IN THE UNITED STATES DISTRICT COURT

FOR THE WESTERN DISTRICT OF WISCONSIN

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COLORTYME, INC.,

Plaintiff,

v.

ARE NOT, INC. and
DAVID J. ARNDT,

Defendants.

OPINION AND
ORDER

03-C-0404-C

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Plaintiff Colortyme, Inc. brought this civil suit for monetary relief after defendants Are Not, Inc. and David J. Arndt defaulted on a promissory note and guaranty. Defendants do not dispute the existence of the note and guaranty or their failure to pay. However, they contend that the note and guaranty are not enforceable because defendants were under duress when they entered into the agreement. In addition, defendants have asserted a counterclaim for breach of the duty of good faith and fair dealing.

Jurisdiction is present under 28 U.S.C. § 1332, diversity of citizenship. Plaintiff is incorporated in Texas with its principal place of business in Plano, Texas. Defendant Are Not is incorporated in Wisconsin with its principal place of business in Madison, Wisconsin.

Defendant Arndt is a citizen of the State of Wisconsin. The record shows that the amount in controversy in this case is greater than $75,000.

Presently before the court is plaintiff's motion for summary judgment on defendants' affirmative defense and counterclaim. (Defendants assert duress as both an affirmative defense and a counterclaim, but duress cannot serve as the basis for an independent claim, only as a defense to liability.) I conclude that defendants cannot prevail on their affirmative defense of duress because they have failed to adduce any evidence that plaintiff committed wrongful acts under Wisconsin law. In addition, I am dismissing defendants' counterclaim for breach of a duty of good faith and fair dealing. The franchise agreement between the parties is governed by the law of Texas, which does not recognize a duty of good faith in franchise agreements. Accordingly, I will grant plaintiff's motion for summary judgment.

Before setting out the undisputed facts, a word is required regarding their source. Along with the magistrate judge's preliminary pretrial order, both parties received a copy of this court's Procedures to be Followed on Motions for Summary Judgment. Dkt. #9. The magistrate judge cautioned the parties to comply with these procedures. Although defendants submitted a brief in opposition to plaintiff's motion, they neither responded to plaintiff's proposed facts nor properly proposed their own factual findings, as required by this court's procedures. Instead, defendants referred to facts in their brief only, sometimes citing the record and sometimes not. This court will not consider facts contained only in a

brief. Id., I.B.4.; see also Ziliak v. AstraZeneca, LP, 324 F.3d 518 (7th Cir. 2003) (when a party fails to follow summary judgment procedures, proper response is to disregard party's nonconforming submissions). As plaintiff correctly points out in its reply brief, the consequence of defendants' omissions is that plaintiff's properly proposed facts will be deemed undisputed for purposes of its motion for summary judgment. Doe v. Cunningham, 30 F.3d 879, 883 (7th Cir. 1994). (As discussed below, however, even if I considered the facts in defendants' brief, I would still conclude that plaintiff is entitled to summary judgment.) Therefore, from plaintiff's proposed facts, I find the following facts to be undisputed.

UNDISPUTED FACTS

A. The Franchise Relationship

Plaintiff ColorTyme, Inc. is a franchisor of 317 rental stores in 39 states. Plaintiff's stores carry primarily electronics and other home furnishings. At one point, plaintiff had franchises in Wisconsin, but it does not any longer.

Defendant Are Not became the ColorTyme franchisee in Madison, Wisconsin, in July 1997. At all pertinent times defendant David Arndt was the sole owner of Are Not. On behalf of Are Not, Arndt signed a "ColorTyme, Inc. Rental Store Franchise Agreement" on July 16, 1997. The franchise agreement provided for an initial term of five years. At the

conclusion of the five years, Are Not could renew its franchise for one additional term of three years, provided that it was not in default of any provision of the franchise agreement and that it gave plaintiff written notice of their election to renew their franchise. One of the material provisions of the agreement required Are Not to be current on all monetary obligations.

B. Defendants' Credit History

Beginning in June 1999, Are Not financed its store inventory through STI Credit Corporation. STI was also known by the name SunTrust. Later, STI/SunTrust was bought out by Textron Financial. STI and Are Not entered into a credit and security agreement on June 22, 1999, which provided for a revolving credit line up to $250,000 to be used solely to finance Are Not's acquisition of inventory for use in the store. Are Not granted STI security interests in Are Not's inventory, accounts, accounts receivable and in the proceeds of each. The credit and security agreement provided that any failure by Are Not to pay and satisfy its debt to STI would constitute default. Upon default, Are Not's entire debt would be accelerated. Arndt gave a personal guaranty to STI guaranteeing payment of Are Not's obligations to STI. Plaintiff also guaranteed Are Not's debts to STI.

