## CONTENTS

**About the Editors**  
xxiii

**About the Authors**  
xxv

**Foreword**  
xxvii

**Introduction**  
xxix

*Christina Noyes and Leonard Vines*

1 **Introduction to Practical Problems and Issues Associated with Buying or Selling a Franchise Company**  

*Harris J. Chernow and Charles S. Modell*

I. Introduction to Franchise Acquisitions  
A. Overview  
B. Motivations of Buyers  
C. Motivation of Sellers  
II. Unique Aspects to the Acquisition of a Franchisor  
A. Nature of a Franchisor’s Assets  
B. Nature of a Franchisor’s Liabilities  
C. Franchise Laws  
III. Information Access—Beyond the Typical Due Diligence  
IV. Rights of, and Duties to, Franchisees  
A. Breach of Contract  
B. Common Law Fraud  
C. Breach of Implied Covenant of Good Faith and Fair Dealing  
D. Tortious Interference with Contract  
E. Violation of Antitrust Laws
iv CONTENTS

F. Intra Chain Competition 21
G. Lack of Qualifications 22

V. The Franchise Agreement and FDD—General 23
   A. Transfer and Assignment Provisions 23
   B. Trademarks 23
   C. System Changes 24
   D. Territorial Rights and Encroachment Problems 25
   E. Advertising and Marketing Programs 26
   F. Dispute Resolution Procedures 27
   G. Venue, Jurisdiction and Choice of Law 28
   H. Area Development and Subfranchising Rights 28

VI. Disclosure and Registration Issues with Respect to the Sale of the System 29

VII. Initial Drafting and Document Issues 33
   A. Exploratory Stage 33
   B. Confidentiality Agreement 33
   C. Letter of Intent 35
   D. The Definitive Agreement 37

VIII. Conclusion 39

2 NEGOTIATING KEY PROVISIONS IN THE AGREEMENT 41
Dawn Newton, Rebekah Prince, and Les Wharton

I. Introduction 41

II. Nondisclosure/confidentiality Agreement 42
   A. Confidential Information 43
   B. Term 44
   C. Other Provisions 45

III. Letter of Intent 47
   A. Binding vs. Non-binding 47
   B. General Issues 48
   C. Access to Information 49
   D. Announcement 51

IV. Asset Purchase Agreement 52
   A. Definitions 52
   B. Purchase Price Adjustments: Holdbacks, Escrows, Earn-Outs, and Clawbacks 59
   C. Closing 60
   D. Representations and Warranties 61
   E. Pre-closing Covenants 67
3 DUE DILIGENCE ON FRANCHISE SYSTEMS

John Baer, Mark Kirsch, and Beata Krakus

I. Overview and Goals of Franchise Due Diligence
   A. Due Diligence—Generally
   B. Analysis of System and Assets
   C. Buyer and Seller Due Diligence
   D. Timing
II. Overlap with General Corporate Issues; Coordinating with Other (Usually Corporate) Counsel
   A. Educating Other Counsel
   B. Coordinating Document Review and Purchase Agreement Drafting
   C. Reliance on Seller’s Representations When Buyer Does Its Own Due Diligence
III. Franchise-Specific
   A. Scope of Due Diligence
   B. Large Franchise System Due Diligence
   C. Due Diligence in Pre-Bid Situations
   D. Documents to Review
   E. Issues to Look For
   F. Due Diligence When Acquiring a Competing System
   G. Discussions with Franchisees or Franchise System Advisory Committees
IV. Franchise Related Due Diligence—Special Issues
   A. Purchasing and Supply Issues and Rebates
   B. Real Estate
   C. Financing
   D. Financial Reporting
   E. Antitrust Issues
   F. Intellectual Property
   G. Other Franchise-Related Issues
CONTENTS

V. International Franchise Issues in Due Diligence 116
   A. Type of Program 116
   B. The Foreign Master Franchisee or Developer 117
   C. Complying with Foreign Franchise and Other Laws 118
   D. Complying with U.S. Franchise Laws 118
   E. Complying with Other U.S. Laws 119
   F. Master Franchise Issues 119
   G. Translations/Copyright Ownership 120
   H. Exit Strategy/Dispute Resolution 121
   I. Use of Local Counsel to Assist in the Review 122

VI. Technology-Related Issues in Due Diligence 122
   A. Data Rooms—Who Sets Them Up, Populates Data, and Organizes Them 122
   B. Technology Review Challenges 123
   C. Avoid “Post-Merger Discovery Surprises” 124

