LOS ANGELES
Daily Journal

VOL 127 NO. 236 FRIDAY, DECEMBER 5, 2014 www.dailyjournal.com

Daily Journal

VERDICTS & SETTLEMENTS

CONTRACTS

BREACH OF CONTRACT

Excessive Royalties

BENCH DECISION: Defense.

CASE/NUMBER: Plover Financial Services, LLC v. ITS Financial, LLC, et al. / TCO24993.

COURT/DATE: Los Angeles Superior Compton / Sept. 12, 2014.

MEDIATOR: Scott L Gilmore.

ATTORNEYS: Plaintiff - Thomas M. Green (Green & Green, Dayton, Ohio); Hanwei Cheng (Adi Law Group PC, Los Angeles).

Defendant-Tim M. Agajanian, Mhare 0. Mouradian (Murchison & Cumming LLP, Los Angeles); Todd Bryant (Instant Tax Service, Beavercreek, Ohio).

TECHNICAL EXPERTS: Plaintiff - Barry Kurtz, franchise, Encino; Jennie McNulty, CPA, economics, Los Angeles.

Defendant - Scott Bosworth, intellectual property, Irvine; Barbara Gottlieb, CPA, accounting, real estate development and financing, Beverly Hills; Martin Laffer, CPA, taxes and financial investigation, Beverly Hills; Joe Matthews, franchise, Nashville, Tenn.

FACTS: Plaintiff Plover Financial Services LLC, a franchisee sued its franchisor, defendant ITS Financial LLC, whose franchises operated under the name of Instant Tax Services. Ohio-based ITS operated a multi-state franchise system, and Fezum Ogbazion was ITS' Chief Executive Officer and Chairman.

Prior to its dealings with Plover, ITS had no franchises operating in the Southern California area, but it wanted to open franchises there. In 2006, Ogbazion negotiated with Henock Teferi, one of Plover's owners and its managing partner and other Plover representatives for the opening of ITS franchises in the Los Angeles area. Both sides were looking to start a new enterprise in Los Angeles from scratch, with ITS to provide its brand and experience operating tax preparation franchises elsewhere.

Teferi executed all four of the Franchise Agreements on Dec. 16, 2006. Teferi and Kiflit Abraham, a principal of Plover also executed four associated Guarantees.

The Franchise Agreements indicated that ITS would provide a functioning franchise system, and the operational experience, proprietary information, service products, training, and technical systems that Plover would need to start a tax service business in its "Protected Area". Plover acquired four Protected Areas in Los Angeles, comprising of Central Los Angeles, extending south down to and including Long Beach, Inglewood and Carson. In return, Plover agreed to operate the franchises subject to ITS' guidance and direction and to pay, among other things, a one-time franchise fee, an annual Royalty Fee, and an annual Advertising Fee. The Agreements also provided that the Royalty Fee owed to ITS by Plover would be calculated as a percentage of Calendar Year "Gross Sales," a term defined in the Agreement as all revenues from all business conducted upon or from the Franchise Office including, without limitation, the amounts received from the sale of goods and services of every kind and nature provided or performed in connection with the preparation of tax returns.

PLAINTIFF'S CONTENTIONS: Plover alleged that ITS withheld excessive royalties, charged excessive advertising fees, *withheld* excessive *transaction* fees, improperly routed calls to other franchisees, and violated the protected area covenant.

DEFENDANTS CONTENTIONS: Defendant contended the specified Royalty Fee was 14 percent of the first $100,000 of the annual Gross Sales for each Protected Area. The fee stepped down to 12 percent for the next $100,000 of Gross Sales for that area, and then could be further reduced 'automatically by 2 percent for each additional $100,000 in annual Gross Sales but not below 8 percent. As the body of the Franchise Agreement was originally worded, Plover was also to pay 1TS an Advertising Fee of 6 percent of annual Gross Sales in addition to the Royalty Fee (this resulted in a maximum annual deduction of 20 percent from Plover's revenues). The Advertising Fee was to be used to fund the operation of an Advertising Fund that ITS would control and manage. The Advertising Fund would be used as ITS saw fit to promote its brand and ITS' franchise operations. ITS made no promise to use this money to benefit Plover in its Protected Areas. ITS reserved the right to defer or reduce the Advertising Fee assessed against a particular franchisee, or to close down the Fund completely.

When the four Franchise Agreements were signed on Dec. 16, 2006, Teferi also executed four addenda, "Special Stipulation to Franchise Agreement - Use of Advertising Fee". Plover contended that these Stipulations were part of and modified all four of the Franchise Agreements. No representative of ITS signed the Stipulations, and Ogbazion denied knowing about the Stipulations.

The Stipulations purported to effect a significant change to how Plover's revenue would be used. Without the Stipulations, Plover was expected to fund local marketing itself and to pay a 6 percent Advertising Fee to ITS, which ITS could have used wherever and however it saw fit to promote its brand. The Stipulations did not change ITS' right to collect the 6 percent Advertising Fee. However, the 6 percent Advertising Fee had to be used exclusively for marketing in Plover's territories, or be refunded to Plover. Plover's franchise operations were to commence with the beginning of calendar year 2007, which involves income tax preparation services for the client's earnings in the prior calendar year 2006.

ITS filed a cross-complaint against Plover for breach of contract, injunctive relief, misappropriation of trade secrets, unfair business practices in violation of Business and Professions Code section 17200 and interference with economic relationships.

ITS also claimed breach of the provisions of the Franchise Agreement that require Plover to use designated software and a service bank system to avoid paying ITS royalties and to prevent ITS from having accurate records of Plover's gross sales. In addition, ITS claimed that Plover further breached the Franchise Agreement by engaging in a competitive business and misappropriating trade secrets.

ITS argued it should be awarded damages for Plover's breach of the Franchise Agreements. Defendant contended that evidence established that Plover benefited from obtaining and using all of ITS' trademarks, brand and know-how and failed to pay royalty fees. Defendant contended that evidence also established that Plover terminated the Franchise Agreement without cause prematurely and continued to operate using ITS trademarks, brand name and expertise.

ITS claimed that the parties orally agreed to replace the 14 percent-12 percent-10 percent-8 percent step-down royalty fee structure with a flat 14 percent Royalty Fee at a face-to-face meeting in Los Angeles in March 2007. The meeting took place before the work for the 2006 tax season had even ended.

RESULT: Judgment entered in favor of ITS and Ogbazion on all causes of action, including failure to pay royalty fees, alleged in Plover's complaint. The court found in favor ITS on its cross-complaint for breach of contract only against Plover, who will pay ITS the net sum of $867,684.

Judgment was entered in favor of Plover on Fez Ogbazion's cross-complaint.

OTHER INFORMATION: Tim M. Agajanian is no longer at Murchison & Cumming LLP.

FILING DATE: Dec. 30, 2010.