state supreme courts currently recognize and follow the "American Rule" regarding the recovery of attorney fees by the prevailing party in a civil action. This rule provides \* \* \* that attorney's fees are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefor." (Emphasis added.) *Fleischmann Distilling Corp. v. Maier Brewing Co.* (1967), 386 U.S. 714, 717, 87 S.Ct. 1404, 1406, 18

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<sup>211</sup> *Reddy v. Gade*, 2105 NY Slip Op 31109(U), No. 103129/2010, 2015 N.Y. Misc. LEXIS 2286 (N.Y. Sup. Ct. June 23, 2015).

<sup>212</sup> 164 Cal. Rptr. 3d 811, 221 Cal. App. 4th 867 (Cal. Ct. App. 2013).

<sup>213</sup> *Id.* at 883.

<sup>214</sup> *Id.* at 885.

<sup>215</sup> *Id.* at 886 ("willful" was defined as "as intentional wrongful conduct, done either with a knowledge that serious injury to another will probably result, or with a wanton and reckless disregard of the possible results.")

<sup>216</sup> Haw. Rev. Stat. § 482E-9; Hawaii Stat. § 482E9: Civil liability.

<sup>217</sup> See S.D. Cod. Laws Ann. § 37-5B-49 (treble damages); Wash. Rev. Code § 19.100.190 (treble damages).

<sup>218</sup> Ohio Rev. Code § 1334.09(A)(1)(b) (Action for rescission and damages).

L.Ed.2d 475. See, also, *Alyeska Pipeline Service Co. v. Wilderness Society* (1975), 421 U.S. 240, 257, 95 S.Ct. 1612, 1621, 44 L.Ed.2d 141, and Comment d to Section 356 of the *Restatement of the Law 2d, Contracts* (1981) 160, which provides in part: "Although attorneys' fees are not generally awarded to the winning party, if the parties provide for the award of such fees the court will award a sum that it considers to be reasonable."<sup>219</sup>

So although attorney fees are "not ordinarily recoverable," in the franchise world, counsel may generally rely on two exceptions to the rule: statutes and franchise agreements providing for recovery.

Although there are myriad cases concerning the recovery of attorney fees in various aspects of franchise-related matters, we will confine our review to matters involving direct disputes between franchisees and franchisors.

Recent decisions in which courts awarded attorney fees under specific franchise agreement provisions include:

- *Creative Playthings Franchising Corp. v. Reiser*<sup>220</sup> - a terminated franchisee continued to operate its store, requiring the franchisor to sue to enforce the termination. Following a trial, the court awarded attorney fees and expenses to the franchisor. The franchise agreement provided for the recovery of *reasonable* attorney fees, and the franchisee challenged the reasonableness of fees requested. In reviewing the billing records (under the lodestar approach), the court found certain shortcomings: the entries did not uniformly indicate the number of hours spent on each task and did not always identify which attorney completed the task. The court reduced the fees by 25 percent due to these deficiencies but gave no weight to the fact that the fees awarded were more than the damages awarded.
- *Dunkin' Donuts Franchising, LLC v. Claudia I, LLC*<sup>221</sup> - Dunkin' obtained an award of attorney fees from its former franchisee despite a claim that they were unreasonable. The challenge focused on the fact that Dunkin's counsel's hourly rate was more than twice that charged by counsel representing a third-party defendant. The court rejected the challenge because reasonableness of fees is judged by the prevailing rate in the geographical locale, and counsel's rate was not inconsistent with the prevailing rate.
- *Regis Corp. v. Southern El Dorado Corp.*<sup>222</sup> - the Third Circuit affirmed a bankruptcy court's award of attorney fees to the franchisor against a purchaser of franchises from a bankruptcy debtor. The court noted that "[t]he Franchise Agreements are governed by Kansas law, which permits a court to award attorneys' fees where, as here, they are

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<sup>219</sup> *Nottingham Homeowners' Assoc., Inc. v. Darby*, 33 Ohio St.3d 32, 33-34, n. 4, 514 N.E.2d 702 (Ohio 1987) ("At least twenty-nine state supreme courts and the District of Columbia have recognized the contract exception to the 'American Rule' regarding attorney fees").

<sup>220</sup> No. 09-11456-DLC, Bus. Franchise Guide (CCH) ¶ 15,565 (D. Mass. Aug. 3, 2015).

<sup>221</sup> No. 12-2010, 2014 WL 7008593 (E.D. Pa. Dec. 12, 2014).

<sup>222</sup> Nos. 14-3385, 14-3386, 2015 U.S. App. LEXIS 9912 (3d Cir. June 10, 2015).

“provided for by contract.” [citation omitted]<sup>223</sup> The franchise agreements provided for the recovery of reasonable attorney fees by the prevailing party, and the court found the fees to be reasonable.

- *CareMinders Home Care, Inc. v. Sandifer*<sup>224</sup> - an arbitrator awarded the franchisor \$243,766.78 in attorney fees and expenses after finding that it was entitled to them under the franchise agreement and/or Georgia statutory law.<sup>225</sup> The court affirmed the arbitrator's attorney fee award because the American Arbitration Association Commercial Rules permitted the award and because the Federal Arbitration Act prohibited the court from reviewing the franchisee's argument under Georgia law.

An interesting, related area for discussion is the matter of unilateral fee-shifting clauses—those that permit just one side to recover attorney fees. Although the concept may strike some as unconscionable, a line of non-franchise-cases has supported enforcement in some instances:

- *Wilborne v. Bank One Corporation*<sup>226</sup> - the Supreme Court of Ohio stated that “[a] provision in a residential-mortgage contract requiring a defaulting borrower to pay a lender's reasonable attorney fees as a condition of terminating pending lender-initiated foreclosure proceedings on a defaulted loan and reinstating the loan is not contrary to Ohio statutory or decisional law or against Ohio public policy.”<sup>227</sup> Although the court did not use the word “unilateral,” it upheld the one-sided provision after citing the American rule and its exceptions because parties to a contract are free to provide for the payment of attorney fees, and the practice did not violate public policy.
- *Allied Industrial Scrap, Inc. v. Omnisource Corporation*<sup>228</sup> - the Sixth Circuit reversed a district court's ruling that a unilateral fee-shifting clause for attorney fees was unenforceable under Ohio law as a matter of public policy. The Sixth Circuit noted a change in Ohio law after the date of the case the district court relied on, stating “Three years after the Scotts case [*Scotts Co. v. Central Garden & Pet Co.*, 403 F.3d 781 (6th Cir. 2005)], the Ohio Supreme Court in *Wilborn v. Bank One Corp.*, 906 N.E.2d 396 (Ohio 2009), made it clear that it would enforce such unilateral or one-sided fee-shifting contract provisions. Therefore, we must reverse.” The court

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<sup>223</sup> *Id.* at 7.

<sup>224</sup> No. 1:14-CV-03573-WSD, 2015 U.S. Dist. LEXIS 85016 (N.D. Ga. June 29, 2015).

