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FRANCHISE LAW REMEDIES:
WHAT DO I WANT AND HOW DO I GET IT?

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I. WHAT DOES THE CLIENT WANT

For both parties to the franchise relationship, arriving at litigation is nothing less than a failure of their relationship. It is the last and least desirable option, and signifies the end of an arrangement that the parties had envisioned as being long term and profitable.

This program will discuss the different remedies available to the parties once they find themselves in litigation. If an injunction is sought, what must the claimant prove to establish a right to injunctive relief and what is the injunction’s permissible scope? If rescission, restitution or money damages is sought, what are the bases for seeking relief (breach of contract, fraud or statutory violations), and what are the possible defenses? What type of damages can be claimed (lost profits or liquidated, statutory, compensatory, or punitive) and how enforceable are damage limitations?

This program will discuss these various remedies and provide an analysis of the seminal cases updated by recent trends in case law.

A. Franchisor Objectives

Franchisor affirmative objectives often center on terminating a perceived wayward franchisee followed by enforcement of post termination provisions. These may include enjoining continued use of system trademarks, enforcement of non-compete and trade secret provisions, and turnover of telephone numbers, leases and equipment. Sometimes a franchisor does not seek termination, and instead seeks to compel performance or seek damages while maintaining the franchise relationship. After determination of client objectives, franchisor counsel will need to evaluate substantive law and evidence, as well as available remedies.

B. Franchisee Objectives

Franchisee affirmative objectives may vary from seeking to remain in the franchise system on termination or nonrenewal or, conversely, seeking to leave a failing franchise system to operate as an independent business or simply close up the business. In other situations franchisees may seek damages or restitution for losses suffered in their franchise business. As with franchisor counsel, after determination of client objectives, franchisee counsel likewise will need to evaluate substantive law and evidence, as well as available remedies.

II. REMNANTS OF LAW VERSUS EQUITY

Remedies in the American legal system emanate from centuries of English jurisprudence of law and equity. One treatise divides American legal remedies into three categories, as follows: “Specific relief remedies the wrong specifically, for example by returning the thing that was taken or ordering the performance that was expected. Substitutionary relief substitutes money for the specific relief. Declaratory relief tells people what their rights are, but orders no relief.”¹ Equitable relief is usually specific, but not always. Legal relief is most often substitutionary in awarding damages, but not always. “Equitable relief is recognized by the fact

¹ Robert Leavell, Jean Love, Grant Nelson, & Candace Kovacic-Flesischer, Equitable Remedies, Restitution and Damages, WEST PUBLISHING CO., 1 (5th ed. 1994).
that it is a court order to the defendant to do or not do something. Legal relief is recognized by the fact that ordinarily it is a judgment stating that plaintiff is entitled to something.\textsuperscript{2}

Equitable relief evolved from the Court of Chancery in medieval England nearly a millennium ago. Yet this jurisprudence still shapes franchise and other litigation today. In that era most courts in England administered the common law which over centuries evolved into limited forms of action often providing only damages rather than specific relief. Meanwhile the Chancellor received authority, as agent of the King, to grant alternative relief often premised on the inadequacy of legal remedies. Such equitable relief was designed to provide relief from unfair common law rules and judgments and led to such equitable remedies as injunctions, specific performance, rescission and restitution, and declaratory relief.

While equity claims are generally no longer heard in separate Courts, there are some remaining practical matters. First, equitable claims are generally not entitled to jury trials.\textsuperscript{3} However, some actions involve both equitable and legal claims, for which a jury trial is available only for the latter. Second, equitable claims still often examine the inadequacy of remedies or why legal damages do not provide an adequate remedy. Indeed certain equitable defenses may bar remedies including laches and unclean hands defenses. Ultimately equitable remedies may provide the desired result which damages cannot, i.e. for specific relief ordering a franchisor or franchisee to do something or, conversely, to not do something.

III. INJUNCTIVE RELIEF

Preliminary injunctive relief may be vital to both franchisors and franchisees at the outset. A franchisee may be facing termination and the loss of her entire business with preliminary relief. Conversely, a franchisor may need to address a rogue franchisee not paying royalties and serving unwholesome products—not only in breach of franchise agreement, but also in violation of local health codes and requirements. The requirements for such relief vary somewhat from federal to state courts. Further, counsel will initially need to determine what forum the action is likely to be filed in, or removed to, as determinative of the governing rules and applicable case law which will need to be cited.

A. Federal Law Standards

The standards for preliminary injunctive relief, as recently confirmed by the United States Supreme Court in \textit{Winter v. Natural Resources Defense Council},\textsuperscript{4} include four familiar elements. The moving party “must establish that he is likely to succeed on the merits, that he is likely to suffer irreparable harm in the absence of preliminary relief, that the balance of equities tip in his favor and that an injunction is in the public interest.”\textsuperscript{5}

Franchisors often seek preliminary injunctions under the Lanham Act to stop continued use of their trademarks by franchisees that have been terminated. A key issue in such motions

\textsuperscript{2} Id.

\textsuperscript{3} The Seventh Amendment to the United States Constitution preserves the right to jury trial only “[i]n Suits at Common Law.” U.S. Const. amend. VII.


\textsuperscript{5} Id. at 20.
is whether the franchisor has established a proper termination.\textsuperscript{6} When the franchisor has established a likely proper termination, an injunction usually issues.\textsuperscript{7} But when the termination is questionable, then a preliminary injunction for the franchisor is less likely.\textsuperscript{8} Franchisees, on the other hand, typically seek preliminary injunctive relief to stop terminations or non-renewals.\textsuperscript{9} On occasion both parties may file dueling preliminary injunction motions.\textsuperscript{10}

The element of irreparable harm for many years was cited by franchisors arguing that “damages constituted an adequate remedy”\textsuperscript{11} for franchisees seeking injunctive relief. Increasingly, however, courts have recognized the loss of a long term franchise business, through asserted wrongful termination or nonrenewal, can constitute irreparable injury.\textsuperscript{12} A federal district court enjoining a franchisor from terminating a hotel franchisee described the irreparable harm as follows:

Irreparable harm can generally be assumed where a franchisor is attempting to terminate an exclusive franchise arrangement on short notice. By the nature of the exclusive arrangement, the franchisee’s business operation depends upon the economic relationship established by the franchise agreement. The franchise relationship is the lifeline of the franchisee’s business; the franchisee’s investment of capital, time and effort in promoting the franchisor’s goods and services - to the general exclusion of competing goods and services – would be irreparably lost upon termination. Money damages cannot make the franchisee in such situations whole.\textsuperscript{13}

There is diverging authority in other states, however, that franchisees are not entitled to injunctive relief to mandate that the franchisor permit continued operation. For example, in Florida franchise agreements are considered personal services contracts; thus, they “are not subject to a suit for specific performance, which would be the result of injunctive relief.”\textsuperscript{14}

\textsuperscript{6} Typically, a franchisor must establish the termination was proper as a condition to injunctive relief. \textit{See, e.g.}, \textit{McDonald’s Corp. v. Robertson}, 147 F.3d 1301 (11th Cir. 1998).


\textsuperscript{8} \textit{Robertson}, 147 F.3d 1301; \textit{DeLaria v. KFC Corp.}, BUS. FRANCHISE GUIDE (CCH) ¶ 10,667 (D. Minn. 1995).


\textsuperscript{11} \textit{Id.} Some courts, however, now question the tautological nature of this argument. \textit{Bray v. QFA Royalties, LLC}, 486 F. Supp. 2d 1237, n.7 (D. Colo. 2007).


\textsuperscript{14} \textit{Burger King Corp. v. Agad}, 911 F. Supp. 1499, 1506-07 (S.D. Fla. 1995) (holding that the court may not order parties to continue the performance of a franchise relationship); \textit{Burger King Corp. v. Weaver}, 798 F. Supp. 684 (S.D. Fla. 1992); \textit{contra Husain}, 205 Cal. App. 4th. 860.
Permanent injunctive relief involves the same elements as preliminary injunctive relief except the moving party must have prevailed on the merits. Such relief for franchisors is “the remedy of choice for trademark and unfair competition cases since there is no adequate remedy at law for the injury caused by the defendant’s continuing infringement.” Franchisees have obtained permanent injunctive relief, for example, enjoining termination of the franchise agreement.

B. State Law Standards

State law standards for preliminary injunctive relief tend to focus on two main considerations: likelihood of prevailing on the merits and balancing of harms or equities in granting or denying preliminary relief.

C. Practice Pointers

Franchisors typically seek injunctive relief for trademark infringement, misuse of trade secrets, violations of non-compete provisions, and breach of post termination provisions such as return of manuals and telephone lines. Preliminary Injunction relief seeking to enjoin continued use of trademarks by a terminated franchisee is common. A key to obtaining such relief is the franchisor establishing a likelihood of prevailing on the merits of the termination.


16 Agad, 911 F. Supp. at 1509-10 (citing Century 21 Real Estate Corp. v. Sandlin, 846 F. Supp. 1175, 1180 (9th Cir. 1991)).

17 LaGuardia Assocs., 92 F. Supp. 2d at 131; see also Mahroom, 2009 WL 248262.


Conversely when a franchisee establishes that the termination may have been wrongful, a preliminary injunction for the franchisor will likely be denied.23

A strong showing of franchisee misconduct by the franchisor led to reversal of a preliminary injunction favoring the franchisee to a preliminary injunction favoring the franchisor in a cookie franchise system.24 On review of the evidence, Justice Posner of the Seventh Circuit Court of Appeals found the merits strongly favored the franchisor in terminating the franchisee: the franchisee had repeatedly made late payments, bounced checks to the franchisor, underreported sales, and failed inspections including with oozing cheesecake and runny brownies. The balance of harms was likewise found to favor the franchisor since the franchisee wrongly used non-approved batter and products which it then passed off as franchised branded cookies.

Franchises typically seek injunctive relief to enjoin a termination or failure to renew a franchise agreement.25 A preliminary injunction favoring terminated franchisees was granted protecting franchisees who served as the officers of a sandwich franchisee association.26 The franchisee association maintained a website and had posted therein the suicide note of a former franchisee who had killed himself following protracted litigation with the franchisor. In response, the franchisor terminated all the Association Board members assertedly for harming the goodwill and marks of the franchisor. But the franchisee Board Members established a likelihood of prevailing on the merits of wrongful termination, and that the harm to the franchisees of losing their business outweighed the franchisor’s claimed injuries.