For approximately two years, Arndt used the STI revolving line of credit to purchase inventory for the franchise. During this time, Are Not accrued nearly $200,000 of debt on

the STI line of credit.

On May 10, 2001, STI restructured the debt that Are Not had accrued on the line of credit. (Plaintiff does not propose any facts explaining why STI restructured Are Not's debt. In their brief, defendants argue that plaintiff "direct[ed]" and "insist[ed]" that STI make changes, but defendants do not point to any specific facts explaining how plaintiff was involved.) STI converted $186,940.97 of the debt to a 48-month term note, which Arndt executed on Are Not's behalf. The May 2001 note was to be paid in 48 installments through April 26, 2005. The revolving line of credit under the June 1999 credit and security agreement was left in place, but the limit was reduced to $5,000. To secure the reduced line of credit, STI retained its interest in the same collateral described under the June 1999 credit and security agreement. Arndt then executed a security agreement in favor of STI for the May 2001 note. This agreement covered Are Not's inventory, equipment, fixtures and goods, as well as its accounts and instruments. The May 2001 note provided the same consequences of default as applied under the June 1999 credit and security agreement. Arndt personally guaranteed Are Not's debt under the May 10, 2001 promissory note to STI. Plaintiff also guaranteed Are Not's obligations to STI. In summary, after the execution of the May 2001 note, Are Not owed two separate obligations to STI: first, the balance on the May 10, 2001 note; and, second, a small balance that remained on the revolving line of credit under the June 1999 credit and security agreement.

C. Wisconsin's Lawsuit Against Plaintiff

In August 1999, the Wisconsin Attorney General sued plaintiff and its corporate parent Rent-A-Center, Inc. In its complaint, the attorney general alleged, among other things, that plaintiff's and Rent-A-Center's forms of rental contract violated the Wisconsin Consumer Act.

Arndt was deposed by the attorney general's office on October 10, 2000, in connection with the state's lawsuit. Arndt understood at that time that the attorney general was alleging that plaintiff's "rent-to-own" business model violated state law. Arndt went to meet with a representative of the attorney general's office on several occasions to discuss the legality of the form contract that he was using as a ColorTyme franchisee.

D. The End of the Franchise Relationship

Because of plaintiff's litigation with the State of Wisconsin and a resulting disagreement over what form of rental agreement to use, Arndt decided he wanted to terminate defendant Are Not's franchise relationship with plaintiff before the franchise agreement expired in July 2002. Arndt asked repeatedly to be released from the franchise agreement but plaintiff refused at first because plaintiff remained a guarantor on Are Not's debt to STI, now known as Textron.

Finally, in February 2002, plaintiff and Arndt, on behalf of Are Not, reached an

agreement by which Are Not could separate from plaintiff and continue business on its own. The agreement was conditioned on Arndt's finding financing to pay off Textron. For the next few months, Arndt searched unsuccessfully for such financing.

During this time, Arndt never submitted written notice to plaintiff of his desire to renew the franchise agreement. As a result, the agreement was allowed to expire in July 2002. However, the parties continued to treat each other as franchisor and franchisee while Arndt looked for financing. Both parties understood that if Textron knew there was no longer a franchise relationship between them, the full Textron debt would have been accelerated immediately pursuant to the July 1999 credit and security agreement. Are Not would have been unable to pay the full amount of the debt at that time.

On September 13, 2002, Textron sent notice to Arndt declaring Are Not in default under both the June 1999 Credit and Security Agreement and the May 2001 promissory note. The notice required Are Not to make an immediate payment of the entire balance of Are Not's debt to Textron. The notice stated that Are Not was in default for failure to make payments. It did not refer to Are Not's status as a ColorTyme franchisee.

E. Execution of the Note and Guaranty

Are Not could not cure its default on the Textron debt. On October 8, 2002, plaintiff agreed to pay the principal balance of $137,618.37 on Are Not's debt to Textron. Are Not

was able to pay the outstanding interest on the debt. In exchange for paying off Textron, plaintiff took a note from Are Not. The note set out a schedule by which Are Not was to repay plaintiff the $137,618.37 plaintiff paid to Textron. Plaintiff did not require Are Not to post any collateral to secure the note.

Are Not continued to run an independent business for several months after October 2002 and made payments on the note through February 2003. Are Not has not made a payment on the note since February 2003 and is now in default. The note provides that, in the event of default, the entire debt becomes immediately due and payable.