<sup>225</sup> The relevant statutes were O.C.G.A. § 13611 and O.C.G.A. § 91514. O.C.G.A. § 13611 provides for the award of litigation expenses where a “plaintiff has specially pleaded and has made prayer thereof and where the defendant has acted in bad faith, has been stubbornly litigious, or has caused the plaintiff unnecessary trouble and expense.” O.C.G.A. § 91514 allows the court to assess reasonable attorney fees if it finds that a party asserted claims or defenses that lacked substantial justification, were asserted for the purpose of delay or harassment, or the claims “unnecessarily expanded the proceeding by other improper conduct.”

<sup>226</sup> 121 Ohio St.3d 546, 906 N.E.2d 396 (Ohio 2009).

<sup>227</sup> *Id.* Syllabus of the Court.

<sup>228</sup> 776 F.3d 452 (6th Cir. 2015).

observed that although the defendant negotiated important contract provisions, it had left the fee clause alone: “In the event purchaser shall default in his obligations hereunder, purchaser shall be liable for [the plaintiff]’s costs of collection, including attorney fees.” The court also noted that the parties were “experienced and sophisticated commercial entities” that were on an “equal footing” and “there was no duress.”<sup>229</sup>

The remaining exception to the American Rule is grounded in state and federal statutes. Attorney fee awards under the federal Lanham Act are discussed in Section III above. State franchise disclosure laws generally provide the right to recover attorney fees as well.<sup>230</sup> State franchise laws are another source for the recovery of attorney fees.<sup>231</sup> Finally, 25 states have business opportunity laws, the vast majority of which allow for the recovery of attorney fees.<sup>232</sup>

Because courts and arbitrators generally require a very clear, expressed intent before concluding that the “American Rule” does not apply, parties should be as clear as possible as to what components are included in any cost-shifting provisions while not limiting the provision’s scope. Relief should include all costs, expert witness fees, attorney fees, arbitrator fees, court filing fees, arbitration administration costs and fees, including those incurred before any arbitration or lawsuit was filed.

Although there are a multitude of cases awarding attorney fees, practitioners are well-advised to study rulings that have denied or reduced fee awards.

*Meltzer/Austin Rest. Corp. v. Benihana Nat’l Corp.*<sup>233</sup> demonstrates how particular courts can be when reviewing attorney fees. In scrutinizing a fee-shifting clause, the court found that it was limited to the franchisor’s “enforcement” of certain agreement provisions and therefore did not allow recovery for defending the franchisee’s claims for breach of contract and fraud. The court allowed attorney fee recovery for only a small slice of the franchisor’s effort to shut down a terminated franchisee...but only until the franchisee actually closed.<sup>234</sup>

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<sup>229</sup> *Id.* at 453.

<sup>230</sup> Cal. Bus. & Prof. Code § 31300; Haw. Rev. Stat. § 482E-9; Ill. Rev. L. Ch. 815, § 705/26; Ind. Code § 24-5-8.16; Md. Code Ann. Bus. Reg. § 14-227; Mich. Comp. Laws § 445.1531; Minn. Stat. § 80C.17; N.Y. Gen. Bus. Law § 691.1; N.D. Cent. Code § 51-19-12; Or. Rev. Stat. § 650.020; R.I. Gen. Laws § 19-28.1-21; S.D.C.L. § 37-5B-49; Va. Code Ann. § 13.1-571; Wash. Rev. Code § 19.100.190.

<sup>231</sup> See discussion in Section III.D.; see also Ark. Code Ann. § 4-72-208; Conn. Gen. Stat. § 42-133(g)(a); Del. Code Ann. Tit. 6 § 2553; D.C. Code Ann. § 29-1206; Haw. Rev. Stat. § 482E-9, 480.13; Ill. Rev. Stat. Ch. 815, 705/26; Ind. Code Ann. § 23-2-2.7-4; Iowa Code § 523H.6, 52311.13; Minn. Stat. § 80C.17(3); Miss. Code Ann. § 75-24-57; Mo. Rev. Stat. § 407.410; Neb. Rev. Stat. § 87-409; N.J. Stat. § 56:10-10; Va. Code Ann. § 13.1-571; Wash. Rev. Code § 19.100-190; Wis. Stat. § 135.06; P.R. Laws Ann. Title 10, § 278b; V.I. Code Ann. Tit. 12A, Subch. III, § 135.

<sup>232</sup> For a survey of business opportunity laws and the civil remedies, including attorney fee recovery, see John R.F. Baer and James A. Meaney, *Business Opportunity Laws: An Enforcement and Litigation Trap?*, ABA 24th Annual Forum on Franchising, W5 (2001); see also discussion in Section III.C. above.

<sup>233</sup> No. A-11-CV-542-AWA, 2014 U.S. Dist. LEXIS 172665 (W.D. Tex. Dec. 15, 2014).

<sup>234</sup> *Id.* at 4.

Courts and arbitrators routinely review the reasonableness of costs and fees claimed, even if the provision does not explicitly state that recoverable costs and fees must be reasonable.<sup>235</sup> As a result, fee reduction is not uncommon. *JTH Tax, Inc. v. Grabert*<sup>236</sup> and *Accor Franchising North America, LLC v. HR & F Hotel Group, LLC*<sup>237</sup> are examples. In *JTH Tax, Inc.*, the court reduced the requested attorney fees by 60% because only one claim allowed for attorney fee recovery: collection of promissory notes. The billing failed to distinguish between time spent on the promissory note claim and two other claims that did not allow for fee recovery. The court allowed only 40% of the requested fees. Hence, counsel seeking costs and fees should keep careful, detailed timesheets and be mindful of the claims supporting fee recovery. Supporting documentation, including articles, case law in the jurisdiction, and expert testimony, may be required to prove the reasonableness of the costs and fees requested.<sup>238</sup>

In *Accor Franchising North America, LLC*, the court also drastically cut requested fees. Accor sought \$56,487.87 but was awarded only \$14,907.90 in fees. The reasons for the reduction: (i) the fee statements were heavily redacted affecting the court's ability to analyze the charges and (ii) Accor presented inadequate evidence of the prevailing market rates in the district. Although local counsel submitted an affidavit on the prevailing market rates, the court stated that an unaffiliated law firm or counsel should have submitted the affidavit.<sup>239</sup>

When reviewing the reasonableness of prevailing parties' attorney fees, courts have used different methods to ascertain what constitutes a "reasonable" fee.<sup>240</sup> One method common for statutory claims is a "lodestar" analysis that determines attorney fees by "taking the number of hours reasonably expended on the litigation multiplied by a reasonable hourly rate."<sup>241</sup> That amount may then be adjusted upward or downward based on a variety of factors, including the prevailing party's relative success.<sup>242</sup>

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<sup>235</sup> See, e.g., *Bernback v. Greco*, 69 F. App'x 98, 105 (3d Cir. 2003) (considering whether litigation expenses claimed by prevailing party were 'reasonable' where fee-shifting provision required losing party to pay 'actual' costs, including attorney fees, incurred in litigation).