Bonds are generally required on the grant of a preliminary injunction to protect the enjoined party for wrongful injunction.27 Courts vary on the amount of bond required, and sometimes do not require a bond despite the statutory requirement.28

IV. DECLARATORY RELIEF

Federal courts may grant declaratory relief pursuant to the Declaratory Judgment Act.29 The statute provides district courts with substantial discretion in granting declaratory relief, i.e.,


24 Original Great Am. Chocolate Chip Cookie, 970 F.2d at 276.


26 Bray, 486 F.Supp.2d 1237.

27 FED. R. CIV. P. 65(c); TGI Friday's, 652 F. Supp. 2d at 773; see generally Elliot R. Ginsberg, A Secure Handle on the Requirement of a Bond for a Preliminary Injunction, 31 FRANCHISE L.J. 15 (2011).


district courts “may declare the rights and other legal relations of any interested party.”\textsuperscript{30} Thus, a
district court may grant declaratory relief when there is a substantial controversy with sufficient
immediacy to warrant the relief.\textsuperscript{31} But a court will not grant declaratory relief for future or
contingent acts.\textsuperscript{32} Nor will a court grant declaratory relief if the issues are already being directly
adjudicated in the litigation.\textsuperscript{33}

The Uniform Declaratory Judgments Act is instructive:

Courts of record within their respective jurisdictions shall have power to declare
rights, status, and other legal relations whether or not relief is or could be
claimed. No action or proceeding shall be open to objection on the ground that a
declaratory judgment or decree is prayed for. The declaration may be either
affirmative or negative in form and effect; and such declaration shall have the
force and effect of a final judgment. . . \textsuperscript{34}

Declaratory relief has been upheld in actions seeking to confirm that the termination of a
franchise agreement was proper.\textsuperscript{35}

V. SPECIFIC PERFORMANCE

The equitable remedy of specific performance allows courts to mandate continued
performance of specific franchise agreement provisions. A typical action for specific
performance might involve a franchisee seeking relief for a franchisor refusing to allow renewal
as specified in the franchise agreement.\textsuperscript{36} Franchisors, on the other hand, might seek specific
performance of buyout and non-compete provisions following franchise termination.\textsuperscript{37} The
specific performance decree need not be identical to the contract terms as courts of equity may
alter performance as justice requires.\textsuperscript{38}

For many years, franchisors defended specific performance injunction actions by arguing
that courts should not engage in continuous supervision of franchise agreements nor enforce


\textsuperscript{31} Medimmune, Inc. v. Genentech, Inc., 549 U.S. 118 (2007); Wilton v. Seven Falls Co., 515 U.S. 277, 286 (1994);

\textsuperscript{32} McDonald’s Corp v. Rocky Mountain McDonald’s Inc., 590 P.2d 519 (Colo. App. 1974).

\textsuperscript{33} Postal Instant Press v. Jackson, 658 F. Supp. 739 (D. Colo. 1987); compare Astral Health & Beauty, Inc. v. Aloette

\textsuperscript{34} Wis. Stat. § 806.04 (2013).

\textsuperscript{35} DUFresnoe’s Auto Serv., Inc. v. Shell Oil Co., 192 F.2d 920 (9th Cir. 1993); Arco Prods. Co. v. Stewart & Young
Inc., 50 F. App’x 336 (9th Cir. 2002).

\textsuperscript{36} Prudence Corp. v. Shred-It Am., Inc., 365 Fed. App’x 859 (9th Cir. 2010); see also, Mahroom, 2009 WL 248262.


\textsuperscript{38} Prudence Corp., 365 Fed. App’x. at 861 (citing Restatement (Second) of Contracts § 358(1) (1981)).
personal services contracts. Courts are now increasingly rejecting such arguments, and ruling instead that franchise agreements are subject to specific performance in favor of franchisees. In addition, franchise relations statutes sometimes support specific performance of franchise agreement transfers.

VI. RESCISSION, RESTITUTION AND ANCILLARY RELIEF

A. Common Law

Rescission of a franchise agreement ending the parties relationship may be an available remedy following a material breach of the franchise agreement.

B. Statutory

Numerous franchise statutes, commencing with the California Franchise Investment Law, provide a statutory right of rescission. Many of these statutes require willful violations for rescission, but willfulness usually requires only establishing that the franchisor had a purpose or willingness to commit the violative act. Decisions are split on whether equitable defenses, such as unclean hands, apply to statutory rescission actions.

C. The Trilogy: Rescission, Restitution and Ancillary Relief

In order to obtain rescission of contract, many courts require the rescinding party to return the consideration received. But this requirement is equitable and not absolute. Other courts evaluate timeliness in requesting rescission, and, for example, declining rescission when a franchisee waited two years after purchase to seek rescission against a franchisor which had failed to register its franchise offering.

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47 Id.
48 Clapp v. Peterson, 327 N.W.2d 585 (Minn. 1982).
In many jurisdictions relief for rescission includes not only restitution of consideration provided but also consequential damages, i.e. rescission includes complete relief to make the aggrieved party whole.\(^{49}\) Thus a rescission grant to a franchisee, which purchased an unregistered franchise, properly included an award of franchise, royalty and advertising fees paid by the franchisee as well as franchisor profits for required purchases of spice, dough and other products.\(^{50}\) In granting this equitable remedy, the courts may adjust the equities including to avoid duplicative recovery.\(^{51}\)

A representative case involving appropriate relief in a rescission action of a franchise dispute is \textit{Runyan v. Pacific Air Industries}.\(^{52}\) The trial court granted rescission in favor of the franchisee following evidence of inadequate training and support by the franchisor of an aerial surveying and photogrammetric services. The California Supreme Court affirmed the trial court rescission award to plaintiff franchise to restore the status quo ante consisting of: (1) the initial $25,000 franchise fee; and (2) the loss of franchisee income while operating the franchise based on former employment salary of the plaintiff franchise who resigned the employment in reliance on the franchise agreement.\(^{53}\) The court noted the equities were appropriately adjusted by netting out business income to the franchisee prior to rescission which the plaintiff franchise received while trying to operate the franchise business prior to rescission.\(^{54}\) Finally the California Supreme Court lucidly explained the remedy difference between the legal action for breach of contract and the equitable action for rescission of contract.

Thus the damages available under each remedy are different. The award given in an action for damages compensates the party not in default for the loss of his expectational interest - the benefit of his bargain which full performance would have brought. Relief given in rescission cases - restitution and in some cases consequential damages - puts the rescinding party in the status quo ante, returning him to his economic position before he entered the contract.\(^{55}\)

**VII. DEFENSES TO EQUITABLE RELIEF**

The affirmative equitable defenses include unclean hands, laches, and numerous other defenses available generally such as fraud and waiver. Thus, a franchisor or franchisee which has acted improperly may be denied equitable relief under the doctrine of unclean hands.\(^{56}\) The doctrine applies when the unclean conduct relates to the plaintiff’s pending claims, rather than


\(^{50}\) \textit{Little Caesar Enters., Inc. v. OPPCO, LLC, BUS. FRANCHISE GUIDE (CCH) ¶11,897} (6th Cir. 2000).

\(^{51}\) Id.

\(^{52}\) Runyan, 2 Cal. 3d 304.

\(^{53}\) Id. at 318.

\(^{54}\) Id. at 316.

\(^{55}\) Id.

\(^{56}\) \textit{Dunkin Donuts of Am., Inc. v. Middletown Donut Corp.}, 100 N.J. 166 (N.J. 1985).
for general character evidence of bad behavior.\textsuperscript{57} Laches involves excessive delay in proceeding causing detriment to the other party and is less common in franchise actions.\textsuperscript{58}

An illustrative case of equitable defenses involved the termination of a donut franchise.\textsuperscript{59} The franchisee was terminated following determination that the franchisee had underreported sales with over $100,000 in royalties not being paid. The lower courts decreed that termination of the franchise agreement was proper but required the franchisor to pay the balance of the value of the franchises to the franchisee beyond the underreported royalties. The New Jersey Supreme Court reversed due to the franchisee’s affirmative misconduct resulting in contract specified termination and forfeiture. As the contract at law specified for termination and forfeiture, these provisions would not be disturbed by a court of equity in “the absence of fraud, accident, mistake, duress, or undue influence.”\textsuperscript{60}

\textbf{VIII. DAMAGES}\textsuperscript{61}

Damages are, of course, the most basic of remedies and in some cases may be the only remedy available to make an injured party whole. Different measures of damages apply for different claims including contract damages, tort damages, and statutory damages. Counsel also need to address evidence to properly establish damages including the need for expert testimony in some cases.

\textbf{A. Contractual Damages}

1. \textbf{General Principles}

Traditional contract law recognizes and protects the injured party’s expectancy, reliance, and restitutionary interests in the bargain,\textsuperscript{62} with expectation damages serving as the most common remedy for breach of a franchise agreement. Lost profits, of course, are the most common measure. Courts may award reliance damages when the non-breaching party’s primary injury is the loss of expenditures paid out by a party who assumes the contract will be performed. These are more commonly awarded on promissory estoppel and other quasi-contract claims. Finally, courts will sometimes apply the equitable concept of restitution damages to assign ill-gotten gains from the breaching party to the non-breaching party. Each of these resulting money damages remedies is examined in more detail below.


\textsuperscript{58} Wetzel’s Pretzels, LLC v. Johnson, 797 F. Supp. 2d 1020, 1029, n.4 (C.D. Cal. 2011) (one year delay of franchisor seeking relief not a bar to preliminary injunction).

\textsuperscript{59} Id.; see generally Kerry L. Bundy and Scott H. Ikeda, How Waiver, Modification, and Estoppel May Alter Franchisee Relationships, 30 FRANCHISE L.J. 3 (2010).

\textsuperscript{60} Id; Middletown Donut, 100 N.J. at 186.

\textsuperscript{61} Portions of §VIII are an update of a paper previously co-authored by Michael Joblove’s firm, Jonathan Perlman, Heather Carson Perkins & Andra Terrell, Availability and Probability of Damages in Franchise Litigation (43rd Annual IFA Legal Symposium). Also, for further discussion on damages, see Christopher P. Bussert, Robert M. Einhorn & Christopher Martinez, Calculating and Proving Damages in Franchise Termination Cases, ABA FORUM ON FRANCHISING (2008).

\textsuperscript{62} See Bausch & Lomb v. Bressler, 977 F. 2d 720, 729 (2d Cir. 1992) (discussing each of the three principle contract remedies).
2. **Expectation Damages**

Expectation damages are just that; damages awarded to compensate the non-breaching party for what it "expected from breaching party," had the breaching party performed.\(^{63}\) In the franchise context, these typically constitute lost profits, both actual and future. Expectation damages, are the broadest form of compensatory damages.

Generally, the injured party must prove the value of the contract to the party, had the contract been fully performed and the actual and future loss that the party has suffered or will suffer due to the breach.\(^{64}\) Damages from the breach must be proven with reasonable certainty; speculative damages unsupported by sufficient evidence are not recoverable.\(^{65}\) Mechanical precision is not required with respect to such damages, as long as they are reasonably certain.\(^{66}\) The damages recovered must also have been reasonably foreseeable to the parties at the time the contract was made.\(^{67}\)

3. **Restitution Damages**

By contrast to expectation damages which intend to award the benefit of the bargain, restitution seeks to restore the parties to their pre-contract position.

