IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

ELLIOTT & FRANTZ, INC.	:	CIVIL ACTION
v.	:	
SVEDALA INDUSTRIES, INC.	:	NO. 97-3804

MEMORANDUM AND FINAL JUDGMENT

HUTTON, J. December 30, 1997

Presently before the Court are Defendant Svedala Industries, Inc.'s Motion to Dismiss, Plaintiff Elliott & Frantz Inc.'s Response, and the Defendant's Reply and Supplemental Reply thereto. After appropriate notice, the Court has converted these into motions for against summary judgment. For the foregoing reasons, the Defendant's Motion is granted.

I. BACKGROUND

This action is the attempt of a distributor to extract value from a decade-old relationship with its supplier after the supplier saw fit to let it lapse. The distributor, and plaintiff in this action, is Elliott & Frantz, Inc. ("E&F"), a Pennsylvania corporation based in King of Prussia, Pennsylvania. The supplier initially was Universal Engineering ("Universal"), a division of the Pettibone Corporation ("Pettibone"), an Iowa corporation based in Cedar Rapids, Iowa. However, on September 18, 1995, Svedala Industries, Inc. ("Svedala") purchased from Pettibone all of the assets of Universal, including Universal's contract with E&F, thereby placing itself in Universal's shoes as the supplier.

Universal manufactured crushing, shredding and material handling equipment. On March 20, 1985, E&F entered into a "Distributor's Contract" with Universal, whereby it became the distributor of the complete line of Universal's aggregate processing and recycling equipment for five states and the District of Columbia. (See Pl.'s Compl. at Ex. A).

In 1992, the parties renewed the agreement in an April 1 "Distributor Agreement." (See id. at Ex. B). Article XV of the agreement, entitled "Choice of Law," states in relevant part:

> This Agreement and all questions as to its interpretation, performance, and enforcement and the rights and remedies of the parties hereunder shall be determined in accordance with the laws of the State of Illinois.

(Id.).

Finally, in a March 7, 1995 letter agreement between E. Paul Noring of Universal and James Elliott of E&F (the "Letter Continuation"), the parties executed their (as it later developed) final renewal of the distributorship relationship. (See id. at Ex. C). The Letter Continuation clearly states that it is a continuation of the April 1, 1992 "Distributor Agreement." (Id.). In addition, paragraph two of the agreement reads:

> The term of this Agreement shall be for two years. The parties may by mutual agreement extend it for an additional one year period. Either party may terminate this agreement by giving the other party thirty (30) days written notice of the same.

(Id.). In the margin, a representative of E&F scrawled "with cause" next to the termination portion of paragraph two. (Id.).

As noted above, Universal's ownership changed hands during the two year term of the Letter Continuation. On September 18, 1995 Pettibone assigned Svedala--among other things--the E&F Distributor Agreement and Letter Continuation. As the Letter Continuation was dated March 7, 1995, according to its terms the relationship would lapse on March 7, 1997, unless renewed.

At some point during this period, Svedala determined--for reasons not pertinent to this decision--that it would not renew its relationship with E&F. On February 28, 1997, Lawrence P. Hetzel of Svedala called James Elliott of E&F and informed him that Svedala intended to allow the agreement to lapse. (See Def.'s Mot. to Dismiss at 2). In its Complaint, E&F characterizes the transaction as a termination. It states: "On February 28, 1997, without justification or privilege and in breach of contract, Universal terminated E&F's Distributorship." (Pl.'s Compl. at ¶ 9).

On April 29, 1997, E&F brought the present action in the Pennsylvania Court of Common Pleas, Montgomery County. In it, E&F states that the Letter Continuation "expressly provides the parties may, by mutual agreement, extend the contract for an additional one-year period." (Id. at ¶ 13). Stating its claim as one for breach of contract, E&F alleges further that:

> Universal has violated the implied obligation of good faith and fair dealing in refusing to extend the agreement for one year and has acted capriciously and in bad faith in terminating the contract.

(Id. at ¶ 14). Finally, E&F claims to have sustained lost profits of $375,000.00 as a consequence of the alleged breach, and demands judgment in that amount. (Id. at ¶ 15).

On June 3, 1997, Svedala removed E&F's action to this Court. This Court has diversity jurisdiction under 28 U.S.C. § 1332 (1994). Likewise, venue is proper under 28 U.S.C. § 1441 (1994). In any case, E&F has not asked the Court to remand back to the Court of Common Pleas.

Finally, on December 11, 1997, this Court exercised its discretion under Rule 12(b) of the Federal Rules of Civil Procedure to convert Svedala's motion to dismiss into one for summary judgment. See Fed. R. Civ. P. 12(b); Vosgerichian v. Commodore Int'l, 862 F. Supp. 1371, 1375 (E.D.Pa. 1994).[1] After providing notice by order, and receiving submissions from the parties, the Court is now authorized to proceed under Rule 56.