<sup>236</sup> No. 2:13CV47, 2014 WL 1255278 (E.D. Va. Mar. 26, 2014).

<sup>237</sup> No. 0:12-CV-02129-CMC, 2014 WL 1705402 (D. S.C. Apr. 28, 2014).

<sup>238</sup> Courts often require greater proof than merely an affidavit from the billing lawyer. See, e.g., *In re Trade Secret Inc.*, 609 F. App'x 98, 103 (3d Cir. 2015) ("the party seeking attorneys' fees has the burden to prove that its request is reasonable and it must submit evidence to support hours and billing rates it claims") (internal quotations omitted); *King v. GNC Franchising, Inc.*, Civ. Action No. 04-5125-SRC, 2007 WL 1521253, at \*4 (D. N.J. May 23, 2007) ("[the franchisor] must prove its damages in respect of the obligation for legal expenses.... There must be plenary proof, not merely by ex parte affidavit, of the actual services necessarily rendered in the defense of the action, and of the reasonable value thereof") (internal quotations omitted).

<sup>239</sup> *Accor*, 2014 WL 1705402, at \*3-6.

<sup>240</sup> See *Dunkin' Donuts Inc. v. Peter Romanofsky, Inc.*, No. CV-05-3200, 2006 WL 2433127, at \*4-5 (E.D.N.Y. Aug. 8, 2006) (factors to consider when determining whether a fee is reasonable include "the nature of the case and issues presented, the time and labor required, the amount of damages involved, the result obtained, the experience, reputation and ability of the attorney, the usual price charged for similar services by other attorneys in the same area, [and] the amount of awards in similar cases") (internal quotations omitted).

<sup>241</sup> *Id.* at \*5.

<sup>242</sup> *Id.*



Also notable, time spent by in-house counsel managing litigation that outside counsel are actively defending may not be compensable as statutorily provided attorney fees.<sup>243</sup>

The cases above provide guidance on avoiding the pitfalls inherent in attorney fee recovery. This guidance helps in a number of ways: (i) transactional counsel should be aware that franchise agreements must provide fee-shifting provisions that are clear, comprehensive, and precise; (ii) clients should be informed of any limitations on the chance of recovery from the outset (whether statutory or contractual); and, (iii) litigation counsel must take care to understand the scope of the fee-shifting provision or statute. Courts frequently reduce requested fee awards either because there is a failure of proof, such as insufficiently detailed contemporaneous time records, or for more substantive reasons. These reasons include: (i) rates above those prevailing in the community;<sup>244</sup> (ii) duplication of work by multiple billers;<sup>245</sup> (iii) lower level work performed by high-rate attorney<sup>246</sup>; and (iv) general deficiencies.<sup>247</sup> Litigators anticipating submitting a fee request should be careful to match asserted allegations to claims allowing for recovery, to manage the litigation team's workload to avoid duplication, to precisely record all time entries, and to know the jurisdiction's prevailing attorney fee market rates and the possible need for attorney-expert proof of those rates.<sup>248</sup>

## VII. PERSONAL LIABILITY

An important and related question to "how much?" is "who pays?" A franchisor's employees may be liable under state franchise laws or the common law.<sup>249</sup>

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<sup>243</sup> See *Burger King Corp. v. Mason*, 710 F.2d 1480, \*1498-99 (11th Cir. 1983 ("[a]ttorney's fees for the services of in-house counsel are not recoverable..." in an award for statutory attorney fees); see also *Revlon, Inc. v. Carson Prods. Co.*, 622 F. Supp. 362, 365 (S.D.N.Y. 1985) ("reasonable fees do not include the hours in-house counsel spent acting as a liaison between the client and outside counsel").

<sup>244</sup> See *Accor*, 2014 WL 1705402, at \*4-6. When Plaintiff had not "met its burden of establishing the prevailing market rate," the court approved an hourly rate of \$126 for attorneys and \$35 for paralegals as opposed to the \$225-\$375 an hour for attorneys and \$125 for paralegals requested. Further, the court found only one half of the hours charged to be reasonable due to "Plaintiff's omission of any description of services performed, and the court's inability to determine whether counsels' hours are excessive, redundant, or otherwise unnecessary." See also *Gray v. Toyota Motor Sales, U.S.A., Inc.*, No. 10-CV-3081, 2013 U.S. Dist. LEXIS 99113 (E.D. Mich. May 8, 2013). Practitioners should also be aware that out-of-district litigation counsel may have additional hurdles to clear when seeking recovery, i.e., demonstrating that higher rates are justified than in-district counsel would have charged. *MPC Franchise, LLC v. Tarantino*, No. 11-CV-6310 CJS, 2015 U.S. Dist. LEXIS 13232 (W.D.N.Y. Feb. 4, 2015).

<sup>245</sup> See, e.g., *Berryman v. Metcalf*, 177 Wash. App. 644, 312 P.3d 745 (Wash. Ct. App. 2013).

<sup>246</sup> See *Six Continents Hotels, Inc. v. CPJFK, LLC*, No. 09-CV-2021, 2012 U.S. LEXIS 131675 (E.D.N.Y. Sept. 11, 2012) (finding time spent on default judgment motion excessive where most of the work was performed by senior partner).

<sup>247</sup> See *Creative Playthings Franchising Corp. v. Reiser*, No. 09-11456-DLC, Bus. Franchise Guide (CCH) ¶ 15,565 (D. Mass. Aug. 3, 2015) (imposing a 25% reduction due to poor billing records).

<sup>248</sup> See *Dunkin' Donuts Franchising LLC v. SAI Food Hospitality, LLC*, No. 4:11CV01484, 2014 WL 2009106 (E.D. Mo. May 16, 2014) (awarding Dunkin' \$757,573.96 in attorney fees based on an exemplary fee application supported with all the items mentioned here).

<sup>249</sup> Cynthia M. Klaus, *Personal Liability of Franchisor Executives and Employees Under State Franchise Laws*, 29 Franchise L.J. 2, 99 (Fall 2009).

Under the common law, individuals may be held directly liable for tortious conduct when they are personally involved in the tortious act or if they can be reached by “piercing the corporate veil.”<sup>250</sup> It is also possible that a franchisor’s officer, executive, agent, employee, or franchisee could be required to indemnify the franchisor for liability based on his or her individual wrongdoing. This could happen pursuant to contract<sup>251</sup> or the common law.<sup>252</sup>

In addition, most states with franchise registration and disclosure laws, which are discussed in Section III above, also allow franchisees to “hold a franchisor’s officers, shareholders, directors, and (in certain cases) employees jointly and severally liable” for the franchisor’s violations of these statutes.<sup>253</sup>

## VIII. SPOUSAL AND PERSONAL GUARANTIES

Of course, an important component of maximizing monetary recovery is the depth and number of pockets available. Some franchisors may require franchisee signatories to be individuals but allow them to operate through corporations or limited liability companies, all of which could be liable in the event of default. Many will allow entity franchisees but will require the owners’ personal guaranties.<sup>254</sup> Others will require spousal consents or guaranties, which can increase the number of potentially responsible parties and enhance the collectability of any ultimate award.<sup>255</sup> Whatever the structure of the various relationships, it is important for a franchisor to determine if the assets of individuals or entities other than the named franchisee could be available to satisfy any judgment or award.