Restitution damages attempt to measure the benefit conferred on the breaching party, rather than measuring profits the aggrieved party would have made. Restitution typically works in concert with rescission, an equitable remedy that severs the contractual relationship between


\(^{64}\) See Guzman v. Jan-Pro Cleaning Sys., Inc., 839 A.2d 504, 508 (R.I. 2003) ("It is well settled that a court may award damages for breach of contract to place the injured party in as good a position as if the parties fully performed the contract." (per curium) (internal quotations omitted)); Maytronics, LTD. v. Aqua Vac Sys., Inc., 277 F.3d 1317, 1321 (11th Cir. 2002) (affirming final judgment for plaintiff on an award of lost profits in part because they would make plaintiff whole and place it "in the same position it would have been but for [defendant's] failure to give reasonable notice" (internal quotations omitted)).

\(^{65}\) Restatement (Second) of Contracts § 352 ("Damages are not recoverable for loss beyond an amount that the evidence permits to be established with reasonable certainty."); see also Guzman, 839 A.2d at 508 (stating, "the amount of damages sustained from a breach of contract must be proven with a reasonable degree of certainty, and the plaintiff must establish reasonably precise figures and cannot rely upon speculation").

\(^{66}\) Medinol Ltd. v. Boston Scientific Corp., 346 F. Supp. 2d 575, 600 (S.D.N.Y. 2004) (citing a Second Circuit holding that "it is not always necessary for the aggrieved party to prove its damage with 'scientific rigor'; where a wrong has been done, the courts will endeavor to make a reasonable estimate of damages"); Bonelli v. Volkswagen of Am., Inc., 421 N.W.2d 213, 226 (Mich. Ct. App. 1988) ("The type of uncertainty which will bar recovery of damages is uncertainty as to the fact of the damage and not as to its amount... [since] where it is certain that damage has resulted, mere uncertainty as to the amount will not preclude the right of recovery."); DaimlerChrysler Motors Co., LLC v. Manuel, 362 S.W.3d 160, 191 (Tex. App. 2012) ("The amount of loss must be proven by competent evidence with "reasonable certainty"... but the rule regarding such proof is intended to be "flexible enough to accommodate the myriad circumstances in which claims for lost profits arise.").

\(^{67}\) Hadley v. Baxendale, 9 Exch. 341 (1854); Restatement (Second) of Contracts § 351; see also Medinol, 346 F. Supp. 2d at 599 (holding that under New York law there must be a showing that the particular damages were fairly within the contemplation of the parties to the contract at the time it was made); Hoai v. Sun Ref. & Mktg. Co., No. 87-2456-LFO, 1991 WL 530756, at *6 (D.D.C. May 2, 1991) citing the Restatement (Second) of Contracts § 351 and concluding that "[t]he proper test for such damages is whether the plaintiffs loss was foreseeable as a probable result of the breach").
the parties. Rescission and restitution are most effective when there has been a clean break – a substantial breach and repudiation of the contract – as opposed to a situation where the franchise relationship remains in effect. 68 While restitution and rescission remedies are available to and asserted by both franchisors and franchisees, more often than not it is franchisees who seek restitution and rescission. 69 Several state statutes provide a rescission remedy to franchisees when the franchisor fails to properly register or makes misleading statements in its registration statements. 70

A party cannot recover both restitution and expectation damages. While they may be pleaded in the alternative, the plaintiff will ultimately need to elect its remedy.

4. Lost Profits

The general rule is that lost profits will be allowed as an element of damages for breach of contract if the loss is proven with reasonable certainty and disallowed when they are determined to be uncertain or speculative. 71 Lost profits are commonly sought by franchisors to recover lost future royalties and advertising fund contributions when a franchise agreement is terminated prior to its expiration. 72

B. Consequential Damages

Consequential damages are those that are naturally and proximately caused by the commission of a breach, and those that reasonably could have been contemplated by the defendant at the time of the parties’ agreement. The principle underlying the recovery of consequential damages after rescission and restitution is to allow the parties to be restored to their former positions as much as possible, and to bring about substantial justice despite the inability to reproduce the status quo. 73 Consequential damages are generally limited to cases where the grounds for rescission involved some fault on the part of the nonrescinding party. 74 Since consequential damages result naturally from the defendant’s wrongful acts, the damage must be directly traceable to the wrongful act and result from it. 75 However, courts retain broad

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68 Christopher P. Busser, Robert M. Einhorn & Christopher Martinez, Calculating and Proving Damages in Franchise Termination Cases, at 3, ABA FORUM ON FRANCHISING (2008).

69 See, e.g., Cal. Corp. Code § 31300 (2013); Avcar Leasing Sys., 890 F.2d 165 (analyzing and explaining the basis for the franchisee’s claim for restitution).


71 T&S Distrib., L.L.C. v. Mich. Bell Tel. Co., No. 296257, 2012 WL 954274 (Mich. Ct. App. March 20, 2012) (“Damages for lost profits must be amenable to establishment with some amount of certainty beyond pure speculation...The kind of uncertainty that would be fatal to an award is uncertainty as to whether damages occurred at all; if that has been reasonably established, the jury may analyze what evidence there is to arrive at an amount to the best of its ability.”).

72 See, Postal Instant Press v. Sealy, infra Section X, for the current landscape of lost profits in the franchise context.


74 Id.; see generally Runyan, 466 P.2d 682 (granting consequential damages for loss of income, less gross income realized from franchise operation, after franchisee’s rescission of franchise contract).

75 In re Carroll, 464 B.R. 293, 320-21 (Bkrtcy. N.D. Tex. 2011) (where the officer of a franchisor makes misrepresentations to a potential franchisee, consequential damages may be recoverable; however, where the damage is not foreseeable or directly traceable to the officer’s wrongful acts, consequential damages are prohibited).
Courts may permit consequential damages even where there are damage limitation provisions in contractual agreements. For example, in Estate of Kriefall v. Sizzler USA Franchise, Inc., Sizzler Steakhouse was entitled to recover consequential damages from their meat distributor's breach of implied warranties in the parties' meat supply contract, notwithstanding the damages limitations provision.\textsuperscript{77}

Franchise agreements that do not expressly define terms such as “consequential damages” or “actual damages” may unintentionally permit parties to obtain consequential damages.\textsuperscript{78} In Bonanza Rest Co. v. Wink, where these terms were undefined, the court held that the franchisor’s lost future royalties could be labeled as “direct damages,” rather than “consequential damages,” by bypassing the Franchise Agreement’s consequential damages waiver.\textsuperscript{79} Conversely, an Ohio court held that where terms are ambiguous, a franchisor could not simply characterize lost profit damages as actual damages, thereby dodging the express terms of a License and Operations Agreement with its licensee.\textsuperscript{80} Where agreements have well-defined provisions, courts usually favor adhering to the terms of the freely entered contract.

C. Statutory Damages

Federal and state statutes also provide claims for damages, with the Federal Lanham Act the most prominent and frequent statute invoked by franchisors. Franchisees, on the other hand, often invoke state franchise investment and relationship laws and unfair trade practices laws providing for statutory remedies. Willful infringement of a franchisor’s trademark often triggers these statutory damages.\textsuperscript{81} Courts may award statutory damages in addition to other remedies where a party has committed more than one actionable breach of the agreement. For example, in La Quinta Corp. v. Heartland Props. LLC, liquidated damages were awarded against the franchisee due to its breach of the franchise agreement, in addition to trademark

\textsuperscript{76} CAL. CIV. PRAC. BUS. LITIG. § 30:32; see also JGR, Inc. v. Thomasville Furniture Indus., Inc., 830 F. Supp. 2d 358 (N.D. Ohio 2011) (holding that furniture distributor was not barred from seeking consequential damages from furniture manufacturer which breached oral contract by entering franchise agreement with rival distributor, causing original distributor to lose business and eventually close down; nevertheless, the case was remanded for further jury fact-finding proceedings).

\textsuperscript{77} 816 N.W.2d 853, 874 (Wis. 2012) (permitting consequential damages even with a limitation provision between the meat processor and restaurant franchisor, which stated that processor would not be liable for any incidental or consequential damages of whatsoever nature, since the provision applied only to express warranties contained in guaranty and did not mention implied warranties of merchantability).


\textsuperscript{79} Id.


\textsuperscript{81} U.S. Structures, Inc. v. J.P. Structures, Inc., 130 F.3d 1185 (6th Cir. 1998) (affirming the district court’s award of treble damages where, after franchise agreement was terminated for lack of payment, the defendants-franchisees admittedly continued to use the franchise trademarks); see also Luxottica Retail N.A. Inc. v. CAS-MAN, Inc., No. 1:10-CV-374, 2011 WL 672063, at *5 (S.D. Ohio Jan. 14, 2011) (holding that a court has considerable discretion in determining the proper amount to award in cases involving a franchisee’s unauthorized use of a franchisor’s trademarks).
infringement damages due to the franchisee operating post-termination. Statutory damages may also be awarded in the face of a franchise agreement's limitation of liability clause since contractual waivers limiting statutory damages may be found void for overriding public policy reasons.

Nevertheless, some jurisdictions force the plaintiff to choose between either proving actual damages or claiming statutory damages. Statutory damages "may serve completely different purposes than actual damages," but they have their limits; preventing plaintiffs from tactically choosing statutory damages with the misguided belief that they will obtain high damages without proof of loss.

D. Lanham Act Damages

The Lanham Act provides a private cause of action for trademark infringement and dilution. Specifically, it states that anyone who uses "any word, term, name, symbol, or device...or any false designation of origin" likely to cause confusion or deception in connection with any goods or services, "shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act." Additionally, the Lanham Act entitles the owner of a famous mark to an injunction, as well as other relief, against another person's commercial use of a mark or trade name that dilutes the distinctive quality of the famous mark.

The remedies provided for under the Lanham Act are found primarily in 15 U.S.C. §1117. Under Section 1117, a Lanham Act plaintiff can recover: (1) defendant's profits; (2) actual damages suffered by the plaintiff, and; (3) attorneys' fees and costs of litigation. It is important to note that a Lanham Act plaintiff may recover all three remedies. Additionally, a

82 603 F.3d 327, 344-46 (6th Cir. 2010); see also Gorenstein Enter., Inc. v. Quality Care-USA, Inc., 874 F.2d 431, 435 (7th Cir. 1989) (holding enhanced damages to be justified because the franchisee's continued use of the franchisor's trademark was "so deliberate," and their justifications "so weak," that "it might have been abuse of discretion for the district court not to have awarded...treble damages").

