

**IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MARYLAND
(NORTHERN DIVISION)**

WW, LLC, *
RICHARD WELSHANS, *
DEBORAH WILLIAMS *

Plaintiffs *

v. * Civil No. 09-524-AMD

PEAR, SPERLING, EGGAN & *
DANIELS, P.C. *
PAUL R. FRANSWAY *

Defendants *

* * * * *

MEMORANDUM OF LAW IN OPPOSITION TO MOTION TO DISMISS

Plaintiffs, WW, LLC, Richard Welshans and Deborah Williams, by their attorneys, Harry M. Rifkin and the Franchise and Business Law Group, submit this Memorandum of Law in Opposition to the Motion to Dismiss filed by Defendants, Pear, Sperling, Eggan & Daniels, P.C. (“Pear, Sperling”) and Paul R. Fransway (“Fransway”)(jointly “Defendants”). Contrary to the Motion, limitations have not run, Plaintiffs have standing to assert their claims against Defendants and the complaint is pled with the requisite specificity. First, Plaintiffs were unaware and could not have been aware that the law firm was responsible for the wrongful acts rather than the client, The Coffee Beanery, Ltd. It was not until Joanne Shaw testified at the arbitration hearing in January, 2007 and laid the blame directly on Defendants herein for any disclosure violations that Plaintiffs became aware of or could have become aware of Defendants involvement in and commission of wrongful acts. Second, during the time from March 28, 2007,

when the arbitrator ruled against Plaintiffs on their suit against The Coffee Beanery, Ltd. (“The Coffee Beanery”) and its senior executives for the false and fraudulent misrepresentations and omissions in the Franchise Offering Circular prepared by Defendants until March 2, 2009 when the Sixth Circuit issued its mandate vacating the arbitration award, limitations were tolled. The arbitration award, attached hereto as Exhibit 1 effectively barred the claim asserted herein by *res judicata*. Third, the fraud claim is pled with requisite specificity as required under the rules.

I. Factual Background

This case arises out of a dispute by and among Plaintiffs and The Coffee Beanery, along with the results of an investigation by the State of Maryland, Office of the Attorney General regarding The Coffee Beanery’s franchise offering circular (hereinafter “UFOC”) for the State of Maryland registered in May, 2003. Defendants herein were counsel for The Coffee Beanery. Until 2002, the UFOC for The Coffee Beanery contained earnings claims identifying the gross sales for every store in its chain and identifying each store by concept. The 2000 and 2001 UFOCs showed that cafes were grossing less than the traditional coffee shops and showed that the costs of operating cafes were higher. This made it difficult to sell cafes as savvy prospects would be able to “run the numbers” and see that the concept was not going to work. These UFOCs also disclosed that The Coffee Beanery had a contract with Pepsi which provided it with moneys, that it made money on the sale of required equipment to franchisees and that it required the franchisees to participate in a gift check program, although the charges for the program were not disclosed.

In-house counsel for The Coffee Beanery, Rick Kalisher, departed sometime in 2001 and was replaced by outside counsel, Paul R. Fransway and Pear, Sperling. During this period, the Coffee Beanery did not register franchises in Maryland and other states. The UFOC was

basically rewritten in 2002 by new counsel, Defendants herein, at the behest of JoAnne Shaw. The new UFOC and Franchise Agreement were developed by JoAnne Shaw, Ken Coxen and Fransway. The stores were no longer broken out by concept, the gross sales were no longer reported, the Pepsi contract and the gift check program references were deleted. There was a conscious decision by The Coffee Beanery and its counsel, Defendants herein, to omit this information previously disclosed in earlier UFOCs. The UFOC then was modified by and at the direction of The Coffee Beanery's counsel, Pear, Sperling and Fransway, to include new language that The Coffee Beanery had been operating retail specialty stores, cafes, kiosks, and coffee/espresso bars since 1976 and had been franchising these types of stores since 1985. This information was not true. The first cafes were not opened until the 1990s and the first café franchise opened in 1997.

Contracts with third-party vendors which franchisees are required to enter into must be disclosed in the UFOCs and it is the practice of lawyers involved in the preparation of UFOCs to not only disclose such contracts but to attach them to the UFOC.