## IX. DEFENSES IN GENERAL – DISCOUNTING TO PRESENT VALUE, DOUBLE RECOVERY, AND MITIGATION

### A. Discounting to Present Value and Related Methods

Several tools may help ensure that the damages sought are not overstated: (1) discounting to present value (the most common), (2) applying an expected value, and (3) considering economic risk.<sup>256</sup> All three are intended to avoid over-compensation when predicting the future.

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<sup>250</sup> *Id.*

<sup>251</sup> See *Cohen v. Steve’s Franchise Co., Inc.*, 927 F.2d 26, 27–28 (1st Cir. 1991) (requiring franchisee to indemnify franchisor for franchisee’s agents’ “act or omission with respect to the business of operation of the [franchisee]” under parties’ franchise agreement); *Estate of Anderson v. Denny’s Inc.*, 987 F. Supp. 2d 1113, 1161 (D. N.M. 2013) (same).

<sup>252</sup> See, e.g., *Bair v. Peck*, 248 Kan. 824, 842, 811 P.2d 1176, 1190 (Kan. 1991) (“If an employer who is vicariously liable is required to pay damages for the tort of the employee, the employer has a cause of action against the employee to recover the amounts paid”).

<sup>253</sup> Klaus, *supra* note 249, at 99.

<sup>254</sup> For a discussion of guaranties in franchising, see Alison McElroy and Nicole S. Zellweger, *Guaranties and Other Franchise Owner Undertakings*, ABA 37th Annual Forum on Franchising, W13 at 1–5 (2014).

<sup>255</sup> See Ronald A. Giller, Lisa K. Garner and Adam L. Sheps, *Yours, Mine, Ours, and Theirs: The Role of Spousal Guaranties and Consents in the Franchise Relationship*, 33 Franchise L.J. 1, 71 (Summer 2013).

<sup>256</sup> Micklich et al., *supra* note 39, at 224–226 (citing Robert M. Lloyd, *Discounting Lost Profits in Business Litigation: What Every Lawyer and Judge Needs to Know*, 9 Transactions: Tenn. J. Bus. L. 9, 10 (2007)).

We are all familiar with the present value of money being more valuable than that obtained in the future but, perhaps, not as familiar with the other two tools.

Practitioners seldom use expected value analysis in the courtroom but should be aware of it. It is essentially a further adjustment to an estimated award taking into account the probability of the occurrence of certain future events that may bear on the anticipated profit.<sup>257</sup> For instance, what is the likelihood that a particular product or technology will continue to be as desired or used in years to come? Economic risk, similar to “expected value,” attempts to take into account downturns or upturns in the economy that may affect the appropriate discount rate. These two tools may cause more dispute than accord and clearly require industry and economic experts.

Any calculation of future damages, such as projected lost profits, must be discounted to present value. To a layperson, and perhaps even to a franchisee client, it could seem perfectly reasonable to assume that a franchisee who establishes that he or she lost \$100,000 per year in profits for ten years should recover \$1,000,000 in lost profits at trial. But of course that is not accurate because of what financial advisors and others like to call the “time value of money.” The online resource Investopedia provides a helpful and simple explanation of this concept:

The time value of money (TVM) is the idea that money available at the present time is worth more than the same amount in the future due to its potential earning capacity. This core principle of finance holds that, provided money can earn interest, any amount of money is worth more the sooner it is received.<sup>258</sup>

The time value of money requires that damage claims be adjusted downward to compensate the plaintiff for projected future losses. This adjustment is “referred to as ‘present discounted value.’”<sup>259</sup> Although the interest rate used is outdated, Investopedia provides the following simple example:

Everyone knows that money deposited in a savings account will earn interest. Because of this universal fact, we would prefer to receive money today rather than the same amount in the future. For example, assuming a 5% interest rate, \$100 invested today will be worth \$105 in one year (\$100 multiplied by 1.05). Conversely, \$100 received one year from now is only worth \$95.24 today (\$100 divided by 1.05), assuming a 5% interest rate.<sup>260</sup>

In the above example, the five percent figure is known as the “discount rate.” The higher the rate of future return assumed, the lower the present value. In other words, the higher the projected rate of return, the lower the present value, or lump sum damages for future losses, would be awarded at trial. The discount rate applied is the ordinary present interest rate –

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<sup>257</sup> Micklich et al., *supra* note 39, at 227.

<sup>258</sup> Ben McClure, *Discounted Cash Flow Analysis*, Investopedia (April 2016), available at <http://www.investopedia.com/university/dcf/>.

<sup>259</sup> *Id.*

<sup>260</sup> *Id.*

determined by the court or by statute – minus the projected rate of inflation.<sup>261</sup> At least one court has determined that the award for past and present damages may not be included as a factor in determining the discount rate for calculating the future value of the business.<sup>262</sup> When a franchisee fails to submit evidence regarding the appropriate discount rate for its lost future profits claim, the franchisor may be entitled to judgment as a matter of law.<sup>263</sup> Given the complicated nature of calculating interest rates and discounting to present value, litigants should, if at all possible, employ a persuasive expert who has a talent for simplifying this dense topic to permit the average juror to grasp the issues and understand the consequences of their decision.

## **B. Double Recovery and Related Issues**

In addition to failing properly to discount to present value, plaintiffs sometimes also improperly claim duplicative damages. Although presenting alternative damage calculations and theories may be permissible,<sup>264</sup> duplicative damages are not.<sup>265</sup> One common error (inadvertent or not), is an attempt to claim both lost future profits and fair market value of the business in wrongful termination and other cases. A franchisee plaintiff generally cannot recover both lost profits and the value of its franchises because that would result in recovery of not only the cash value of the stores, but also the profit they were supposed to generate, which would be impermissible double recovery.

“In economic theory . . . the current market value of a company is the discounted present value of the estimated flow of future earnings.”<sup>266</sup> In other words, when a claimant asserts that it has “been forced to go out of business by the defendant’s breach, and thus [is] entitled to recover the *value of its business* as damages for breach of contract . . . [the] ‘value’ figure . . . is nothing more than . . . expected future earnings capitalized . . . to their present value.”<sup>267</sup> Accordingly, “[P]laintiff should not be permitted to recover both the capitalized value

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<sup>261</sup> Allen et al., *supra* note 66, at 495–96.

<sup>262</sup> See *Diesel Mach., Inc. v. B.R. Lee Indus., Inc.*, 418 F.3d 820, 837 (8th Cir. 2005).

<sup>263</sup> See *Lithuanian Commerce Corp., Ltd. v. Sara Lee Hosiery*, 23 F. Supp. 2d 509, 517 (D. N.J. 1998).