VII. Other Practical Aspects 124
   A. Visiting the Franchisor’s Offices 124
   B. Discussions with the Franchisor’s In-House or Outside Counsel 125
   C. Writing the Report 125
   D. The Risk to Counsel 126

VIII. Sample Due Diligence Lists 126

4 Real Estate Matters in Acquisitions and Mergers 129
Herbert A. Hedden and Judith L. Marsh

I. Introduction 129

II. Control of the Franchised Site 130
   A. Direct Control 130
   B. Indirect Control 134

III. Franchisor Liability for Site Selection 138

IV. Due Diligence 142
   A. Generally 142
   B. Review of the Leasehold Structure 143
   C. The FDD and the Franchise Agreement 144

V. Sample Acquisition Document Provisions 145
   A. Representations and Warranties 145
   B. Covenants 150
   C. Conditions to Closing 151

VI. Conclusion 153
5 Valuation of Franchise Companies

Richard Greenstein and Richard Morey

I. Concepts and Methods for Calculating Valuation of Franchise Companies
   A. Key Definitions
   B. Internal Rate of Return

II. Common Multiples of EBITDA for Franchise Company Deals

III. A Buyer’s Focus When Assessing Valuation
   A. Recent Growth
   B. Unit-Level Economics
   C. Quality of Earnings
   D. Characteristics of Franchisees
   E. Anticipated Revenue Streams
   F. Cost Reductions
   G. Unit-Level Performance
   H. Timing

IV. Strategies for Selling Franchisors to Maximize Valuation
   A. Hiring Professional Advisors
   B. Reducing Uncertainty
   C. Cost Cutting
   D. Data Rooms
   E. Company-Owned Units
   F. Potential for Growth
   G. Equity for Management
   H. Franchise Performance and Satisfaction

V. Structuring Issues Impacting Valuation
   A. Asset or Stock Purchase
   B. Distressed Sales
   C. Representations and Warranties
   D. Auctions
   E. Earn-outs
   F. Financial Benchmarks

VI. Conclusion

6 Income Tax Considerations in Acquisitions and Combinations of Franchise Businesses

Michael J. DeLaurentis and Will K. Woods

I. Introduction
II. Preliminaries 176
  A. Tax Treatment of Franchise Transfers in General 176
  B. Significance of Type of Entity—Basics 179
  C. General Considerations 180

III. Taxable Transactions 181
  A. Asset Sales 181
  B. Sales of Stock or Partnership Interests 193

IV. Tax-Deferred Transactions 198
  A. Corporate Reorganizations 198
  B. Cross-Border Reorganizations—I.R.C. 367 214
  C. Combinations Involving Noncorporate Parties 216
  D. The Inheritance of Corporate Traits 216

V. State Tax Considerations: Nexus 219

7 Trademark Considerations in Franchise Transfers 223
Christopher P. Bussert and William M. Bryner

I. Introduction 223
  A. What Are Trademarks? 223
  B. Why is Trademark Law Important to Franchise Transfers? 225
  C. Trademarks Distinguished from Patents, Copyrights, and Trade Secrets 225
  D. Domain Names and Cybersquatting 227
  E. Trademark Due Diligence 228

II. Trademarks Subject to the Transaction and Potential Encumbrances on Them 229
  A. Potential Sources of Trademark Rights 229
  B. Scope of Trademark Rights 231
  C. Loss of Trademark Rights 233
  D. Liens on Trademark Registrations 235
  E. Potential Infringement of Others’ Trademarks 235
  F. Infringement of the Seller’s Trademarks by Others 237
  G. Trade Dress Infringement 238
  H. Trademark Dilution 239
  I. Tools and Sources of Additional Information 240

III. Trademark Licenses 240
  A. Exclusive or Nonexclusive Licenses 241
  B. Control of Licensees 241
  C. Ownership of New Marks 242
  D. Challenging Infringement by Others 243
E. Advertising 243
F. Summary of Intellectual Property Provisions 243

IV. Valuation of Trademarks 244
A. How Much Would a Bank Loan on the Strength of the Trademark Alone? 244
B. Comparable Values 244
C. Cost of Developing and Promoting a Mark 244

V. Transfer of Trademark Rights 245
A. Transfer Agreement Terms Relating to Trademarks 245
B. Recordation 246

VI. Maintenance of Trademarks and Other Considerations 247
A. Continued Use and Incontestability Affidavits 247
B. Marking of Trademarks, Patented Items, and Copyrighted Works 247
C. Developing a Trademark Style Guide 248