II. DISCUSSION

In its motion, Svedala argues it did not terminate its relationship with E&F, but rather permitted it to lapse. It claims that under the terms of the Letter Continuation it was under no

[1] Rule 12(b) states in relevant part:

> If, on a motion asserting the defense numbered (6) to dismiss for failure of the pleading to state a claim upon which relief can be granted, matters outside the pleading are presented to and not excluded by the court, the motion shall be treated as one for summary judgment and disposed of as provided in Rule 56, and all parties shall be given reasonable opportunity to present all material made pertinent to such a motion by Rule 56.

obligation, either express or implied, to renew the relationship. Accordingly, as a matter of law it could not, and did not, breach the contract that formerly existed between the parties. E&F counters that the language of the Distributor Agreement and Letter Continuation demonstrate that E&F "bargained for and received a commitment from Svedala and/or its predecessor to act in good faith in arriving at a contract extension." (Pl.'s Response at 3).

A. Standard Of Review

A court may grant summary judgment where "the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). In considering the motion, the court must draw all inferences in the light most favorable to the nonmovant. Big Apple BMW, Inc. v. BMW of N. Am., Inc., 974 F.2d 1358, 1363 (3d Cir. 1992), cert. denied, 507 U.S. 912 (1993). Under the Rule 56 framework, the moving party bears the initial burden of proving that there exists no triable issue of material fact. Celotex Corp. v. Catrett, 477 U.S. 317, 323 (1986). Where it has done so, the burden shifts, and the nonmovant must present affirmative proof that triable issues remain or else face summary judgment. Fed. R. Civ. P. 56(e). The non-movant cannot survive summary judgment merely by insisting on its interpretation of the facts, or by relying on unsubstantiated allegations, general denials, or vague statements. Id.; Trap Rock

Indus., Inc. v. Local 825, 982 F.2d 884, 890 (3d Cir. 1992).

B. Applicable Law

An initial question is which state's substantive law governs this contract dispute. Svedala argues that Illinois law applies pursuant to the choice of law provision in the Distributor Agreement, incorporated by reference into the Letter Continuation. E&F claims that Pennsylvania law applies after consideration of Illinois' choice of law principles.

A federal court sitting in diversity must begin by applying the choice of law rules of the forum state. Kruzits v. Okuma Mach. Tool Inc., 4 F.3d 52, 55 (3d Cir. 1994) (citing Klaxon Co. v. Stentor Electric Mfg. Co., 313 U.S. 487 (1941)); Leonard A. Feinberg, Inc. v. Central Asia Capital, 974 F. Supp. 822, 828 (E.D.Pa. 1997). Accordingly, the analysis begins with Pennsylvania's choice of law rules.

"Pennsylvania courts generally honor the intent of the contracting parties and enforce choice of law provisions executed by them." Kruzits, 40 F.3d at 55 (citing Smith v. Commonwealth Nat. Bank, 557 A.2d 775, appeal denied, 569 A.2d 1369 (1990)). E&F and Universal were sophisticated business entities represented by counsel at the time of their Distributor Agreement and Letter Continuation, and the Court sees no reason to disturb ex post their carefully negotiated allocation of risk. See RTC Commercial Assets Trust v. Ashme Realty Assoc., 1997 WL 260424, *2 (E.D.Pa. May 13, 1997). As noted before, the choice of law provision incorporated

by reference into the Letter Continuation read: "This Agreement and all questions as to its interpretation, performance, and enforcement and the rights and remedies of the parties hereunder shall be determined in accordance with the laws of the State of Illinois." (Pl.'s Compl. at Ex. B). The clear import of this language is that the substantive law of Illinois law governs the interpretation of the contract. See Feinberg, 974 F. Supp at 828; Springfield Oil Services, Inc. v. Costello, 941 F.Supp. 45, 47 (E.D.Pa. 1996). As this case requires the Court to determine the meaning of the termination/renewal clause--a portion of the agreement, there is no question that, at least at the time of signing, both parties meant that such a dispute be governed by Illinois law.

C. Breach of Contract Claim

The parties agree on all of the details of the contractual history between them, and agree on the text of the termination/renewal provision. They only disagree as to its meaning and application to their case.

The language at issue states: "The term of this Agreement shall be for two years. The parties may by mutual agreement extend it for an additional one year period." (Pl.'s Compl. at Ex. A). E&F reads these terms as creating an obligation between the parties to negotiate a new agreement at the end of the existing one. The mutual agreement language, it argues, would otherwise be meaningless, because no contractual provision would have been

necessary to express the obvious fact that the parties could renew their agreement. Therefore, E&F claims, the mutual agreement language, in combination with the implied duty of good faith and fair dealing, required Svedala at least to enter renewal negotiations in good faith.