OPINION

The Court of Appeals for the Seventh Circuit has held that summary judgment is appropriate if the court concludes that "if the record at trial were identical to the record compiled in the summary judgment proceedings, the movant would be entitled to a directed verdict because no reasonable jury would bring in a verdict for the opposing party." Russell v. Acme-Evans Co., 51 F.3d 64, 70 (7th Cir.1995). A party moving for summary judgment will prevail if it demonstrates that there is no genuine issue of material fact and that it is entitled to judgment as a matter of law. Fed.R.Civ.P. 56(c); Celotex Corp. v. Catrett, 477 U.S. 317, 322 (1986); Anetsberger v. Metropolitan Life Ins. Co.,14 F.3d 1226, 1230 (7th Cir.1994). When the moving party succeeds in showing the absence of a genuine issue as

to any material fact, the opposing party must set forth specific facts showing that there is a genuine issue for trial. Fed.R.Civ.P 56(e); Matsushita Electric Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 586 (1986); Whetstine v. Gates Rubber Co., 895 F.2d 388, 392 (7th Cir.1988). If the nonmovant fails to make a showing sufficient to establish the existence of an essential element on which that party will bear the burden at trial, summary judgment for the moving party is proper. Celotex, 477 U.S. at 322.

Because the parties agree that Wisconsin law applies to defendants' duress defense and that Texas law applies to defendants' breach of good faith and fair dealing counterclaim, it is unnecessary to conduct a choice of law analysis.

A. Economic Duress

The elements of a claim for economic duress in Wisconsin are: (1) the party claiming duress is the victim of a wrongful or unlawful act or threat; (2) the act or threat deprives the victim of his unfettered will; (3) as a result of the first and second elements, the victim is compelled to make a disproportionate exchange of values or to give up something for nothing; and (4) there is no adequate legal remedy. Wurtz v. Fleischman, 97 Wis. 2d 100, 106, 293 N.W.2d 155, 158 (1980). The party claiming duress must prove these elements by clear and convincing evidence. Id. at 110-11, 293 N.W. 2d 155. Plaintiff has moved for summary judgment on the first, third and fourth elements.

As an initial matter, I note that when defendants filed their answer they identified plaintiff's failure to renew the franchise agreement as its only wrongful act. As plaintiff points out, the failure to renew cannot be a wrongful act because the facts show that defendants never exercised their option to renew the agreement. In their response brief, defendants identify three additional "wrongful" acts: (1) plaintiff forced Textron to restructure defendants' credit line, resulting in a reduced credit limit and defendants' inability to purchase inventory; (2) plaintiff refused to sell inventory to defendants; and (3) plaintiff decided to withdraw from business in the state of Wisconsin. As noted above, defendants failed to propose any facts in support of these assertions, which is reason enough to reject defendants' defense. However, even if I consider the facts alleged in defendants' brief, plaintiff would still be entitled to summary judgment.

With respect to plaintiff's conduct in forcing Textron to restructure defendants' credit line and refusing to sell inventory to defendants, defendants argue that these acts were wrongful because they created financial difficulties for defendants and eventually caused them to default on the Textron debt. Even if I assume that defendants were "compelled" to give plaintiff a note and guaranty as a result of the restructured debt, defendants have failed to show that it was plaintiff's wrongful acts that caused Textron to act as it did. Although defendants accuse plaintiff of "forcing" Textron to restructure defendants' debt, they point to no evidence showing *how* or *why* plaintiff did this. Defendants cannot show that there is

a genuine issue of fact on the question of wrongfulness if they do not develop the circumstances surrounding plaintiff's conduct. A nonmoving party cannot defeat a motion for summary judgment with conclusory allegations. Thomas v. Christ Hospital and Medical Center, 328 F.3d 890, 892-93 (7th Cir. 2003)

With respect to plaintiff's decision to discontinue business in Wisconsin, defendants seem to argue that this conduct was wrongful for two reasons. First, it effectively forced defendants out of business and, second, plaintiff's settlement with the state of Wisconsin set out a means by which plaintiff could legally continue its franchise with defendants. Whether or not an act is wrongful depends, in part, on whether plaintiff had a legal obligation to continue business in Wisconsin. See Wurtz, 97 Wis. 2d at 110, 293 N.W.2d 155. The facts show that the franchise agreement between the parties expired months before plaintiff settled its case with the state of Wisconsin. Therefore, plaintiff's decision to pull out of Wisconsin could not have been wrongful because plaintiff did not have a legal obligation to act otherwise. To the extent that defendants mean to argue that plaintiff decided to leave while they still had an agreement, they fail to point to any fact that this was the case, even in their brief.