83 Lift Truck Lease & Serv. v. Nissan Forklift Corp., N.A., No. 4:12-CV-153 CAS, 2013 WL 3092115, at *2 (E.D. Mo. June 18, 2013) (holding that parties’ contractual limitation of liability clause did not bar statutory damages under the Missouri Franchise Termination Notification Act, § 407.410); see also Century 21 Real Estate LLC v. All Prof'l Realty, Inc., 889 F. Supp. 2d 1198, 1217 (E.D. Cal. 2012) (finding franchisee's use of franchisor's mark to be willful and in violation of the Lanham Act; 15 U.S.C. § 1117(b) is meant to punish violators, requiring the court to award treble damages unless it finds extenuating circumstances); VoiceStream Wireless Corp. v. U.S. Commc'ns, Inc., 912 So.2d 34, 38 (Fla. Dist. Ct. App. 2005) (stating that a party cannot waive liability imposed by statutory provisions that are intended to protect both the individual and the public).

84 Cont'l Cablevision, Inc. v. Poll, 124 F.3d 1044, 1049 (9th Cir. 1997).

85 Id.


Lanham Act plaintiff is entitled to enhanced reparations in the form of treble damages where there is evidence of counterfeiting or intentional use of “a mark or designation, knowing such mark or designation is a counterfeit mark...in connection with the sale, offering for sale, or distribution of goods or services.”  

In the franchise context, courts have awarded treble damages where the infringement was intentional. For example, in Century 21 Real Estate, LLC v. Destiny Real Estate Props., the court determined that a hold-over franchisee’s continued unauthorized use of a franchisor’s mark constitutes counterfeiting under the Lanham Act. Accordingly, the violation permitted the franchisor to obtain treble damages and attorneys’ fees under the Act. The court stated, “[i]f an unrelated entity had created an identical trademark and provided authorized goods or services (of the kind provided by the owner of the mark) under the mark, there would be no question that there was counterfeiting.” Additionally, courts have the ability, in their discretion, to award pre-judgment interest. In another trademark infringement case, Passport Health, Inc. v. Travel Med., Inc., a court decided not to award treble damages pursuant to the Lanham Act where the infringing franchisee’s infringement was not found to be “intentional or willful.” The parties entered into a franchise agreement, but it was terminated after the franchisee stopped making royalty payments. Nevertheless, the franchisee continued to use the franchisor’s name in its website URL. The franchisor was awarded damages in the amount of the franchisee’s gross profits for the months that it was infringing the franchisor’s marks; however, the court determined that a treble damages award would not be appropriate since the franchisee was trying to disassociate itself from the mark and was not deliberately trying to mislead its customers.

Courts balance several factors in determining the damages to award such as: “whether defendant was willful, negligent, or innocent; whether plaintiff suffered losses in any provable amount; whether there is proof of actual confusion of some customers; and whether defendant realized profits from its infringing actions.” Courts have the liberty to emphasize different factors according to the facts of a particular case, and have occasionally awarded monetary recovery on the rationales of preventing unjust enrichment and/or deterrence of defendant and

90 Id.
91 See, e.g., U.S. Structures, 130 F.3d at 1191-92; Babbit, 38 F.3d at 1183; see also Pearle Vision, Inc. v. Star Vision Centers, Inc., No. 08-00046-CG-C, 2008 WL 2329196 (S.D. Ala. June 3, 2008) (noting that where infringement was intentional, court was “required” to treble damages, as well as award attorneys’ fees unless the court finds extenuating circumstances).
93 Id.
94 Babbit, 38 F.3d at 1183.
96 Id.
97 Id. at *7.
98 5 J. THOMAS MCCARTHY, MCCARTHY ON TRADEMARKS AND UNFAIR COMPETITION, § 30:57 (2013 ed.).
E. Statutory Damages Invoked by Franchisees

Franchisees typically seek damages for disclosure, termination and under non-renewal state franchise statutes. However, very little case law exists under many of the state franchise statutes on the issue of damages. Counsel should address the statutory language as well as the purpose of seeking appropriate relief under these statutes. Thus, disclosure statutes may provide for damages upon actual reliance rather than justified reliance upon franchisor misrepresentations on the sale of a franchise.\(^\text{100}\)

Available statutory damages remedies typically include damages caused by the violation of the statute.\(^\text{101}\) Under some statutes, rescission is available as a remedy and may provide for not only return of the consideration paid to the franchisor but also losses suffered by the franchisee in reliance on the franchise investment.\(^\text{102}\) State Little FTC Acts and Unfair Trade Practices statutes sometimes provide for double or treble damages.\(^\text{103}\) Finally, willful violations of state statutes in some but not all states may allow a franchisee to seek punitive damages.\(^\text{104}\)

F. Tort Damages

Tort damages are also among the remedies sought in a franchise dispute with tortious interference and fraudulent inducement claims among the most prevalent. Often franchisees will assert claims of tortious interference against a franchisor, claiming intentional invasion of, or interference with, their economic or contractual rights.\(^\text{105}\) Only third parties or strangers to the contractual relationship may be liable for tortious interference, protecting a franchisor from liability in a contract between itself and a franchisee (or vice versa).\(^\text{106}\) A plaintiff in a franchise relationship cannot sustain a claim for intentional interference with a prospective economic advantage based on conduct governed by the contract.\(^\text{107}\) Nevertheless, a franchisee’s claim for

\(^{99}\) Id.


\(^{102}\) Id.

\(^{103}\) See, e.g., Smith v. Strickland, BUS. FRANCHISE GUIDE (CCH) ¶ 10,422 (S.C. Ct. App. 1994); Akers v. Bonifasi, BUS. FRANCHISE GUIDE (CCH) ¶ 8,614 (M.D. Tenn. 1985).

\(^{104}\) See, e.g., Mac Tools, Inc. v. Griffin, BUS. FRANCHISE GUIDE (CCH) ¶ 10,569 (Idaho 1994).

\(^{105}\) 62B AM. JUR. 2D PRIVATE FRANCHISE CONTRACTS § 270 (2013 ed.).

\(^{106}\) Id. at § 272.

\(^{107}\) See Manhattan Motorcars, Inc. v. Automobili Lamborghini, S.p.A., 244 F.R.D. 204, 220 (S.D.N.Y. 2007) (stating that in order to maintain a claim for fraud when there is a contract between the parties, the plaintiff must allege either a legal duty separate and apart from the contractual duty to perform, a fraudulent representation collateral or extraneous to the contract, or special damages proximately caused by the fraudulent representation that are not recoverable under the contract measure of damages); JRS Prods., Inc. v. Matsushita Elec. Corp. of Am., 115 Cal. App. 4th 168 (2004) (holding that a franchisee may only recover contractual damages when its claim was based essentially on conduct within the contract, and franchisor terminating the contract without good cause did not change the essential nature of the claim); Tom Pappas Toyota, Inc. v. Toyota Motor Distrib., Inc., 729 F. Supp. 71, 72-73 (E.D. Mo. 1990) (holding that the franchisee was not entitled to recover punitive damages under the Missouri Motor
tortious interference against its franchisor may be treated like any other claim against an intervenor in the franchisee’s relationship with its customers or others.\textsuperscript{108} Parties may also recover where the conduct underlying the tortious interference claim is different than contemplated by the contract.\textsuperscript{109}

In \textit{Getty Petroleum Mktg., Inc. v. 2211 Realty, LLC}, a gasoline dealer effectively proved that its supplier intentionally reduced and terminated gasoline deliveries to interfere with their relationship with their customers and cause them financial harm. Even though the allegations of tortious interference were not detailed or specific in providing the identities of the customers, the dealer was successful in demonstrating that the supplier knew of the dealer’s relationship with its customers, and that its actions intended to interfere with customer relations. The court determined that the interference was deserving of tort damages.\textsuperscript{110}

A franchisor may also have a claim against a franchisee for tortious interference. In \textit{NBT Assocs., Inc. v. Allegiance Ins. Agency CCI, Inc.}, the franchisor alleged that two of its franchisees began diverting commission away from the franchisor’s trust account and stopped paying their royalties and advertising fees.\textsuperscript{111} The franchisor claimed that the franchisees were violating the franchise agreement at the behest of their third party silent partner, leading the court to find an issue of material fact regarding whether the partner had tortiously interfered with the franchise relationship.\textsuperscript{112}

Fraud may in certain circumstances be an appropriate remedy in the franchise context, although not where the contract covers the subject matter at issue. In \textit{Ayu’s Global Tire, LLC v. Sumitomo Corp.}, the franchisee alleged that the franchisor fraudulently induced it into becoming a franchisee by falsely promising to sell tires at competitive prices and provide a sufficient supply of tires.\textsuperscript{113} The court agreed with the franchisor that no tort independent of the contract had been pled and found that the franchisor had fulfilled its obligations in the franchise agreement on each point. Further, the contract’s integration clause barred consideration of any allegedly inconsistent statements made before the agreement was signed.\textsuperscript{114}

On the other hand, courts may find that the evidence points to fraudulent inducement outside of the franchise agreement. In \textit{Cohen v. Roll-A-Cover, LLC}, a distributor successfully proved that its manufacturer fraudulently induced it into purchasing a distributorship by

\begin{footnotesize}

\textsuperscript{108} 62B Am. Jur. 2d Private Franchise Contracts § 272 (2013 ed.).


\textsuperscript{112} Id. at *13.


\textsuperscript{114} Id.

\end{footnotesize}
presenting a comprehensive marketing plan and business program that, at the time, the manufacturer knew, contained a myriad of “material untruths.” The evidence at trial demonstrated that Roll-A-Cover falsely represented that it had distributorships in Southeast Asia and Florida, when it actually had none, stated that it had delivery backlogs when it had only ever sold a small number of units, and claimed to hold six patents and four trademarks when it never had any registered intellectual property. The court affirmed the trial court’s judgment in favor of Cohen against Roll-A-Cover for fraud, fraudulent inducement, and intentional misrepresentation by clear, precise, and unequivocal evidence.

The economic loss rule also helps franchisors fend off franchisee fraud claims that develop out of franchise agreements. Although an independent tort could conceivably arise out of breach of contract in limited circumstances, it could not do so where the claims were not distinct from the primary breach of contract claim. Some courts will not allow fraud claims to proceed where all that existed was the failure to carry out a promise in contract.

In Beaver v. Inkmart, LLC, for example, the franchisee filed suit against the franchisor alleging fraudulent misrepresentation and inducement. Inkmart moved to dismiss the complaint arguing that the fraud-based claims were precluded by the terms in the franchise agreement and barred by the economic loss rule. The court stated that in Florida, “reliance on fraudulent representations is unreasonable as a matter of law where the alleged misrepresentations contradict the express terms of the ensuing written agreement.” Accordingly, the court found that the claims relating to the fraudulent inducement of the franchise agreement were barred under the economic loss rule, as the franchisee sought to recover purely economic damages based on oral representations concerning the heart of the franchise agreement.