The difficulty with E&F's argument is that it applies with equal force to the inclusion of the preceding provision--that the contract would last for a term of two years. In its supplemental brief, E&F argues that Svedala acted arbitrarily, and lacked a proper basis for "terminating" the agreement.[2] (See Pl.'s Supp. at 3). Apparently it regards the contract as one of effectively unlimited duration, subject to termination by either party for cause. But such a reading renders the two-year provision nugatory. The Court cannot ignore the two-year provision; the parties could have entered into an open-ended contract, but did not. The presence of separate language on termination within the same section further indicates that the parties meant that the relationship exist in a series of discrete terms. There would be no point in structuring the relationship in this manner if the parties had not meant to give each other the ability--at some point--to walk away free and clear of legal entanglements.

In any case, the Court finds that the language in question does not create an obligation to negotiate a new agreement. See

[2] E&F continues to view the situation as a termination rather than a lapse. (See Pl.'s Supp. Mem. in Opposition at 3). This position is plainly counterfactual, as the contract language is clear and E&F does not claim Svedala waived or agreed to modify it by conduct or otherwise.

Digital Equip. Corp. v. Uniq Digital Technologies, Inc., 73 F.3d 756, 758 (7th Cir. 1996) (finding no good faith duty under Illinois law for manufacturer to continue relationship with value-added reseller). Rather it states unambiguously that the parties "may" do so. There is a world of difference between "may" and "shall," and the Court presumes that sophisticated parties can distinguish between the two.

As the Illinois courts state:

> Where the language of a contract is unambiguous, the express provisions govern and there is no need for construction or inquiry as to the intention of the parties. A court must construe the meaning of a contract by looking at words used and cannot interpret the contract in a way contrary to the plain and obvious meaning of those words. The rights of parties to a contract are limited by the terms expressed in the contract. A court will not rewrite a contract to suit one of the parties, but will enforce the terms as written. There is a strong presumption against provisions that easily could have been included in the contract but were not.

Klemp v. Hergott Group, Inc., 641 N.E.2d 957, 962 (Ill. App. Ct. 1994) (finding contract language did not imply duty to sue for zoning change after city council rejected it) (emphasis added) (citations omitted). See also Saunders v. Michigan Avenue Nat. Bank, 662 N.E.2d 602, 610 (Ill. App. Ct. 1996); Resolution Trust Corp. v. Holtzman, 618 N.E.2d 418, 423 (Ill. App. Ct. 1993). Whether a contract is ambiguous is a question of law for the court to decide. Stichter v. Zuidema, 646 N.E.2d 296, 298 (Ill. App. Ct. 1995). As Svedala points out, the parties could easily have

included language requiring good faith negotiation and renewal, but did not. The Court agrees, and holds that the provision created no obligation to negotiate in good faith for the renewal of the agreement. When the agreement lapsed, Svedala was under no contractual obligation to E&F whatsoever.

Furthermore, E&F cannot bootstrap an enforceable obligation out of nothing through the general implied duty of good faith and fair dealing. The implied duty of good faith is a gap-filling rule of construction that exists only to prevent one party from exploiting ambiguities in a contract to harm the other. Continental Bank, N.A. v. Everett, 964 F.2d 701, 705 (7th Cir. 1992); Digital Equip. Corp. v. Uniq Digital Technologies, Inc., 1995 WL 12297, *4 (N.D.Ill. 1995), aff'd, 73 F.3d 756 (7th Cir. 1996).

> It has little to do with the formation of contracts . . . and nothing to do with the enforcement of terms actually negotiated. Because this duty is an estimate of what parties would agree to if they dickered about the subject explicitly, parties may contract with greater specificity for other arrangements.

Everett, 964 F.2d at 705. In this case, the parties did make explicit arrangements as to the lapse, termination, and renegotiation of the contract, and the implied duty of good faith is inapplicable.[3] E&F has cited no cases to the contrary.

[3] Furthermore, breach of the implied duty of good faith and fair dealing does not exist as an independent cause of action, as implied in ¶ 14 of E&F's Complaint. See Beraha v. Baxter Health Care Corp., 956 F.2d 1436, 1443 (7th Cir. 1992).

III. CONCLUSION

The Court finds, under the language in paragraph two of the Letter Continuation, and Illinois contract law, that Svedala had no contractual duty to renegotiate its lapsing contract with E&F. Therefore, E&F's claim for breach of contract is entirely without merit.

An appropriate Order follows.

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FINAL JUDGMENT

AND NOW, this 30th day of December, 1997, upon consideration of Defendant Svedala Industries, Inc.'s Motion to Dismiss and Plaintiff Elliott & Frantz Inc.'s Reply and Supplementary Reply thereto, converted into motions for and against summary judgment under Rule 12(b), IT IS HEREBY ORDERED that the Defendant's Motion is **GRANTED**.

IT IS FURTHER ORDERED that Judgment is entered in favor of Defendant and against Plaintiff.

BY THE COURT:

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HERBERT J. HUTTON, J.