<sup>264</sup> See, e.g., *Degla Grp. Invs., Inc. v. BoConcept USA, Inc.*, No. CV-09-05278-MMM, 2014 WL 3893367, at \*21 (C.D. Cal. Aug. 8, 2014) (“It is well established that double recovery is precluded when alternative theories seeking the same relief are pled and tried together.”) (internal quotations omitted) (quoting *Clappier v. Flynn*, 605 F.2d 519, 530 (10th Cir. 1979)); *Inter Medical Supplies Ltd. v. EBI Medical Sys., Inc.*, 975 F. Supp. 681, 691 (D. N.J. 1997) (permitting plaintiffs to try a case “on numerous alternative theories of liability each of which would support an award of ‘lost profits’”).

<sup>265</sup> See, e.g., *In re Sherwood Invests. Overseas Ltd., Inc.*, No. 6:10-AP-00158-KSJ, 2015 WL 4464470, at \*24 (Bankr. M.D. Fla. July 22, 2015) (“if a business is completely destroyed, the proper total measure of damages is the market value of the business on the date of the loss, not lost profits. But where a business is *not* completely destroyed, it may recover lost profits.”) (internal quotations omitted); *Envtl. Biotech, Inc. v. Sibbitt Enters., Inc.*, No. 203-CV-124-FTM, 2008 WL 5070251, at \*3-4 (M.D. Fla. Nov. 24, 2008) (same); *Birmingham News Co. v. Horn*, No. CV-99-4243, CV-00-257, 901 So.2d 27 (Ala. June 11, 2004) (awards of both lost profit and business value are impermissibly duplicative).

<sup>266</sup> *Beverly Hills Concepts, Inc. v. Schatz & Schatz, Ribicoff & Kotkin*, 247 Conn. 48, 66 (1998) (quoting Note, *Private Treble Damage Antitrust Suits: Measure of Damages for Destruction of All or Part of a Business*, 80 Harv. L. Rev. 1566, 1580 (1967)) (court’s alterations).

<sup>267</sup> *W. Haven Sound Dev. Corp. v. City of W. Haven*, 201 Conn. 305, 319, 514 A.2d 743, 741 (1986) (“*West Haven I*”) (emphasis in original).

of its projected earnings *and* the lost value of the capital investment necessary to generate those earnings.”<sup>268</sup> Because a business’s value necessarily captures the profits that it is expected to earn (capitalized to present value), courts routinely recognize that a party who seeks both profits *and* the value seeks to recover twice for the same damages.<sup>269</sup>

Fact finders generally also reduce damage awards by “avoided costs.”<sup>270</sup> When the franchisee is a closely-held business, it may try to claim that it should not have to deduct its owners’ salaries when calculating net lost profit because the real parties in interest, the owners, lost their salaries in addition to the business’s profits. The franchisor may, however, be able to argue that the owners lack standing to claim their lost income, particularly if they are not named plaintiffs, and that the general rule requiring net profits to deduct owners’ and officers’ salaries should control. Doing so can substantially reduce a lost profit claim.

“When the courts speak of lost profit calculations they of course talk in terms of net profits.”<sup>271</sup> Lost profits (or net profits) are calculated by subtracting the cost of performance from the gross amount that would have been received had the contract been performed.<sup>272</sup>

As discussed in Section II.A., plaintiffs must prove their damages with “reasonable certainty.” Therefore, in order to prove lost profits, plaintiffs must present evidence regarding

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<sup>268</sup> *Id.* at 329 (emphasis in original).

<sup>269</sup> See, e.g., *Forsyth v. Associated Grocers of Colorado, Inc.*, No. 82CA1131, 724 P.2d 1360, 1365 (Colo. Ct. App. Jan. 2, 1986) (recovery for lost profits, together with market value is “improper double recovery”); *Knauf Fiber Glass, GmbH v. Stein*, 615 N.E.2d 115, 128, Fed Carr. Cas. P 83, 838 (Ind. Ct. App. 1993), *aff’d in part, vacated in part on other grounds*, 622 N.E.2d 163 (Ind. 1993) (jury instruction that damages may include “lost profits and the value of the business” improper because it could “allow[] double recovery”); *Sostchin v. Doll Enters., Inc.*, 847 So.2d 1123, 1128, n.6, 28 Fla. L. Weekly D1470 (Fla. 3d Dist. Ct. App. 2003) (business cannot recover both lost profits and the market value of a business as damages (citing *Aetna Life & Cas. Co. v. Little*, Nos. 78-1785 and 781786, 384 So.2d 213 (Fla. 4th Dist. Ct. App. May 21, 1980))).

<sup>270</sup> See, e.g., *Green-Kelly et al.*, *supra* note 11, at 8–9.

<sup>271</sup> *East Point Sys., Inc. v. Maxim*, Civ. Action No. 3:13-CV-00215-VAB, 2016 WL 1118237, at \*10 (D. Conn. Mar. 22, 2016) (“With respect to calculation of lost profits, ‘net profit’ is the gross amount that would have been received, less the cost of running the business.”) (internal quotations omitted); *New Hampshire Ins. Co. v. Blackjack Cove, LLC*, No. 3:10-cv-607, 2014 WL 1270984, at \*12 (M.D. Tenn. Mar. 26, 2014) (“the recovery of lost profits must be based on net profits and not on gross profits”); *Harris v. Fairweather*, No. 11 Civ. 2152-PKC-AJP, 2012 WL 3956801, at \*5 (S.D.N.Y. Sept. 10, 2012) (“the accepted method of calculating lost profits is to deduct overhead expenses and costs to calculate net profits... lost profits are calculated by estimating the revenue lost due to the infringing conduct and subtracting what it would have cost to generate that revenue”) (internal quotations omitted); see also 1 Robert L. Dunn, *Recovery of Damages for Lost Profits*, § 6.1 (6th ed. 2005) (“Lost profit damages are usually defined as lost net profits.”); see also *Gordon v. Indusco Mgmt. Corp.*, 164 Conn. 262, 275, 320 A.2d 811, 819 (Conn. 1973) (“Net profit can be defined as the gross amount that would have been received pursuant to the business less the cost of running the business.”) (internal quotations and citations omitted); see also *Cheryl Terry Enters. Ltd. v. City of Hartford*, 270 Conn. 619, 649, 854 A.2d 1066, 1085–86 (Conn. 2004) (upholding lost profit award which had been calculated by subtracting future costs from the contract price); *Benvenuti Oil Co. v. Foss Consultants Inc.*, No. CV-010485270-S, 2006 WL 328678, at \*14 (Conn. Super. Ct. Jan. 25, 2006) (“Simply put net profits are what remains after a business deducts expenses.”) (internal citations and quotations omitted); 1 Robert L. Dunn, *Recovery of Damages for Lost Profits* § 6.1 (Lost profit damages in a breach of contract claim are the “contract price less cost of performance, or cost of completion, or, as it is sometimes put, ‘expenses saved’ as a result of plaintiff’s being excused from performance by the other party’s breach.”)