Defendants have failed to show that there is a genuine issue of material fact as to the first element of duress. Accordingly, it is unnecessary to consider whether there is evidence supporting the additional elements.

B. Duty of Good Faith and Fair Dealing

In their counterclaim, defendants contend that plaintiff breached an implied duty of good faith and fair dealing created by the franchise agreement. As noted above, the parties agree that Texas law governs this claim. To provide a legal basis for this contention, defendants point out that Texas courts generally impose a duty of good faith and fair dealing when a special relationship is created by a contract between the parties. Arnold v. National County Mutual Fire Insurance Co., 725 S.W.2d 165, 167 (Tex. 1987). In Arnold, the Texas Supreme Court was asked to determine whether an implied duty of good faith and fair dealing exists in insurance contracts. Id. The court found that the unequal bargaining power between an insurer and the insured and the amount of control an insurer has over the entire claims process creates a special relationship between the parties, that gives rise to a duty of good faith and fair dealing. Id. However, the court has since declined to extend the duty to franchise agreements, holding that "a franchisor does not exert control over its franchisee's business comparable to the control an insurer exerts over its insured's claim." Subaru of America, Inc. v. David McDavid Nissan, Inc., 84 S.W.3d 212, 225 (Tex. 2002) (citing Crim Truck & Tractor Co. v. Navistar Int'l Transp. Corp., 823 S.W.2d 591, 595-96 (Tex. 1992)). After Crim Truck, the Texas legislature expressly provided a statutory duty of good faith and fair dealing among parties to a *car dealership* franchise agreement, id. it did not create a statutory duty of good faith and fair dealing in franchise agreements such as the one involved

here. Therefore, I am dismissing defendant's counterclaim because, under Texas law, there is no duty of good faith and fair dealing in this franchise agreement.

Even if a duty of good faith and fair dealing existed between plaintiff and defendants, defendants have failed to adduce any facts showing that it has been breached. Defendants rely on the same allegations they relied on to show that plaintiff committed wrongful acts for purposes of economic duress. Again, defendants' allegations fail to create a genuine issue of fact because they do not indicate that there was anything unfair or wrongful about plaintiff's behavior.

Undoubtedly, defendants' situation is unfortunate. It is unlikely that they could have foreseen the collapse of the "rent-to-own" business model in Wisconsin or the amount of income they would lose as a result. However, defendants cannot escape a legal obligation simply because events did not turn out as they hoped. It is possible that plaintiff could have done more to assist defendants in remaining a viable business. But without evidence that it was plaintiff that caused (rather than simply failed to alleviate) defendants' plight, defendants have no claim for duress. If such evidence exists, defendants have failed to present it to the court.

C. Mitigation of Damages

In their answer, defendants identify plaintiff's failure to mitigate its damages as an

additional affirmative defense. Although, plaintiff moved for summary judgment on this defense, defendants did not respond to plaintiff's argument in their response brief. Accordingly, I conclude that defendants have abandoned their mitigation defense.

The amount of plaintiff's damages, however, remains unclear. At the conclusion of plaintiff's brief, it asks the court to enter a money judgment "in the amount demanded in Colortyme's complaint." However, plaintiff did not submit any evidence to the court regarding the amount still owed to plaintiff. In plaintiff's complaint, it requests "the amounts owed under the Note plus interest" without identifying what that amount is. Although the facts show that the original amount on the note was $137,618.38, the facts show also that defendants did make some payments on the note, though neither side has established how many payments defendants made or what the sum of these payments were. Therefore, I cannot award damages until plaintiff clarifies exactly how much defendants still owe on the note.

ORDER

IT IS ORDERED that

1. Plaintiff Colortyme, Inc.'s motion for summary judgment on defendant Are Not, Inc.'s and defendant David J. Arndt's affirmative defense of duress and counterclaim for breach of the duty of good faith and fair dealing is GRANTED.

2. Plaintiff Colortyme, Inc. may have until April 19, 2004, in which to submit to this court information showing (1) the amount of each payment defendants made on the note and (2) the unpaid balance on the note, plus interest accruing from the date of default at a rate of 7% per annum. Defendants may have until April 26, 2004, in which to file a response to plaintiff's submission.

Entered this 13th day of April, 2004.

BY THE COURT:

BARBARA B. CRABB
District Judge