However, the court found that the franchisees sufficiently plead fraudulent and negligent omissions, including that the franchisor willfully failed to include in the franchise disclosure document that the consultant hired by the franchisee to find a franchise opportunity was an

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116 Id. at 447-48.
117 Id. at 449.
119 Id.
121 Id.
122 Id. at *4.
123 Id. at *5.
Therefore, the omissions in the FDD did not relate to the essence and performance of the contract, and were not barred by the economic loss rule.\(^{125}\)

**G. Punitive Damages**

Punitive damages are an extraordinary remedy and are therefore permitted only under limited circumstances. Contrary to the purpose of compensatory damages, punitive or exemplary damages are not awarded as compensation to an injured party but are instead intended to punish a party and deter that party and others from engaging in similarly egregious wrongful acts in the future. In franchising context, punitive damages are most commonly awarded in actions involving a franchisor committing fraud in the sale of a franchise.\(^{126}\)

Each state has its own standard regarding the nature of conduct required in order to permit a punitive damages award. All require, however, a threshold level of willfulness and outrageous conduct in addition to the commission of a tort such as fraud.\(^{127}\) Some require that the conduct be “wantonly reckless” or “criminal.”\(^{128}\) Many states require that evidence in support of a punitive damages claim be supported by “clear and convincing” evidence.\(^{129}\)

Courts consider a number of factors in considering punitive damage awards, including (1) the defendant's financial condition; (2) the nature and reprehensibility of the defendant's actions; (3) the defendant's awareness of the amount of harm; (4) the duration of the conduct and the attempt to conceal the conduct; (5) the expenses the plaintiff suffered in an attempt to

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124 Id. at *4.

125 Id. at *5; see also Burger King Corp. v. Austin, 805 F. Supp. 1007, 1025 (S.D. Fla. 1992) (holding that damages are available only on showing that violation constitutes separate, independent tort and that defendant's conduct was willful, wanton, malicious, grossly negligent, oppressive, outrageous, deliberately violent, or demonstrated moral turpitude, insult, or fraud).


127 In Lithuanian Commerce Corp., Ltd. v. Sara Lee Hosiery, 219 F. Supp. 2d 600 (D.N.J. 2002), the court denied the manufacturer's motion for judgment as a matter of law on the plaintiff distributor's punitive damages claim. Testimony at trial included an executive of the defendant's statement regarding the distributor ("F&%k him, I don't give a s$&t about him") and that the executive knew that the product at issue (panty hose manufactured in Mexico) was not of the same specifications as U.S. manufactured panty hose. The court found that such evidence, if believed by a jury, evinces actual malice or wanton and willful disregard of the plaintiff's interests. Id. at 611. Moreover, the court found that plaintiff's release of legal claims, of dubious merit or not, in exchange for goods, the quality of which may have been intentionally misrepresented, is an example of the type of serious harm contemplated by New Jersey's Punitive Damages Act. Id.

128 Wirig v. Kinney Shoe Corp., 461 N.W.2d 374, 381 (Minn. 1990) (holding that Minnesota requires a finding of willful, wanton and malicious conduct or willful indifference); Midwest Home Distrib., Inc. v. Domco Indus. Ltd., Bus. FRANCHISE GUIDE (CCH) ¶ 11,495 (Iowa 1998) (willful and wanton conduct is only required such that the actor has intentionally done an act of an unreasonable character in disregard of a known or obvious risk that was so great as to make it highly probable that harm would follow, and which is usually accompanied by a conscious indifference to the consequences); Crues v. KFC Corp., Bus. FRANCHISE GUIDE (CCH) ¶ 8,135 (8th Cir. 1984) (under Missouri law, "actual malice, i.e. motivation by spite or ill will, is not a prerequisite to punitive damages; legal malice will suffice .... Thus, evidence that supports the elements of an intentional tort may also support the legal malice required for punitive damages."); see also Legacy Rests., Inc. v. Minn. Nighls, Inc., No. A11-1730, 2012 WL 3023397, at *2 (Minn. Ct. App. July 23, 2012) (stating that neither negligence nor gross negligence is sufficient to satisfy the deliberate-indifference standard required for punitive damages).

129 See, e.g., MINN. STAT. § 549.20, subd. 1(a) (2013).
recover losses; and (6) whether once the misconduct was known to the defendant, defendant took remedial action. 130 Most courts require that the punitive damage award bear a “reasonable relationship” to the actual damages incurred. 131 The United States Supreme Court has given mixed signals regarding whether a disproportionate punitive damages award raises constitutional issues under the Eighth and Fourteenth Amendments to the United States Constitution. 132

H. Liquidated Damages

It is sometimes advantageous to agree to liquidated damages as a remedy for any breach, especially with respect to the collection of future lost profits. The validity of liquidated damages provisions is a question of state law, which is far from uniform. Their validity in most states turns on “reasonableness,” which usually depends on individualized facts and circumstances. Liquidated damages provisions are unenforceable where they constitute a penalty. The Restatement (Second) of Contracts, § 356(1), adopted in most states 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. 133

Thus franchisors and franchisees may not stipulate to an agreed upon sum designed to punish a party who breaches their agreement.

In order to be enforceable, liquidated damages must constitute a reasonable approximation of compensation for the non-breaching party. 134 Two factors are key in determining their validity: (1) whether the amount fixed must be a reasonable approximation of the loss anticipated when the contract is made, and (2) the difficulty of proof of loss. 135 When the difficulty of proving loss is especially great, “considerable latitude is allowed in the approximation of anticipated or actual harm.” 136

130 Gibson v. Total Car Franchising Corp., 223 F.R.D. 265 (M.D. N.C. 2004) (applying Tennessee law, and noting that a punitive award trebling compensatory damages was not excessive).


133 Although not generally applicable to franchise agreements, Uniform Commercial Code § 2-718 has a similarly worded standard for liquidated damages provisions in contracts for the sale of goods.

134 RESTATEMENT (SECOND) OF CONTRACTS § 356, cmt. a.

135 Id. at cmt. b.

136 Id.
As noted, enforceability of these provisions varies based on different considerations applied by various states. For example, there is a difference among the states in considering the relevant time period for determining whether an approximation of damages would be difficult. Most courts focus on the reasonableness of the parties' prospective approximation of damages at the time they entered into the contract. Others indicate that the question should be re-visited at the time enforcement is sought. In *Kelly v. Marx*, a Massachusetts Court of Appeals labeled the different approaches “single look,” where the court confines its inquiry of reasonableness to the time of contracting, and “double look,” where the court examines the reasonableness of a liquidated damages provision at both the time of contracting and at the time of breach. The questions of who bears the burden of proving the enforceability of a liquidated damages clause also varies among the states. In most states, a party seeking to avoid a liquidated damages provision bears the burden of proof to avoid its enforcement. The rationale among these states is that the party “initially assented to the clause when [he or she] signed the agreement.” Other states place the burden on the party seeking enforcement of a liquidated damages clause “because the party seeking enforcement has the ‘most immediate access to the evidence on the issue of both (a) the difficulty of advance estimation of damages and (b) the reasonableness of the forecast.’” Colorado has adopted a hybrid approach where “the burden of proving that a liquidated damages clause constitutes [an unenforceable] penalty is on the party so asserting, unless it patently appears from the contract itself that the liquidated damages agreed upon are out of proportion to any possible loss.”

Minnesota bars such claims. The Minnesota Administrative Code provides that:

All franchise contracts or agreements and any other devise of practice of a franchisor, shall conform to the following provisions. It shall be unfair and inequitable for any person to...require a franchisee...to consent to liquidated damages.

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137 694 N.E.2d 869, 873–74 (Mass. Ct. App. 1998), rev’d, 705 N.E.2d 1114 (Mass. 1999). After surveying several opinions adopting each approach, the Massachusetts Court of Appeals adopted the double-look approach. Because no actual damages were incurred, the liquidated damages clause at issue amounted to an unenforceable- penalty provision. The Massachusetts Supreme Court later reversed that decision, holding that “a judge, in determining the enforceability of a liquidated damages clause, should examine only the circumstances at contract formation.” 705 N.E.2d at 1116–17.


142 Minn. R. 2860.4400(J) (2013).
Liquidated damage provisions have often been enforced in the franchise context.143

I. Limitation Of Damages

Inclusion of damage limitation provisions in franchise agreements can be valuable to franchisors in limiting their liability in a variety of contexts such as contract terms limiting consequential damages, barring punitive or treble damages, or liquidating damages. Courts will generally respect the damage limitation provisions in a franchise agreement unless the limitation is so one-sided or contravenes public policy, rendering the provision unconscionable. 144 A provision is substantively unconscionable if it has a lack of mutuality; however, this can sometimes be avoided if the provision contains even a degree of bilaterality.145 In Cognitest Corp. v. Riverside Pub'l'g Co., a damage limitation provision was enforced after the court determined its validity under the Uniform Commercial Code as a commercial agreement that provided for a minimum adequate remedy and resulted from substantial negotiation.146

A damages provision will also be unenforceable if it causes a party to the franchise agreement to have meaningless rights.147 In Jacada, Ltd v. International Marketing Strategies, Inc., after finding that the distributor breached the software distribution agreement it had with the software developer, the arbitration panel awarded damages to the distributor that far exceeded the agreement's limitation on damages.148 The arbitrators disregarded the provision after finding that it rendered the distributor's rights meaningless, and the Sixth Circuit affirmed their decision.149


145 Bridge Fund Capital Corp. v. Fastbucks Franchise Corp., No. 2:08CV00767-MCE-EBT, 2008 WL 3876341, at *7 (E.D. Cal. Aug. 20, 2008), affd. 622 F.3d 996 (9th Cir. 2010) (determining that the defendant, as the contract drafter, waived damages with the knowledge that it would likely be the defendant in future litigation, creating an unenforceable one-sided agreement aimed at limiting its liability).

146 107 F.3d 493, BUS. FRANCHISE GUIDE (CCH) ¶ 11,117 (7th Cir. 1997).