The Coffee Beanery's 2003 UFOC provides: "Since 1976, we have operated Stores of the type being franchised and continue to do so. These Stores are located in regional shopping malls, airports, strip centers, office buildings and cafés." It also states "we [The Coffee Beanery] are in the business of: operating specialty retail stores, cafés, kiosks, coffee/espresso carts, and coffee bars. For ease of reference, all of these will be referred to in this Offering Circular as 'Stores' unless otherwise noted. Our Stores sell fresh-brewed coffee, coffee beans, tea, spices, related products such as mugs and coffee makers, and food items. We are also in the business of granting franchises for our Stores and have offered franchises since 1985." The Coffee Beanery has admitted it that has not operated Stores of the café type since 1976 and has not franchised

cafes since 1985. It only offered café franchises starting in 1997.

The 2003 Maryland UFOC received by WW, Williams and Welshans did not contain the November 30, 2002 unaudited financial statement as stated in the UFOC and as required and was otherwise different from the registered Offering Circular.

Defendants herein, unknown to Plaintiffs, had prepared the UFOC. Plaintiffs also were not aware that the decisions to exclude information required to be included were made by Defendants until JoAnne Shaw so testified under oath at the arbitration hearing in January, 2007. They were also not aware of some of the other wrongful acts of the Defendants in connection with the UFOC until testimony at the arbitration revealed their role. From that testimony they were able to investigate the fraud and negligence of Pear, Sperling.

II. Legal Argument

A. Limitations has not run.

Maryland follows the discovery rule for limitations. In *Poffenberger v. Risser*, 290 Md. 631, 635, 431 A.2d 677 (Md., 1981), the Maryland Court of Appeals explained:

In Maryland, the general rule heretofore has been stated to be that the running of limitations against a right or cause of action is triggered upon occurrence of the alleged wrong, and not when it is discovered. *Leonhart v. Atkinson*, 265 Md. 219, 223, 289 A.2d 1, 3-4 (1972). However, the harshness of this general rule was readily observed and has in this State led to the creation of both legislative and judicial exceptions to it one among them, the "discovery rule."² Although perhaps timidly, the Court first applied the discovery rule in Maryland (and some suggest was the first to embrace the concept in the nation, see Note, *The Statute of Limitations in Actions for Undiscovered Malpractice*, 12 Wyo.L.J. 30, 34 (1957)), nearly three quarters of a century ago, when *Hahn v. Claybrook*, 130 Md. 179, 100 A. 83 (1917), it was announced that in medical malpractice cases the cause of action accrues when the wrong is discovered or when with due diligence it should have been discovered. Over the subsequent decades, the rule has spread beyond application solely to the learned professions so as to embrace malpractice in all callings encompassed within the continuously expanding concept of "profession." See *Harig v. Johns-Manville Products*, *supra* 284 Md. at 73-74, 394 A.2d at 304, and *Leonhart v. Atkinson*, *supra* 265 Md. at 224, 289 A.2d at 4, and cases cited in each. Thus, since "the 'discovery rule' has been consistently extended so that now

it is clearly applicable to all cases involving professional malpractice," *id.*, one of the principal inquiries focuses on whether the particular occupation involved in the case constitutes a "profession."

The Court in *Poffenberger, supra*, then continued:

Having already broken the barrier confining the discovery principle to professional malpractice, and sensing no valid reason why that rule's sweep should not be applied to prevent an injustice in other types of cases, we now hold the discovery rule to be applicable generally in all actions and the cause of action accrues when the claimant in fact knew or reasonably should have known of the wrong.

Poffenberger, supra at 636.

Plaintiffs did not know of, and could not have known of, the wrongful actions of Fransway and Pear, Sperling until the arbitration hearing just over two years ago, and filed this suit almost immediately after the mandate issued in *WW, LLC v. The Coffee Beanery* on March 2, 2009.

Bennett v. Baskin & Sears, 77 Md. App. 56 (1988), cited by Defendants does not support their position. In *Bennett*, there was not dispute as to when plaintiffs were on inquiry notice. There was a September 15, 1981 meeting at which there was totally documented complete inquiry notice. Moreover, the procedural posture of *Bennett* was different as discovery had been completed and it was on motion for summary judgment. In this case no discovery has yet been taken and the motion is one confined to the pleadings. The pleadings assert that the Plaintiffs were not on notice of claims against Pear, Sperling and Fransway until the arbitration in January, 2007.