<sup>272</sup> See *Harris*, 2012 WL 3956801, at \*5.

their projected gross revenue as well as future costs saved.<sup>273</sup> Entity plaintiffs nonetheless sometimes try to add back owner or officer salaries to their net profits, such as the amount reported on the entity's tax returns. However, the entity presumably no longer pays these amounts (an expense that is, in effect, "avoided" because of the alleged breach).

In *West Haven Sound Development Corp. v. West Haven*, the Connecticut Supreme Court held that salaries of corporate officers could not be included as part of lost profits when calculating damages based on a breach of contract claim.<sup>274</sup> In that case, a developer was awarded damages based on its claim that its business had failed due to the defendant's contract breach.<sup>275</sup> On appeal, the defendant challenged the recovery of lost profits based on this expert's calculations. The court noted that, in determining plaintiff's future profits, the plaintiff's expert included the salaries of corporate officers as part of the projected revenues and then held that inclusion was improper, stating that, "[t]o the extent that prospective profits were determined without an appropriate deduction from revenues for imputed wages, the going concern value of the Plaintiff's business before the breach, allegedly \$1,900,000, was overstated for the purposes of assessing damages in a contract action."<sup>276</sup>

The presumption that officer salaries must be deducted in *City of West Haven* rests on the standard set forth in an earlier Connecticut case that concluded the plaintiff could not prove his damage claim when he failed to deduct the salary he intended to pay a manager to operate the franchise.<sup>277</sup> There, the plaintiff's determination that his franchise would earn a 12% profit assumed that the plaintiff would run the franchise himself when, in fact, his plan was always to employ a manager.<sup>278</sup> The court concluded that "to determine the cost of operating a business, the factors of production must be analyzed.... One important factor is labor."<sup>279</sup> Thus, labor, including labor performed by the owners and officers, must be deducted to reasonably prove a claim of future lost profits.<sup>280</sup>

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<sup>273</sup> See *Century 21 Real Estate Corp. v. Meraj Intern. Inv. Corp.*, 315 F.3d 1271, 1282 (10th Cir. 2003) ("To be reasonable, an estimate of lost profits must be based on evidence of projected costs as well as projected revenues."); *Coraud LLC v. Kidville Franchise Co., LLC*, 121 F. Supp. 3d 387, 398 (S.D.N.Y. 2015) ("The party claiming lost profits must establish not only the revenue that it would have received absent the breach of contract, but also what costs it avoids as a result of being relieved of its obligations under the contract"); *Cheryl Terry Enters. Ltd.*, 270 Conn. at 619; see also 1 Robert L. Dunn, *Recovery of Damages for Lost Profits* at § 6.1 ("Evidence of gross revenue without proof of the costs incurred in obtaining it will not support a judgment for the plaintiff.").

<sup>274</sup> 201 Conn. at 326.

<sup>275</sup> *Id.* at 308.

<sup>276</sup> *Id.* at 326–27. See also *Beverly Hills Concepts, Inc. v. Schatz & Schatz, Ribicoff & Kotkin*, 1997 WL 41224, at \*23 (stating that the court had questioned the plaintiff's expert's calculation of lost profits because the expert had "add[ed] back" officers' salaries to the cash flow and noting that the plaintiffs, citing to *West Haven Sound Development Corp. v. West Haven*, conceded that officers' salaries should not be added back to the cash flow), *rev'd in part on other grounds by Beverly Hills Concepts, Inc. v. Schatz and Schatz, Ribicoff and Kotkin*, 247 Conn. 48, 717 A.2d 724 (1998).

<sup>277</sup> See *Gordon v. Indusco Corp.*, 164 Conn. 262, 275, 320 A.2d 811, 819 (Conn. 1973).

<sup>278</sup> See *id.*

<sup>279</sup> *Id.* at 275.

<sup>280</sup> See *In re Sherwood Invests. Overseas Ltd., Inc.*, No. 6:10-AP-00158-KSJ, 2015 WL 4464470, at \*32 (Bankr. M.D. Fla. July 22, 2015) ("Failure to include officer compensation in lost profits damages calculations is inadequate as a matter of law") (internal quotations omitted); *Anchor Sav. Bank, FSB v. U.S.*, 59 Fed. Cl. 126, 164 (Fed. Cl. 2003)

A business entity has a separate legal existence from its officers and shareholders. A claim of injury based on a wrong to a corporation may be brought only by or on behalf of the corporation and not by its shareholders to recover on their own behalf.<sup>281</sup> Therefore, the only harm that an entity plaintiff is permitted to redress is the alleged harm to the corporation, not to its individual shareholders or officers. This means that the only damages that the entity is permitted to seek are *its own* lost profits. Adding corporate officers' salaries into the entity's lost profit calculation would improperly inflate the damage claim to recover amounts that the officers themselves (who are not parties to the lawsuit) allegedly lost.

### C. Mitigation

The Restatement of Contracts provides, in relevant part, that "damages are not recoverable for loss that the injured party could have avoided without undue risk, burden or humiliation."<sup>282</sup> As Williston on Contracts explains, a plaintiff cannot recover for damages it could have avoided. Those damages will be considered either as "not having been caused by the defendant's wrong or as not being chargeable against the defendant."<sup>283</sup> The "principle of mitigation of damages has wide application and frequently involves a determination as to whether the plaintiff acted reasonably under the circumstances."<sup>284</sup> Farnsworth on Contracts similarly explains that, "[a] court ordinarily will not compensate an injured party for loss that that party could have avoided by making efforts appropriate, in the eyes of the court, to the circumstances."<sup>285</sup> The principle "encourages the injured party to act so as to minimize the wasteful results of breach."<sup>286</sup> When a loss can be avoided, "the injured party is usually expected not merely to stop performance in order to avoid cost, but to take reasonable affirmative steps to make appropriate substitute arrangements to avoid loss."<sup>287</sup>

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(suggesting that a plaintiff's damages for lost profits could not include time spent by managers and officers implementing the scheme that was the basis of the claims at issue).

<sup>281</sup> *Beverly Hills Concepts, Inc.*, 1997 WL 41224, at \*23, *rev'd in part on other grounds by Beverly Hills Concepts*, 247 Conn. 48, 717 A.2d 724 (Conn. 1998).

<sup>282</sup> Restatement (Second) of Contracts § 350.

<sup>283</sup> Richard A. Lord, 24 Williston on Contracts § 64:27 (4th ed. 2002).

<sup>284</sup> *Id.*

<sup>285</sup> E. Allan Farnsworth, Farnsworth on Contracts § 12:12 (4th ed. 2004).