148 Id.

149 Id.
IX. EXPERTS AND PROOF OF DAMAGES

To recover damages, particularly lost profits, the injured party must prove the value of the contract to the party had the contract been fully performed, and the actual and future loss that the party has or will suffer due to the breach.\footnote{See Tel-Ex Plaza, Inc. v. Hardee’s Rests., Inc., 225 N.W.2d 794, 796 (Mich. Ct. App. 1977) (stating, “[t]he goal in awarding damages for breach of contract is to give the innocent party the benefit of his bargain - to place him in a position equivalent to that which he would have attained had the contract been performed.”); Roboserve, Inc. v. Kato Kagaku Co., 78 F.3d 266, 278 (7th Cir. 1996) (injured party entitled to recover amount that will put the party in as good a position as if the contract had been performed as agreed).} Damages from the breach must be proven with reasonable certainty; speculative or damages unsupported with sufficient evidence are legally insufficient and will preclude recovery.\footnote{Restatement (Second) of Contracts § 352 (“Damages are not recoverable for loss beyond an amount that the evidence permits to be established with reasonable certainty.”).} Once the evidence establishes that damages have indeed been incurred and are directly traceable to the defendant’s wrongful conduct, the injured party need not prove them with mathematical certainty so long as they are reasonably certain.\footnote{Belleville Toyota, Inc. v. Toyota Motor Sales, U.S.A., Inc., 770 N.E.2d 177, 199 (Ill. 2002) (holding that because lost profits are always uncertain to some extent and incapable of calculation with mathematical precision, lost profits do not need to be proven with absolute certainty).}

Courts exercise significant discretion in what they accept as reasonably certain proof. For example, in Days Inn Worldwide, Inc. v. Inv. Props. of Brooklyn Ctr. LLC, Days Inn entered a fifteen-year license agreement with a franchisee, but the franchisee terminated the agreement after only three years.\footnote{No. 10-609 MJD/JJK, 2011 WL 4538076 (D. Minn. Aug. 26, 2011) report and recommendation adopted, No. 10-609 MJD/JJK, 2011 WL 4537934 (D. Minn. Sept. 29, 2011).} Days Inn claimed it was entitled to $1,065,166 in lost future revenue, which represented what it would have expected to receive over the remaining twelve-year period on the license agreement. At issue was whether Days Inn had proven its claimed damages with the “requisite degree of certainty.”\footnote{Id. at *2.} To calculate its damages, it determined that during the last year it had received $101,717 from the property, for an average of $279 per day. It then multiplied the $279 figure by the remaining 4,505 days left on the license agreement. The court found that Days Inn’s calculation was not to a “reasonable degree of certainty,” reasoning that Days Inn had provided no proof “regarding the competitive market conditions in the relevant market since 2007, its historical accuracy in forecasting future revenue streams from franchised hotels, or its ability to forecast economic trends.”\footnote{Id. at *4-5.} The court noted that, in other contexts, a two-year time period is a reasonable measure of a franchisor’s damages for a breach of a franchise hotel agreement.\footnote{Id. at *5.}

A Tenth Circuit decision demonstrates that courts vary widely in what they accept as reasonably certain proof. In Century 21 Real Estate Corp. v. Meraj Int’l Inv. Corp., the franchisor challenged a trial award of lost profits to the franchisee alleging that the evidence was speculative and disproportionate.\footnote{315 F.3d 1271 (10th Cir. 2003).} Even though the franchisee’s only evidence of lost profits
was the testimony of its principal setting forth his own projections for the six years remaining on the franchise agreement at the time of termination, the franchisor provided no contrasting evidence in concluding that the amount was speculative. The Tenth Circuit held that the trial court had not grossly abused its discretion in letting the jury award stand and scolded the franchisor for doing almost nothing to undermine the franchisee’s assumptions at trial. The franchisor gave the jury almost no specifics with which to challenge or reject the projections, failed to call its own expert, and failed to meaningfully cross-examine the franchisee.

In *PSP Franchising v. Dubois* the court found that the franchisor, who terminated the franchise agreement due to the defendant franchisee’s material breaches, was entitled to collect future royalties owed under the agreement. The court concluded that where there is no reason to suspect, or evidence to suggest, that the agreement would not have been performed if the franchisees had not breached, and that the future royalties are owed pursuant to the franchise agreement. Similarly, in *American Speedy Printing Centers, Inc. v. AM Marketing, Inc.*, the franchisee argued that an award of future royalties to the franchisor, following the termination of the franchise for failure to pay royalties, was speculative because there was doubt that the franchisee would be able to continue operating the business in the future. The court concluded that in order to create uncertainty as to the fact of future royalties, the franchisee must produce evidence that the franchisee was likely to fail in some way, or become unprofitable, such that sales would end but without any breach of the franchise agreement. The court was likely swayed by speculative nature of the franchisee’s affidavit testimony regarding the franchise’s viability, and the lack of evidence regarding its imminent failure.

Establishing loss with reasonable certainty depends upon the circumstances of the particular case, but proof of past profits is the most common and accepted method. This can be a problem where the plaintiff is either a new business or was prevented from opening the business. Under various permutations of the traditional “New Business Rule,” courts have denied lost profits to plaintiffs as speculative where the business was new and there is no track record of past performance to gage the anticipated profits. Many jurisdictions, however, have abandoned a blanket prohibition on lost profit awards for a new business so long as there is a reasonable basis supporting the claim. When a reasonable estimate of damages is based on the profits of identical or similar businesses operating under substantially similar market conditions, recovery may not be barred.

158 Id. at 1282.

159 Id. at 1283.


161 Id.


163 Id.

164 See *Tex. Instruments, Inc. v. Teletron Energy Mgmt., Inc.*, 877 S.W.2d 276, 279 (Tex. 1994) (the “facts and circumstances of a particular case” dictate the determination of lost profits and the evidence required for proof is “intended to be flexible enough to accommodate the myriad circumstances in which claims for lost profits are made.”).

For example, in *No Ka Oi Corp. v. Nat'l 60 Minute Tune, Inc.*, the court held that the franchisee could seek a claim for lost future profits even though the franchisee had not sold or developed even one unit in its territory. The court expressly noted that "proof of the nationwide character of the franchise business at issue provided an ample basis for computation of probable losses." In *613 Fairview Ave., L.L.C. v. Pong's Corp., Inc.*, the plaintiff franchisee’s landlord blocked one of the business's entrances and its parking lot, resulting in a five-month delay in opening the new business. The franchisee's expert used financial data regarding similar franchisees of the same system, operating similar adult product retail formats to avoid the “new business rule.” The court noted that where a national franchise system is involved and the system engages in uniform advertising, quality control, data collection, etc., "[t]his sort of evidence is precisely what we deemed sufficient to provide a reasonable basis for estimating loss."  

On the other hand, some courts continue to apply the new business rule in the franchise context to preclude claims of lost future profits. In *Otis v. Doctor's Associates*, the court applied Illinois's new business rule to preclude a fast food development agent from recovering future profits because the franchise, "Cajun Joe's," was a start-up business venture. With a "brand new fast food franchise" there was no baseline against which to measure the post-breach lost profits.  

Experts are frequently used to prove damage from breach of the franchise agreement. In *Sherman St. Assocs., LLC v. JHT Tax, Inc.*, the court admitted testimony from expert witnesses to prove the franchisee's damages. The court observed that the plaintiff had admitted at his deposition that Cajun Joe's was a start-up venture that might very well fail and that the plaintiff’s attorney was unable to provide any principled reason why the new business rule should not preclude the lost profits claim; see also *McDevitt & St. Co. v. Marriott Corp.*, 713 F. Supp. 906, 933 (E.D. Va. 1989) (prohibiting Marriott from using profit information relating to other hotels to establish lost profits during the delay before opening a new hotel because it was undeniably speculative and based on too many changing market and economic conditions).
the former franchisee owner, who was also the accountant, regarding the calculated value of the franchisee's business for the purposes of proving damages.\textsuperscript{173} The court held that, because the franchisee owned the business and was also the accountant, the franchisee could testify as a lay witness under Federal Rule of Evidence 701 regarding his projected value of the business, including estimated future lost profits.\textsuperscript{174} The franchisor would have the opportunity to cross-examine the franchisee regarding the reliability of those calculations to undermine the testimony's weight.\textsuperscript{175}

An expert's valuation of a franchise whose calculations are not based on actual sales is likely to be excluded by the court. In \textit{Mercedes-Benz USA, Inc. v. Coast Automobile Group, Ltd.}, an automobile manufacturer sued a dealer for injunctive relief and damages.\textsuperscript{176} The Third Circuit affirmed the district court's exclusion of the defendant's expert testimony because the expert had made no computations based on Coast's actual sales. Instead, he accepted without question the assertion of Coast's owner-operator that Coast's vehicle allocations from 1995 to 1999 were unfair.\textsuperscript{177} The appellate court also held that the district court did not err when it excluded another expert report that purportedly calculated the value of Coast's franchise at the time of its termination but that was based wholly on the expert's unfounded analysis.\textsuperscript{178}

To the extent expert testimony is presented regarding damages, counsel should study the admissibility of the testimony under Rule 702 of the federal rules of evidence and \textit{Daubert} and its progeny.\textsuperscript{179} If damages testimony is not based on reliable principles and methods reliably applied to the facts of the case, then such testimony is at risk of being disallowed or stricken.\textsuperscript{180}

\section*{X. DEFENSES TO DAMAGES}

\subsection*{A. Postal Instant Press v. Sealy and Meineke v. RLB Holdings}

\textit{Postal Instant Press, Inc. v. Sealy} is of course the seminal case that called into question a franchisor's ability to recover future lost profits. The case had been one of first impression, not awarded the plaintiffs $16.4 million. There is no doubt that franchise practitioners will be watching as this case continues to unfold pending appeal.); see also, Kevin M. Kennedy, \textit{Use of Daubert and Its Progeny to Attack Lost Profit Claims}, 20 \textit{Franchise} L.J. 167 (2001).

\textsuperscript{173} No. 3:03-CV-1875 CFD, 2010 WL 4340444, at *2 (D. Conn. Oct. 25, 2010).

\textsuperscript{174} \textit{Id.} at *2.

\textsuperscript{175} \textit{Id.}

\textsuperscript{176} 362 Fed. App'x 332 (3d Cir. 2010).

\textsuperscript{177} \textit{Id.} at 334.

\textsuperscript{178} \textit{Id.}


\textsuperscript{180} Compare \textit{Alaska Rent-A-Car, Inc. v. Avis Budget Grp., Inc.} 709 F.3d 872 (9th Cir. 2013) with \textit{Sargon Enters., Inc. v. Univ. of S. Cal.}, 55 Cal. 4th 747 (2012).
only in California, but also the entire nation. Seventeen years later, *Sealy* is still the starting point for any discussion regarding a franchisor’s right, if any, to recover lost profits.

In *Sealy*, a franchisor of printing businesses (“PIP”), terminated the Sealy franchise agreement because the franchisee failed to pay royalty and advertising fees. At the time of termination, the franchise agreement had a remaining term of seven-and-a-half years. In its complaint, PIP sought lost future royalties and advertising fees for the remaining term as well as the unpaid past royalties, which were awarded by the trial court.

The California Court of Appeal reversed the lost future profits award, holding that in contract matters, the non-breaching party generally is entitled to recover only those damages—including lost profits—that are “proximately caused” by the specific breach. In *Sealy*, the Court of Appeal held that PIP’s lost profits, however, were not proximately caused by the Sealy breach, but were due to PIP’s intervening decision to terminate the parties’ franchise agreement.

The *Sealy* court qualified its holding, however, stating that a franchisor may be entitled to lost future royalties for a franchisee’s breach of a franchise agreement in certain circumstances, but “that entitlement depends on the nature of the breach and whether the breach itself prevents the franchisor from earning those future royalties.” However, the *Sealy* opinion fails to elaborate on any specific franchisee breaches that might qualify.