Furthermore, there is nothing in the UFOC identifying Pear Sperling or Fransway as attorneys for The Coffee Beanery, or as the preparers of the UFOC. There is also nothing in the UFOC that would indicate or give Plaintiffs any reason to believe that Pear, Sperling or Fransway are responsible for the misrepresentations and omissions. Indeed, a reasonable person

would presume that the lawyers relied upon the information received from their clients and would not violate the Code of Professional Conduct in the preparation of the UFOC. Frankly, Plaintiffs were shocked when they found out in the arbitration that Pear, Sperling made the decisions to omit material facts and misrepresent other facts in the UFOC. The claims are timely filed.

B. Plaintiffs have standing to sue Defendants

These claims are not part of Richard Welshans' bankruptcy estate. The estate is closed and the trustee, who had full knowledge of the litigation with The Coffee Beanery, including the arbitration proceeding and the subsequent appellate reversal of the arbitrator's ruling chose not to maintain any claims against Pear, Sperling and Fransway. Having abandoned these potential claims, Welshans is now free to pursue them.

The other standing arguments fail as well. Defendants owe a duty to those who rely on the franchise prospectus which they prepared. While there are no Maryland cases directly on point, other courts have found such a duty. For example, in *Courtney v. Waring*, 191 Cal. App.3d 1434, 237 Cal.Rptr. 233 (1987), the California Court of Appeal expressly held that as the defendant attorneys allegedly negligently prepared a franchise prospectus (another name for the UFOC) which failed to disclose material information known to defendants, but unknown to plaintiffs and "knew that the prospectus would be shown to prospective franchisees and that the information contained in it would be used to induce these persons to purchase.. franchises," the attorneys had a duty to those whose conduct was influenced by the franchise prospectus. 191 Cal.Rptr. at 1443-44. The *Courtney* case also rejected limitations arguments similar to those raised herein, since there was a question of fact when the plaintiffs reasonably should have

suspected attorney negligence as opposed to negligence on the part of the franchisor. 191 Cal. Rptr. at 1444 n. 10.

In *Haberman v. Washington Public Power Supply System*, 109 Wash.2d 107, 744 P.2d 1032 (1987), the Washington Supreme Court held that bondholders' tort claims against the professionals who rendered services in connection with the issuance of the bonds and who made and participated in making negligent misrepresentations of facts and negligently omitted material facts necessary to make the statements and reports not misleading, stated a cause of action for negligent misrepresentation against the professionals.

Contrary to Defendants assertions, Plaintiffs pled all the elements of the claim of negligent misrepresentation. They allege in their Complaint that:

1. Defendants knew that the Franchise Offering Circular for the State of Maryland was in violation of the Maryland Franchise Registration and Disclosure Law by failing to disclose required information as set forth above.
2. When Defendants prepared the Franchise Offering Circular for the State of Maryland in 2002, they deleted much required information that had been included in the previously filed Franchise Offering Circulars because the inclusion of that information made it more difficult to sell Coffee Beanery Café and Coffee Beanery franchises.
3. Plaintiffs relied to their detriment on the Franchise Offering Circular being complete and accurate in making their decision to buy a Coffee Beanery Café franchise.
4. Defendants owed a duty of care to Plaintiffs and to all others to whom the Maryland Franchise Offering Circular for The Coffee Beanery, Ltd. was distributed as the Maryland Franchise Offering Circular was registered and provided to potential franchisees of its client, The Coffee Beanery, Ltd.
5. Defendants breached their duty of care to Plaintiffs by preparing and registering an Offering Circular which omitted material facts and which misstated other facts.

6. Defendants' failure to disclose material required information and the misstatements of fact in the Maryland Franchise Offering Circular was the proximate cause of Plaintiffs' injury.
7. Plaintiffs reasonably relied on the Maryland Franchise Offering Circular in deciding to purchase a Coffee Beanery Café franchise.
8. Defendants' failure to disclose material required information in the Maryland Franchise Offering Circular was not in accordance with the standard of care required of attorneys preparing and registering Franchise Offering Circulars in the State of Maryland.
9. Plaintiffs lost in excess of \$1,500,000 in owning and operating their Coffee Beanery Café franchise in Annapolis, Maryland.