<sup>286</sup> *Id.*

<sup>287</sup> *Id.*; see also *Moran Foods, Inc. v. Mid-Atlantic Mkt. Dev. Co., LLC*, 476 F.3d 436, 440 (7th Cir. 2001) (citing Restatement (Second) § 350 for the proposition that, "The duty to mitigate damages . . . forbids the victim of a breach of contract, which might well be involuntary, to allow his damages to balloon (when he could easily prevent that from happening), as he might be tempted to do in order to force a lucrative settlement."); *Worrall v. Davis Coal & Coke Co.*, 122 F. 436, 439 (2d Cir. 1903) ("The law does not permit a party to enhance his claim for damages against another for a breach of contract by his own neglect. It would be inequitable, as well as repugnant to this legal rule, to compel [the defendant] to pay the considerable claim in this present case, when all damage could have been avoided by the exercise of common good judgment and prudence . . .").

Mitigation in franchising varies widely. Some states do not require franchisors to mitigate damages.<sup>288</sup> Other states require that when a franchise agreement terminates prematurely, the franchisor must try to replace the franchisee.<sup>289</sup>

## X. EXPERTS

Expert witness testimony may be necessary to ensure recovery of damages in a franchise dispute. While much of this paper's discussion of other damage issues is generously peppered with cases involving the use of experts and their impact, here we zero in on the mechanics and applicable rules.<sup>290</sup>

The Federal Rules of Evidence under the topic of "OPINIONS AND EXPERT TESTIMONY"<sup>291</sup> seem straightforward enough but the U.S. Supreme Court's 1993 *Daubert*<sup>292</sup> decision generated complexities that led to the current version of the rules and reverberate to this day.

The essence of *Daubert* appears in the Court's summary at Part IV of the decision: "'General acceptance' is not a necessary precondition to the admissibility of *scientific* evidence under the Federal Rules of Evidence, but the Rules of Evidence especially Rule 702 do assign to the trial judge the task of ensuring that an expert's testimony both rests on a reliable foundation and is relevant to the task at hand. Pertinent evidence based on *scientifically* valid principles will satisfy those demands."<sup>293</sup> Colloquially, this task became known as "gatekeeping."

The Supreme Court's 1997 decision in *Kuhmo Tire Co. v. Carmichael*<sup>294</sup> expanded trial judges' gatekeeping role to all expert testimony. As one of our colleagues noted shortly after the *Kuhmo* decision: "Consequently, before admitting any type of expert testimony, the trial judge is obligated 'to make certain that an expert, whether basing testimony upon professional studies or personal experience, employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field.' This holding has particular significance to franchising, since most expert testimony admitted under Rule 702 in franchise disputes, including testimony in support of lost-profit damage claims, is nonscientific."<sup>295</sup>

Thus, this gatekeeper role over expert testimony found its way to franchise disputes and is articulated today in the current Federal Rules of Evidence:

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<sup>288</sup> See, e.g., *Burger King Corp. v. Hinton, Inc.*, 203 F. Supp. 2d 1357, 1365 (S.D. Fla. 2002) ("under Florida law a franchisor does not have an obligation to minimize losses or mitigate damages, as a franchise agreement is a non-exclusive contract.").

<sup>289</sup> See *Villager Franchise Sys., Inc. v. Thakore*, No. IP 00-1946-C H/F, 2002 WL 1800205, at \*2-3 (S.D. Ind. July 2, 2002).

<sup>290</sup> We will focus mainly on the Federal Rules of Evidence, Fed. R. Evid. 701-705.

<sup>291</sup> *Id.* at Article VII.

<sup>292</sup> *Daubert v. Merrell Dow Pharma., Inc.*, 509 U.S. 579 (1993).

<sup>293</sup> *Id.* at 597 (emphasis added).

<sup>294</sup> 526 U.S. 137 (1999).

<sup>295</sup> Kevin M. Kennedy, *The Use of Daubert and its Progeny to Attack Lost-Profit Claims*, 20 Franchise L.J. 167, 168 (Spring 2001) (footnotes omitted).



**A. Rule 702. Testimony by Expert Witnesses**

A witness who is qualified as an expert by knowledge, skill, experience, training, or education may testify in the form of an opinion or otherwise if:

- (a) the expert's scientific, technical, or other specialized knowledge will help the trier of fact to understand the evidence or to determine a fact in issue;
- (b) the testimony is based on sufficient facts or data;
- (c) the testimony is the product of reliable principles and methods; and
- (d) the expert has reliably applied the principles and methods to the facts of the case.

History. As amended Apr. 17, 2000, eff. Dec. 1, 2000; Apr. 26, 2011, eff. Dec. 1, 2011.

**B. Rule 703. Bases of an Expert's Opinion Testimony**

An expert may base an opinion on facts or data in the case that the expert has been made aware of or personally observed. If experts in the particular field would reasonably rely on those kinds of facts or data in forming an opinion on the subject, they need not be admissible for the opinion to be admitted. But if the facts or data would otherwise be inadmissible, the proponent of the opinion may disclose them to the jury only if their probative value in helping the jury evaluate the opinion substantially outweighs their prejudicial effect.

History. As amended Mar. 2, 1987, eff. Oct. 1, 1987; Apr. 17, 2000, eff. Dec. 1, 2000; Apr. 26, 2011, eff. Dec. 1, 2011.

**C. Rule 704. Opinion on an Ultimate Issue**

(a) IN GENERAL-NOT AUTOMATICALLY OBJECTIONABLE. An opinion is not objectionable just because it embraces an ultimate issue.

(b) EXCEPTION. In a criminal case, an expert witness must not state an opinion about whether the defendant did or did not have a mental state or condition that constitutes an element of the crime charged or of a defense. Those matters are for the trier of fact alone.

History. As amended Pub. L. 98-473, title II, § 406, Oct. 12, 1984, 98 Stat. 2067; Apr. 26, 2011, eff. Dec. 1, 2011.

**D. Rule 705. Disclosing the Facts or Data Underlying an Expert's Opinion**

Unless the court orders otherwise, an expert may state an opinion- and give the reasons for it-without first testifying to the underlying facts or data. But the expert may be required to disclose those facts or data on cross-examination.

History. As amended Mar. 2, 1987, eff. Oct. 1, 1987; Apr. 22, 1993, eff. Dec. 1, 1993; Apr. 26, 2011, eff. Dec. 1, 2011.

The practical application of these rules and expanded discussions of the mechanics have been well-presented in a number of Forum papers and articles.<sup>296</sup>

Two relatively recent decisions from an Indiana federal court apply the principles embodied in the rules but reach different conclusions—even though the experts used the same basic methodology.

In *CDW LLC v. NETech Corp.*,<sup>297</sup> the district court excluded a major portion of an expert's lost profit calculation because the methodology did not meet the "reliability" requirements of Fed. R. Evid. 702. This action involved plaintiff CDW's claims against a competitor for pirating its confidential and trade secret information when former CDW employees defected to NETech. The defections occurred from the CDW Indianapolis branch.

Citing *Daubert*, the court defined its role "as gatekeeper to bar expert testimony that is not sufficiently reliable or relevant to issues in the case, or testimony offered by a person not sufficiently expert in the field of study that his testimony concerns."<sup>298</sup> The reliability concern focused on the expert's use of the "yardstick" or comparable method.<sup>299</sup> The yardstick method, also sometimes called the benchmark method, uses an available benchmark or standard to determine what the revenues and profits would have been if the situation had not occurred. For

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<sup>296</sup> See, e.g., *id.* at 168; Paula J. Morency and Edward Kushell, *The Art and Science of Using An Expert Witness: A Decade After Daubert*, ABA 27th Annual Forum on Franchising, W4 (2004).