In addition, the *Sealy* court also found that the substantial future damages award obtained by the franchisor was improper given the nature of franchising. This alternate portion of the ruling has been forgotten by courts and commentators. The Court of Appeals ruled: “As a second independent and sufficient rationale for our reversal of the trial court’s “lost future profits award,” we conclude it would violate the statutory and common law prohibition of damages which are “unreasonable, unconscionable or grossly oppressive.”

In the time since *Sealy* was decided, there has been a general lack of consensus among courts nationwide as to the circumstances under which a franchisor is entitled to recover from a franchisee post-termination breach of contract damages for lost future profits. Several courts have allowed such damages when the franchisee terminates, repudiates, or abandons its franchise. The main area of disagreement has been in cases where the franchisor terminates after a default or breach by the franchisee.

While several courts have denied future damages in such situations, reasoning that the franchisor proximately caused its own future losses through its decision to terminate the franchise relationship, other courts have ignored *Sealy* and have awarded franchisors future damages even when the franchisor terminates and the franchisee has not repudiated, terminated, or abandoned. Among these is *Meineke Car Care Centers, Inc. v. RLB Holdings*,

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182 *Sealy*, 43 Cal. App. 4th at 1708.

183 *Id.*

184 *Id.*

185 *Id.* at 1713-14.
In *Meineke*, franchisee (“RLB”) and Meineke entered into four separate franchise agreements, each providing for a fifteen-year term. RLB closed each of its shops well before the end of the franchise agreement term. Upon learning of the shop closures, Meineke sent a default letter to RLB notifying them that their actions would be deemed breaches of the franchise agreements. Further, Meineke requested that RLB communicate its intent with respect to each of the closed shops. However, RLB did not reopen any of the shops. The lower court found that the franchisee had abandoned its shops prior to the expiration of the franchise agreement term, which the court concluded was a material breach. The court also found that franchisor terminated those agreements after efforts to persuade the franchisee to reopen the units. Notwithstanding these findings, the trial court denied the franchisor’s claim for future lost profits since the franchise agreement did not provide for future lost profits. The district court held that the franchise agreements did not entitle Meineke to recover future damages, and that Meineke failed to set forth a viable common law claim for future lost profits.

The Fourth Circuit reversed and remanded the lower court’s decision and held that lost future profits are recoverable even though the franchise agreements do not specifically provide for their recovery. Further, the court reasoned that, nothing in the franchise agreement expressly prohibits the recovery of lost future profits and that it was the franchisee’s breach, rather than the franchisor’s termination, that was the proximate cause of the lost future profits. The Fourth Circuit also concluded that, because the franchisor’s profits were derived from a percentage of the franchisee’s gross revenue, some profits were reasonably certain.

1. **Lost Profits Allowed**

Following *Sealy* and *Meineke*, courts across the nation appear to be split as to whether to allow the recovery of lost profits when the franchisor terminates the franchise relationship.

In *Hardee’s Food Systems, Inc. v. Hallback*, the Court examined both *Sealy* and *Meineke* while determining whether the franchisor was entitled to future lost profits. The franchisee, Hallback, began to lose money on its units and closed the restaurant with approximately 15 months remaining on the term of the franchise agreement. Subsequently, Hardee’s terminated the franchise agreement and then filed suit to collect expected future royalty payments. The franchisee argued that no provision in the agreement provided for recovery of future royalty fees, and that calculations to prove lost profits would be too speculative.

The court looked to *Meineke* for guidance, and determined that a breaching party can recover future lost profits and that the franchisee’s abandonment of the store was the proximate cause of any lost profits. The court also noted that the absence of an explicit contract provision

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186 423 F. App’x 274 (4th Cir. 2011).

187 Id. at 277.

188 Id. at 276.

189 Id.

providing for future damages did not preclude their recovery. Instead, the court found that genuine issue of material fact existed as to whether lost royalties in advertising fund contributions were reasonably contemplated by the parties at the time they entered into the agreement. However, most importantly, the court refused to adopt Sealy for the proposition that Hardee’s is not entitled to any future fees because it terminated the franchise agreement.

In Vino 100, LLC v. Smoke on the Water, LLC, the franchisees stopped making payments under their lease and franchise agreement. In turn, the franchisor terminated the franchise agreement and sought to recover damages for the remainder of the term under the franchise agreement. The franchisees argued that since the franchisor elected to terminate the franchise for non-payment of royalties, franchisor was the proximate cause of future lost profits. The court cited to Sealy and Hinton while analyzing the franchisees’ argument and stated that these courts reason that the franchisor would allow the contractual relationship to continue and bring suit against the franchisee for past-due payments. In citing Meineke, the court explained that in cases where a franchisee voluntarily abandons or terminates the business, courts have held that the franchisee’s decision to close the business caused the loss of future royalties. Ultimately, the court held that genuine issues of material fact existed as to causation for future royalty claims.

In Progressive Child Care Systems, Inc. v. Kids ‘R’ Kids International, Inc., an appellate court in Texas applied Georgia law in holding that a child care franchisor was entitled to future royalties it would have received but for the franchisee’s breach of the franchise agreement. In Progressive Child Care, the franchisee stopped making royalty payments for two child-care facilities based on their belief that the franchisor, Kids ‘R’ Kids, was providing poor organizational support. The franchisee also changed their name to Legacy Learning Center. As a result, Kids ‘R’ Kids sued the franchisee for, among other things, breach of contract. A jury returned a verdict in favor of Kids ‘R’ Kids and found that it had complied with the terms of the franchise agreements.

In holding that Kids ‘R’ Kids was entitled to lost future profits, the court in Progressive Child Care discussed Sealy, but ultimately distinguished it based on the Sixth Circuit’s decision in American Speedy Printing Centers, Inc. v. AM Marketing and a Pennsylvania case, Maaco Enters., Inc. v. Cintron. In rejecting the application of Sealy, the Progressive Child Care court performed the traditional contract law analysis under Georgia law, and held that lost profits were recoverable because they could be shown with reasonable certainty and were in the contemplation of the parties at the time the franchise agreements were entered into.

193 Id. at *4.
194 Id. at *1-4.
195 69 Fed. App’x. 692.
In *American Speedy*, the Sixth Circuit, applying Michigan law, awarded the franchisor lost future royalties. A print shop franchisee was terminated for failure to make the required monthly royalty payments and the franchisor was awarded lost profits/royalties. On appeal, the Sixth Circuit rejected the franchisee’s argument that lost future royalties were too speculative, saying that because the franchise contract does not provide for the termination of the contract by the franchisee in the absence of a material breach by the franchisor, any unilateral decision by the franchisee to end the franchise relationship would constitute a breach of the agreement, thereby entitling the franchisor to future profits.

In *Lady of America Franchise Corp. v. Arcese*, the franchisee voluntarily notified the franchisor of her desire to cease operation of her franchise. The franchisor sued for breach of contract and royalties for the remaining 111 months remaining on the parties’ franchise agreement and was awarded lost future royalties. The court held the franchisee’s decision to cease operation of the franchise was the proximate cause of the termination of the parties’ agreement and of the franchisor’s lost future royalties. In so holding, it rejected the franchisee’s claim that the franchisor’s letter confirming the franchisee’s termination meant the franchisor was responsible for the termination. The court reasoned that the franchisor’s notification merely confirmed the automatic termination, but that “it was not the vehicle for termination.”

In so holding, the court in *Lady of America* cited to another Southern District of Florida decision, *Burger King Corp. v. Barnes*, where the court dealt with the issue of whether and how much lost profits a franchisor was entitled to recover if the franchisee voluntarily abandoned the franchise before the expiration of the franchise term. BURGER KING® sought royalties for the entire 210 months remaining in the franchise term and estimated lost future royalties based on an average of the sales for the 29 months that the franchise was in operation. The court accepted BURGER KING®’s calculation and rejected the franchisee’s arguments that the amount was too speculative and that BURGER KING® has a duty to mitigate.

2. **Lost Profits Not Allowed**

In *Medical Shoppe International, Inc. v. TLC Pharmacy, Inc.*, the franchisor requested $748,029 worth of future license fees, constituting the present value of the license fees it expected to receive from the franchisee had the agreement run its full 20-year term. Under Missouri law, lost profits can only be obtained if they were within the contemplation of the parties at the time of the agreement. The court concluded that the franchise agreement

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198 69 Fed. App’x. at 693.
199 Id. at 698.
200 BUS. FRANCHISE GUIDE (CCH) ¶ 13,561 (S.D. Fla. 2006).
201 Id.
203 Id. at 1372.
204 No. 4:09CV00683 AGF, 2010 WL 2757328, at *1 (E.D. Mo. July 12, 2010).
205 Id. at *2.
proved neither party contemplated the payment of future license fees in the event of termination. The provision addressing the rights and obligations of the parties upon termination merely stated, “[a]ll...obligations which expressly or by their nature survive the...termination of this Agreement shall continue with full force and effect subsequent to and notwithstanding...its termination.” The court determined that future license fees were neither expressly stated, nor meant to survive the termination by their nature.

Conversely, in Burger King Corp. v. Hinton, Inc., the same judge as in Barnes considered the availability of an award of lost profits where the franchisor terminated because of the franchisee's failure to pay royalties. While the franchisee argued that Sealy should be applied, the Hinton court declined to apply Sealy because the franchise agreement contained a Florida choice of law provision. Nonetheless, the court in Hinton held, as did Sealy, that the franchisee's failure to pay royalty fees and other payments did not proximately cause the franchisor's loss of future royalty payments. The court also distinguished Barnes by pointing out that the franchisee in Barnes abandoned its franchise and, accordingly, the franchisee’s actions in Barnes did proximately cause the franchisor's loss of future profits. BURGER KING® also argued that it was entitled to future revenue because the franchisee “anticipatorily breached” the franchise agreement. The court dismissed this argument, finding that BURGER KING®’s claim was outside of the pleadings in the case.

Similarly, in Kissinger, Inc. v. Singh, the court held that a franchisor could not recover lost future royalties after terminating franchise agreement for failure to pay past royalties because it was the franchisor’s decision to terminate that is the proximate cause of the lost royalty payments.