The elements of negligent misrepresentation, having been properly pled, suffice for the assertion of these claims by Plaintiffs. The decisions in *Noble v. Bruce*, 349 Md. 730, 739 (1998) and *Ferguson v. Cramer*, 116 Md. App. 99, aff'd, 339 Md. 760, 765-66 (1998) are simply inapposite and do not support the proposition for which they are offered by Defendants. The document at issue, the UFOC, was prepared by Pear, Sperling with the intent that it be distributed to potential franchisees to induce them to purchase the Coffee Beanery Café franchise. To the contrary, in *Noble, supra*, the Court of Appeals also concluded that the testamentary beneficiary of a will could not maintain a cause of action for professional malpractice against an attorney where it is alleged that the attorney either provided negligent estate planning advice or negligently drafted the will in a manner that resulted in significant estate and inheritance taxes. The court recognized that attorney liability to non-clients was far from settled but that in the will drafting and estate planning context public policy required strict privity, noting that while the client is alive, the lawyer owes him or her a duty of complete and undivided loyalty. Clearly the duties of Defendants in this case were not just to The Coffee Beanery but were to their prospective franchisees as well as the UFOC is prepared expressly for the benefit of the franchisees. The statutory framework of the Maryland Franchise Registration

and Disclosure Law mandates that the UFOC be prepared for and distributed for the benefit of potential buyers of the franchise. Thus, public policy weighs against the strict privity rule.

Ferguson also was an action brought by the beneficiaries of an estate against the personal representative's attorney. The Court of Special Appeals held that the trial court did not err in dismissing the complaint on the grounds that the beneficiaries did not have standing to sue the attorneys for legal malpractice. In affirming the ruling, the court recognized that the strict privity rule that an attorney is not liable in an action arising out of his professional duties to anyone other than his client in the absence of fraud or collusion (which are of course alleged in the instant matter), was no longer the rule and that a third party beneficiary could sue an attorney if the attorney's work was performed for his benefit. 116 Md. App. at 105. That clearly is the case herein. Statutorily, Pear, Sperling and Fransway had liability and moreover, the UFOC was prepared specifically for the benefit of franchisees. It was not prepared for the benefit of The Coffee Beanery but for its prospective franchise owners such as Plaintiffs herein. As such, Plaintiffs have standing to sue Pear, Sperling and Fransway.

III. The Fraud claims are pled with requisite specificity

The Complaint provides extensive detail on the fraud of Defendants. Plaintiffs allege:

1. Pear, Sperling, Eggan & Daniels, P.C., is a Michigan law firm which prepared and registered the Franchise Offering Circular for The Coffee Beanery, Ltd. in the State of Maryland.
2. Paul R. Fransway is an attorney and shareholder of Pear, Sperling, Eggan & Daniels, P.C., and was the lead attorney at Pear, Sperling, Eggan & Daniels, P.C., who prepared and registered the Franchise Offering Circular for The Coffee Beanery, Ltd. in the State of Maryland. Fransway directed the preparation of the Franchise Offering Circular for The Coffee Beanery, Ltd. and decided what should be included in the Franchise Offering Circular.
3. On or about June 11, 2003, The Coffee Beanery, Ltd., delivered to Welshans and Williams a Franchise Offering Circular for the State of Maryland in the

State of Maryland. This offering circular was drafted by Defendants, although Plaintiffs did not know it at the time.

4. The Franchise Offering Circular for the State of Maryland delivered to Plaintiffs was in violation of the Maryland Franchise Registration and Disclosure Law in numerous ways, including, *inter alia*, the failure of The Coffee Beanery to disclose that Kevin Shaw had a felony conviction for grand larceny, the differences between the mall traditional retail coffee store and the cafes, the identity of the cafes, mall stores, kiosks, and other concepts, the mandatory Gift Card Program, the Pepsi Contract and the mandatory DMX Remote Eyes and Music Program.
5. Defendants knew that the Franchise Offering Circular for the State of Maryland was in violation of the Maryland Franchise Registration and Disclosure Law by failing to disclose required information as set forth above.
6. When Defendants prepared the Franchise Offering Circular for the State of Maryland in 2002, they deleted much required information that had been included in the previously filed Franchise Offering Circulars because the inclusion of that information made it more difficult to sell Coffee Beanery Café and Coffee Beanery franchises.
7. Plaintiffs relied to their detriment on the Franchise Offering Circular being complete and accurate in making their decision to buy a Coffee Beanery Café franchise.
8. At an arbitration hearing held in February, 2007, JoAnne Shaw, President of the Coffee Beanery, Ltd., testified that Defendants prepared the Franchise Offering Circular provided to Plaintiffs and that Defendants advised The Coffee Beanery, Ltd. on what information to include and what information to exclude from the Franchise Offering Circular and that The Coffee Beanery, Ltd. relied on the advice provided by its counsel, Defendants herein, in preparing and registering the Franchise Offering Circular.
9. On September 12, 2006, the State of Maryland and The Coffee Beanery, Ltd. entered into a consent decree in which The Coffee Beanery, Ltd., admitted that the Maryland Franchise Offering Circular omitted material facts as set forth above herein.
10. Defendants owed a duty of care to Plaintiffs and to all others to whom the Maryland Franchise Offering Circular for The Coffee Beanery, Ltd. was distributed as the Maryland Franchise Offering Circular was registered and provided to potential franchisees of its client, The Coffee Beanery, Ltd.
11. Defendants intentionally omitted material facts and intentionally included false statements of material fact in the Maryland Franchise Offering Circular