<sup>297</sup> 906 F. Supp. 2d 815 (S.D. Ind. 2012).

<sup>298</sup> *Id.* at 821.

<sup>299</sup> The "yardstick" methodology called into question in this case is discussed extensively by Micklich et al., *supra* note 39, at 224–226.

example, historical revenues and profits might be the yardstick against which revenues and profits for the damage period are compared to calculate the loss. Industry averages are another common measurement tool that expert witnesses use.<sup>300</sup> The court first noted that “A yardstick approach is an acceptably reliable method under *Daubert* for calculating lost profits only if the benchmarks (or yardsticks) are sufficiently comparable that they may be used as accurate predictors of what the target would have done.”<sup>301</sup>

Here, the court disapproved of the “comparables” selected and even more that the “comparables” were averaged. Although the expert selected other CDW branches in the “Great Lakes region” as comparable, he did not explain why those branches were selected to compare to the target market: “In fact, his analysis averages the revenue growth experiences of the other CDW branches, so he does not even compare the Indianapolis branch to the actual experience of any other business entity. It appears that using the average revenue growth experience of the branches, rather than the actual revenue growth or decline of a particular branch, permitted Mr. Hosfield to avoid explaining how another branch’s experience in any year (or over time) could appropriately be applied to Indianapolis. The data for individual branches shows wide variations in branch performance from year to year.”<sup>302</sup> The court concluded that the “average” yardstick method was not reliable for purposes of Fed. R. Evid. 702 and *Daubert*.<sup>303</sup>

More recently in *Andy Mohr Truck Center, Inc. v. Volvo Trucks North America*,<sup>304</sup> the court accepted a “yardstick” approach under Fed. R. Evid. 702 and *Daubert*. Perhaps guided by the deficiencies identified in *CDW LLC*, the expert explained why he selected certain “yardstick” method comparisons: “I have identified similar markets to that of Mohr Truck and compared Volvo Trucks’ market share in those markets to Volvo Truck’s market share in the Indianapolis market to ascertain Mohr Truck’s lost sales. This methodology is consistent with both a yardstick and market share approach.”<sup>305</sup> Moreover, the selected markets were all Midwest markets that the expert believed were most similar to the target geographically and “because they’re considered more economically similar in that they’re impacted by similar economic events. So I was looking for markets that were-had a proximity to Indianapolis and which were larger metropolitan markets.”<sup>306</sup>

The court accepted this explanation as well as the remainder of the expert’s report commenting that it did “not find the methodology to be so unreliable that it should not be submitted to the jury” and that any defects in the information relied on by the expert could be challenged on cross-examination.<sup>307</sup> Thus, the expert’s “straight” yardstick approach was

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<sup>300</sup> See, *Calculating Damages: What Is Reasonable Certainty?*, Fraud, Files Forensic Accounting Blog (<http://www.sequenceinc.com/fraudfiles/2013/02/calculating-damages-what-is-reasonable-certainty/>) (February 21, 2013).

<sup>301</sup> 906 F. Supp. 2d at 821, 824.

<sup>302</sup> *Id.*

<sup>303</sup> *Id.* at 825.

<sup>304</sup> No. 1:12-cv-448-WTL-DKL, 2015 WL 4426861 (S.D. Ind. July 20, 2015).

<sup>305</sup> *Id.* at \*3.

<sup>306</sup> *Id.*

<sup>307</sup> *Id.* at \*4.

acceptable for presentation to the jury, subject to cross-examination to address any reliability concerns.

This comparison of two judges' decisions in the same court illustrates how fact-intensive a *Daubert* review can be, the importance of proper expert witness selection, and how application of the "yardstick" approach may yield different results.

As discussed in Section II.D. above, retained experts should become educated on the applicable standards of proof for damage calculations, particularly when presenting a lost profit analysis. Projecting an overly rosy picture of increasing profits is risky.<sup>308</sup> The expert will be on thin ice during cross-examination if he or she cannot convincingly support the projected increases with adequate reasoning and data.<sup>309</sup> Although routinely done in personal injury cases, shooting for the moon and leaving it to the fact-finder to reduce unrealistic damage projections in business cases can be disastrous.<sup>310</sup>

## XI. CONCLUSION

Too many lawyers treat damages as an afterthought when they are really the crucial endgame. In most cases, a finding of liability is meaningless if there is no damage recovery. Both sides' initial litigation strategy should include detailed analyses of best and worst case damage theories and scenarios, and parties should also consider retaining damage experts to test, expand and lend credibility to the lawyers' analyses. The time and expense of developing or rebutting damage theories and calculations are generally well-spent because of the dividends they can pay in the ultimate award.

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<sup>308</sup> Green-Kelly et al., *supra* note 11, at 11–12.

<sup>309</sup> See, e.g., *Passport Health, Inc. v. Travel Med, Inc.*, No. 2:09-cv-01753-GEB-JFM, 2011 WL 3915840, at \*5 (E.D. Cal. Sept. 6, 2011) ("estimating an increase in gross revenue, and thereby estimating an increase in royalty payments, is too speculative" for a "franchisee's business [that] is not yet established"); *Sorrels v. Lukins & Annis, P.S.*, No. Civ. 01-086-H, 2002 WL 31496418, at \*2–3 (D. Or. Sept. 3, 2002) (concluding that expert's reliance on plaintiff's opinion of value of franchises, rather than past profits or reasonable projections, failed to provide proof of damages); *Brewer v. Custom Builders Corp.*, 42 Ill. App. 3d 668, 356 N.E.2d 565 (5th Dis. 1976) (only nominal damages appropriate where a party establishes entitlement to damages but has not provided a proper basis by which to calculate actual damages); *Norfolk & Western Railway Company v. United States Railway Equip. Co.*, 563 F. Supp. 747 (N.D. Ill. 1983) (overturning an over \$2 million damage award where expert failed to provide non-speculative damage calculation).

<sup>310</sup> See, e.g., *Sorrels*, 2002 WL 31496418, at \*2–3 (granting summary judgment with prejudice where franchisee's projection of profits was based on plaintiffs' opinions rather than facts or reasonable projections); *Gesellschaft Fur Geratebau v. GFG Am. Gas Detection, Ltd.*, No. 70630, 967 S.W.2d 144, 147 (Mo. Ct. App. 1998) (reversing the jury's judgment for lost profit damages where plaintiff offered only "projections that were calculated on neither any actual sales nor revenue"); *Beverly Hills Concepts*, 247 Conn. at 78 (issuing judgment on damages for defendant-franchisor where plaintiffs evidence of lost profits was mere speculation that the franchisee would remain in business and profitable for the 12 year period for which plaintiff sought damages).