VII. Conclusion 248

8 Acquisition of a Franchisor, or Its Assets, Through a Bankruptcy Proceeding 249
Glenn D. Moses

I. Introduction 249
A. Note on Due Diligence 250

II. Advantages of Chapter 11 Sales 250
A. Sales in Bankruptcy Are Generally Free and Clear of Liens, Claims, and Interests 250
B. Purchasers Have the Ability to “Cherry Pick” Favorable Contracts and Leases 251
C. Ability to Bind Dissenting Shareholders 252
D. Protection against Fraudulent Conveyance and Successor Liability Claims 252
E. Protection against Risk of Rejection of Sale Contract in a Subsequent Bankruptcy 253
F. Protection for the Seller’s Management and Directors 253

III. Choosing 363 Sales or 363 Plans 254
A. 363 Plans in General 254

IV. The 363 Sale Process 255
A. First Stage: Approval of Stalking Horse Agreement, Break-Up Fee, Bid Procedures, and Protections 256
B. Second Stage of the 363 Sale: Auction and Bankruptcy Court Approval 258

V. Assumption, Assignment, and Rejection of Contracts and Leases 260
   A. Conditions to Assumption or Rejection 261
   B. Timing of Assumption or Rejection 261
   C. Ability to Override Anti-assignment Provisions 262

VI. Acquisition through a Plan of Reorganization 263

VII. Particular Issues in Acquiring the Assets of a Franchisor in Bankruptcy 265
   A. Special Protections Granted to Licensees of Intellectual Property 266
   B. Section 365(n) in Practice 268
   C. What “Intellectual Property” is within the Scope of 365(n)? 269
   D. Are Trademarks Protected? 269
   E. The Issue of “Bundled Rights” 271
   F. Payment of Royalties under a 365(n) Election 272
   G. Can a 363 Sale Extinguish the 365(n) Rights of a Licensee under a Rejected IP Agreement? 273

VIII. Conclusion 274

9 INTERNATIONAL ISSUES 275

Jeffrey A. Brimer, Lucie Guyot, and Kenneth S. Levinson

I. Introduction to International Issues 275

II. Franchise Registration and Disclosure Requirements 275
   A. Application of U.S. Franchise laws 276
   B. Foreign Franchise Disclosure and Registration Laws 277

III. Transaction Structure and Due Diligence Issues 282
   A. Due Diligence Investigation 282
   B. Transaction Structure 284
   C. Corporate Governance Issues 286
   D. Valuation Issues/Currency Exchange and Risk/Exchange Controls 286
   E. Employment Law Issues 287
   F. Translation Issues 287

IV. Tax Issues 288
   A. Tax Issues Generally Affecting Structure of Transaction 288
   B. Franchising through Your Subsidiary vs. an Unrelated Entity 291
   C. Permanent Establishment/Tax Nexus Issues 294
D. Tax Issues Locally for Individuals Performing Certain Local Services 297
E. Withholding Taxes 298
F. U.S. Rules on Reporting Foreign Bank Accounts 302
G. Tax Issues in the Use of Flow-Through Structures 303
V. Dispute Resolution 305
   A. Litigation as Recourse: Hazards and Home Court Advantage Issues 306
   B. Types of Alternative Dispute Resolution 306
   C. Enforcement of Foreign Judgments and Awards 311
VI. Non-franchise U.S. Laws Affecting International Mergers and Acquisitions 311
   A. USA Patriot Act/Specially Designated Nationals and Blocked Persons 312
   B. Foreign Corrupt Practices Act 312
   C. Export Controls 316
VII. Foreign Laws Affecting International Mergers and Acquisitions 316
   A. Intellectual Property 317
   B. Data Privacy Laws 319
   C. Attorney-Client Privilege 320
   D. Securities Regulation 320
   E. Employment Law Issues 321
   F. Noncompetition Covenants 323
   G. Third-Party Approvals 324
   H. Antitrust Laws 325
VIII. Post-Merger Compliance Issues 330
IX. Working with Foreign Counsel and Foreign Parties 330
    A. Impact of Cultural Issues on Business Relationships 330
    B. Selecting Foreign Counsel 331
    C. Working with Foreign Counsel 332
    D. Negotiation of the Acquisition Agreement 332
X. Conclusion 333

APPENDIX A-1 335

APPENDIX A-2 343

APPENDIX B 349