for the purpose of inducing Plaintiffs and other potential franchisees to buy Coffee Beanery franchises.

12. In the alternative, Defendants omitted material facts and included false statements of material fact in the Maryland Franchise Offering Circular with reckless disregard as to their truth or falsity, knowing that the Maryland Franchise Offering Circular would be used to induce Plaintiffs and other potential franchisees to buy Coffee Beanery franchises.
13. Defendants breached their duty of care to Plaintiffs by preparing and registering an Offering Circular which intentionally omitted material facts and which misstated other facts.
14. Defendants' failure to disclose material required information and the misstatements of fact in the Maryland Franchise Offering Circular was the proximate cause of Plaintiffs' injury.
15. Plaintiffs reasonably relied on the Maryland Franchise Offering Circular in deciding to purchase a Coffee Beanery Café franchise.
16. Defendants' failure to disclose material required information and their inclusion of false statements of fact in the Maryland Franchise Offering Circular was not in accordance with the standard of care required of attorneys preparing and registering Franchise Offering Circulars in the State of Maryland.
17. Plaintiffs lost in excess of \$1,500,000 in owning and operating their Coffee Beanery Café franchise in Annapolis, Maryland.

Plaintiffs do not know what more details that they need to put into the complaint. The rules require that fraud be pled with specificity. They require an identification of the requisite elements of the claim in sufficient detail to reveal the existence of the fraud. *Heinrich v. Goodyear Tire and Rubber Co.*, 532 F. Supp. 1348 (D. Md. 1982). That was clearly done in this case. Each of the events was detailed from JoAnne Shaw's statements that Defendants knew that the UFOC was false, that Defendants were given the information by The Coffee Beanery sufficient to make a complete and accurate UFOC including information on the Pepsi Contract, the Gift Card contract, the breakdown of franchises by concept, among others, but that Defendants advised The Coffee Beanery not to include that information as it would make it

difficult to sell café franchises which was the focus of The Coffee Beanery's business. The preparation of the UFOC by Defendants is alleged and the fraudulent nature of the UFOC which Defendants prepared and registered is described in detail. There is simply no merit to the claim that fraud was not pled with specificity. Indeed, there are seventeen separate detailed paragraphs describing Defendants' fraud. Plaintiffs have included all that they know. More information likely lies within documents exchanged between The Coffee Beanery and Defendants, which Plaintiffs have heretofore not been privy to because of the now waived attorney-client privilege.¹

IV. Conclusion

For the reasons set forth herein, Plaintiffs respectfully request that this Court deny Defendants' Motion to Dismiss and grant them attorneys' fees, and such other relief as this Court deems necessary and proper.

/s/

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¹ By JoAnne Shaw's testimony at the arbitration concerning the decision to exclude material information from the UFOC by Defendants, The Coffee Beanery has waived the attorney-client privilege as to communications concerning the preparation of and registration of the UFOC.

CERTIFICATE OF SERVICE

I hereby certify this 27th day of May, 2009 that the foregoing Memorandum in Opposition to Motion to Dismiss was electronically filed and mailed first class postage prepaid to Kathleen Howard Meredith, Esquire, Stephan Y. Brennan, Esquire, Patriots Plaza, Suite 201-203, 8055 Ritchie Highway, Pasadena, Maryland 21122.

_____/s/_____
Harry M. Rifkin