B. Mitigation of Damages

Generally, a party injured by a breach of contract and seeking money damages has a duty to mitigate its damages. Several recent cases have addressed this issue in the context of lost future royalties. In Kiddie Academy Domestic Franchising LLC v. Faith Enterprises DC, LLC, the court noted that awarding the franchisor lost future royalties for the entire remaining eleven-year term would create an opportunity for a double recovery, given that the franchisor would have the ability to secure a replacement franchisee at some point during that period. As such, the court held that the franchisor was limited to recovering only lost future royalties

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206 Id.
207 Id.
208 Id.
210 Id. at 1366.
211 Id. at 1367.
213 See, e.g., Ebe et al., supra note 143, at 10.
from the time of termination until the date of judgment.215 Similarly in Days Inn Worldwide, the
court denied the franchisor from receiving twelve years of lost profits after the franchisee
prematurely terminated its franchise agreement and sold the hotel to a third party.216 The court
found that Days Inn presented no evidence that it had attempted to mitigate its damages by
finding another franchisee and opening another hotel in the same market.217 The court reasoned
that allowing Days Inns to obtain a judgment for its requested twelve-year income stream “would
be encouraging [Days Inns] to commit economic waste by putting forth no efforts to mitigate its
damages.”218

Radisson Hotels International, Inc. v. Majestic Towers, Inc., dictates that when a
franchisor terminates a franchisee for its breach, the franchisor may recover lost future profits,
including lost royalties if, at the time of contracting, it might reasonably have been foreseen by
the parties that loss of such profits would be the probable result of the franchisee’s breach.219 A
franchisor may not, however, recover future losses that a franchisee proves could have been
mitigated by installing a replacement franchisee, or otherwise could have been avoided, as
stated by the Restatement, without “undue risk, burden or humiliation.”220

As franchisors have a duty to mitigate their damages, franchisors and franchisees
should be prepared to present evidence relating to the franchisor’s ability and efforts to replace
the franchise business.221 This issue will benefit franchisees where the franchisor has been
unable to find a replacement franchisee over a multi-year period.222 In Rocky Mountain
Chocolate Factory, Inc. v. SDMS, Inc., evidence of a franchisor’s system success or failure in
the franchisee’s state or locality is more likely to resonate with the court than is evidence of the
franchisor’s viability nationwide.223

Finally the proper measure of damages in a lost profits case is generally lost profits, not
lost revenues. Thus, when a franchisor only establishes lost royalties but fails to present its
expenses in obtaining those royalties from a franchisee, it may be denied damages.224

215 Id.
216 BUS. FRANCHISE GUIDE (CCH) ¶ 14,756 (D. Minn. 2011).
217 Id.
218 Id.
219 488 F. Supp. 2d 953, 963 (C.D. Cal. 2007); Ebe et al., supra note 143, at 10.
220 RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981); 24 SAMUEL WILLISTON, FORESEEABILITY, A TREATISE ON THE LAW
OF CONTRACTS, § 64:27, at 193 (4th ed. 2002); Ebe et al., supra note 143, at 10.
221 Douglas R. Hafner & Logan W. Simmons, Lost Future Royalties: Lessons from Recent Decisions, 31 FRANCHISE
L.J. 150, 156 (2012).
222 Id.
224 E.g., id; Barnes, 1 F. Supp. 2d at 1370 (S.D. Fla. 1998).
C. Punitive Damages Limitations

In the franchise law context, the possibility of punitive damages surfaces in fraudulent inducement and tortious interference cases, where the wrongdoer’s actions are perceived as sufficiently reprehensible. Indeed, punitive damages are generally not available on breach of contract claims. These limitations on punitive damages are a function of the economic loss rule. Simply stated, in the absence of a tort independent of the contract, it is said that all economic losses must be redressed in accordance with the reasonable expectations of the parties, pursuant to their agreement. In nearly all jurisdictions, punitive damages are reserved for true tort cases (i.e., distinct from contractual performance). Permitting remedies beyond contractual expectations destroys the very purpose of contracting to manage risk by agreement.

In most cases, a jury decides whether, and in what amount, punitive damages should be awarded. The jury’s award will stand unless the award is irrational and excessive. Further, many states have statutes that “cap” the allowable award of punitive damages. Moreover, many states condition the availability of punitive damages on a finding of actual damage.

In BMW of America, Inc. v. Gore, the Supreme Court established three factors for appellate courts to use in determining whether punitive damage awards violate the Due Process Clause of the Fifth and Fourteenth Amendments as arbitrary or excessive: (1) the degree of reprehensibility of the defendant’s conduct; (2) the ratio between the damages plaintiff actually suffered and the punitive award; and (3) the difference between the punitive award and the civil penalties authorized in comparable cases. Moreover, in Cooper Industries, Inc. v. Leatherman Tool Group, Inc., the Supreme Court ruled that all appellate courts, both state and federal, must review all punitive damage awards under a de novo standard (i.e., without deference to lower court proceedings). In states that have no statutory cap on punitive damages, a defendant challenging such an award will be able to argue that the jury’s award is not final until an appellate court has independently ruled on the size of the award. Further, in State Farm Mutual Automobile Insurance Company v. Campbell, the Supreme Court held that the punitive award of $145 million was neither reasonable nor proportionate to the wrong committed, and it

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225 It has been held that a breach of the implied duty of good faith and fair dealing is a contract claim, and the general rule that punitive damages are unavailable in contract claims applies, precluding an award of punitive damages. Bonfield v. AAMCO Transmissions, Inc., 708 F. Supp. 867 (N.D. Ill. 1989).

226 Selle v. Tozser, 786 N.W.2d 748, 757 (S.D. 2010).

227 But see Robinson Helicopter Co. v. Dana Corp., 34 Cal. 4th 979 (2004) (finding that plaintiff should be compensated for its losses, and receive punitive damages from the seller of nonconforming helicopter clutches on the basis of its misrepresentation in the performance of its contractual obligations by knowingly issuing compliance certificates for the clutches to plaintiff; Robinson is an outlier case in awarding punitive damages on a contract).

228 Crues v. KFC Corp., BUS. FRANCHISE GUIDE (CCH) ¶ 8,135 (8th Cir. 1984).


was thus an irrational, arbitrary, and unconstitutional deprivation of the property of the insurer.\textsuperscript{233}

Punitive damages are also limited by contractual provisions entered into by the parties in their franchise agreement. Courts will enforce express, unambiguous waivers of punitive damages, when these waivers are not unconscionable or against public policy.\textsuperscript{234} Punitive damages waivers can be very effective and encompassing. In fact, they can be phrased to cover not only issues within the contract, but those arising out of or connected to the contract, and even other contracts.\textsuperscript{235} Franchisors are thus well advised to manage their risk with a punitive damages waiver provision; however, these provisions must be mutual.\textsuperscript{236}

\textsuperscript{233} 538 U.S. 408 (2003).


\textsuperscript{235} \textit{Dunkin' Donuts Franchised Restaurants LLC v. Manassas Donut Inc.}, No. 1:07CV446 (JCC), 2008 WL 110474 (E.D. Va. Jan. 8, 2008) (in granting the franchisor’s motion to strike the franchisee defendant’s demand for punitive damages, the court found that “the language of [the Agreement’s waiver provision] is broad enough to encompass all disputes between the parties, including those not arising out of their contractual relationship”).

\textsuperscript{236} \textit{IJL Dominicana S.A. v. It's Just Lunch Int'l, LLC}, No. CV08-5417-VAP, 2009 WL 305187 (C.D. Cal. Feb. 6, 2009) (finding that a punitive damages waiver was substantively unconscionable as it lacked mutuality, reasoning that a franchisor is more likely to be defending against punitive damages than seeking them); \textit{see also Gold v. Melt, Inc.}, No. B210452, 2010 WL 1509795, at *5 (Cal. Ct. App. Apr. 16, 2010) (holding that minimal evidence of procedural unconscionability was sufficient to require examination of substantive unconscionability).
XI. BIOGRAPHIES

MICHAEL D. JOBLOVE

Michael D. Joblove leads Genovese Joblove & Battista’s commercial litigation practice, which focuses on franchise, real estate, employment and securities litigation. In franchising, the Firm provides national franchise counsel to Burger King Corporation, which is headquartered in Miami, and handles Burger King Corporation’s litigation with respect to franchisees throughout the United States. Mr. Joblove also has represented numerous other franchisors, including Benihana, Jamba Juice Company, T.G.I. Friday’s®, Smoothie King, Bennigan’s®, Pearle Vision, Inc., Denny’s, Inc., Assist-2-Sell®, and Pollo Campero®.

Mr. Joblove is “AV” rated by Martindale-Hubbell and is a Fellow in the Trial Lawyer Honorary Society of the Litigation Counsel of America. Mr. Joblove is also listed in Best Lawyers in America and has been named the Best Lawyers’ 2011 Miami Franchise Lawyer of the Year. He has been ranked as one of the country’s leading franchise attorneys by Chambers & Partners USA, has been named as among Florida’s top attorneys by Florida Trend magazine and South Florida Legal Guide, has been recognized by Franchise Times magazine as one of the nation’s leading franchise attorneys, and is included as a “Super Lawyer” in the Florida Super Lawyers publication. In addition, Mr. Joblove has been selected by Who’s Who Legal, which describes him as a “stellar practitioner,” to appear in the “International Who’s Who of Franchise Lawyers” and the “International Who’s Who of Business Lawyers.”

Mr. Joblove is a lecturer before the American Bar Association (“ABA”) and the International Franchise Association (“IFA”) on franchise law topics. He has served as a member of the Governing Committee of the ABA’s Forum of Franchising, serves on the IFA’s Board of Directors and chairs the IFA’s Supplier Forum Board. He co-authored the Annual Franchise and Distribution Law Developments book, published by the ABA, and has published articles on franchise law for the National Law Journal, New York Law Journal, Franchise Times and the ABA.

The Law firm of Genovese Joblove & Battista, P.A. was counsel for the franchisor in the following cases cited herein:

PETER C. LAGARIAS

Peter C. Lagarias is the founder of Lagarias Law Offices in San Rafael, California. His trial practice consists of representing franchisees and franchisee associations in negotiations, arbitrations, litigation and trials. He is also a mediator and arbitrator. Mr. Lagarias is a Certified Specialist in franchise and distribution law by the Board of Legal Specialization of the State Bar of California. He is a past Co-Chair of the Franchise Law Committee of the State Bar of California and served as a member of the Franchise and Distribution Law Advisory Commission of the State Bar of California. Mr. Lagarias is a frequent lecturer and writer on franchise and distribution law, and is the author of Effective Closing Argument (Michie 1989), and chapters in the Antitrust Adviser (McGraw Hill 1985), Financial Performance Representations, the New and Updated Earnings Claims, ABA Forum on Franchising (2008) and California Franchise Law and Practice (CEB 2009). Mr. Lagarias is a co-founder and active with Rotaplast International, Inc., an organization providing free cleft lip and palate surgery on ten missions annually to developing countries around the world.

Mr. Lagarias received his B.A. in 1973 from the University of California at Berkeley (Phi Beta Kappa) and his J.D. in 1977 from the University of California, Hastings College of the Law (Order of the Coif, Hastings Law Journal).

Peter Lagarias was counsel for the franchisees in the following cases cited herein:

- Prudence Corp. v. Shred-It Am., Inc., 365 F. App’x 859 (9th Cir. 2010)