IN THE COURT OF APPEALS OF THE STATE OF WASHINGTON

TELEKENEX IXC, INC., a Delaware corporation, Respondent, v. CHARLOTTE RUSSE, INC., a California corporation, Appellant.	)	No. 64192-1-I DIVISION ONE UNPUBLISHED FILED: November 15, 2010

Cox, J. — A trial court may set aside an order of default and default judgment where there is substantial evidence to support, prima facie, a defense to the opposing party's claims and certain other criteria are met.[1] This determination is subject to review for abuse of discretion.[2] Where the trial court denies a trial on the merits, we may more readily decide that the trial court abused its discretion.[3]

Here, Charlotte Russe Incorporated ("Charlotte") has established a prima

---

[1] White v. Holm, 73 Wn.2d 348, 352, 438 P.2d 581 (1968); CR 60(b)(1).

[2] Griggs v. Averbeck Realty, Inc., 92 Wn.2d 576, 582, 599 P.2d 1289 (1979).

[3] White, 73 Wn.2d at 351-52.

facie case of economic duress in connection with its entering into an agreement with Telekenex IXC, Inc. ("IXC"). Moreover, Charlotte has satisfied the other criteria required to set aside an order of default and default judgment under White v. Holm[4] and other authority. We reverse the order denying Charlotte's motion to set aside the default judgment and remand for further proceedings.

In December 2004, Charlotte entered into a Master Service Agreement ("MSA") with AuBeta Network Corporation ("AuBeta") for communication services at its retail stores. They later extended the MSA through April 1, 2009. On that date, the MSA would automatically continue month-to-month until terminated with either 90 days notice by AuBeta or 30 days notice by Charlotte.

On Wednesday, March 25, 2009, less than a week before the MSA would have turned month-to-month, Tom Hunsinger from AuBeta e-mailed Giri Durbhakula, Charlotte's Vice President of Technology. He stated that Telekenex had acquired AuBeta and that Charlotte would need to "make a commitment to Telekenex to avoid service disruption" by Friday, March 27, 2009. Durbhakula received a proposed amendment to the MSA ("Amendment") at 8:48 p.m., Thursday, March 26. The following morning, Hunsinger advised Durbhakula to have the Amendment "in by end of day to avoid service disruption." Hunsinger and Brandon Chaney, CEO of IXC and Telekenex, Inc. ("Telekenex"), then granted Durbhakula an extension until Monday, March 30, 2009. On Monday afternoon, Chaney e-mailed Durbhakula to remind him that the Amendment must

[4] 73 Wn.2d 348, 352, 438 P.2d 581 (1968).

be "executed today or your service could be disconnected by the underlying carriers." Durbhakula signed the Amendment, but stated:

> [We have] an existing agreement with AuBeta, which we believe should be honored. Despite our multiple requests, no one has explained why this agreement is somehow no longer valid. Instead, we have been presented with a demand that we sign up for a long term commitment or service to 185 of our stores will be shut off today . . . . [I]t has been made clear repeatedly that our service would be shut off if we do not sign up to a long term commitment.[5]

In May 2009, Durbhakula told Chaney that Charlotte believed the Amendment was unenforceable. On June 4, 2009, counsel for Charlotte sent a letter to Chaney describing Charlotte's position. Charlotte also filed a Complaint for Declaratory and Injunctive Relief against Telekenex in California Superior Court. On June 29, 2009, that court issued a Temporary Restraining Order, enjoining Telekenex from terminating Charlotte's service.

Meanwhile, on June 11, 2009, IXC sued Charlotte for breach of contract in King County Superior Court, regarding the same MSA and Amendment. IXC served a summons and complaint on Charlotte's registered agent the next day, but these pleadings were lost and Charlotte did not answer. IXC moved for default on July 9, 2009, and the motion was granted the same day. On July 13, 2009, IXC moved for entry of a default judgment. The judgment was entered the next day. IXC served five writs of garnishment based on that default judgment on July 24, 2009.

On July 29, 2009, Durbhakula received a fax from Wells Fargo notifying

[5] Clerk's Papers at 172.

him that it received a writ. Durbhakula immediately contacted Charlotte's counsel who called IXC's counsel to discuss the default judgment. On July 30, 2009, Charlotte asked IXC to stipulate to vacate the default judgment and quash the writ of garnishment. IXC refused. On August 3, 2009, Charlotte moved to vacate the default judgment and to quash the writ of garnishment. On August 27, 2009, the trial court denied Charlotte's motion.

Charlotte appeals.

Vacation of Default order and Judgment

Charlotte argues that the trial court abused its discretion in refusing to grant its motion to vacate the default judgment. We agree.

CR 60(b) provides for relief from orders and judgments based on certain criteria. Under White, the moving party has the burden to prove two primary and two secondary factors before a court will vacate a default judgment.[6] The primary factors are (1) that there is substantial evidence supporting a prima facie defense and (2) that the failure to timely appear and answer was occasioned by mistake, inadvertence, surprise, or excusable neglect.[7] The secondary factors are (1) that the defendant acted with due diligence after receiving notice of the default judgment and (2) that the plaintiff will not suffer a substantial hardship if the default judgment is vacated.[8] The overriding concern is whether or not

[6] White, 73 Wn.2d at 352.

[7] Little v. King, 160 Wn.2d 696, 703-04, 161 P.3d 345 (2007) (citing White, 73 Wn.2d at 352).

[8] Id. at 704 (citing White, 73 Wn.2d at 352).

justice is done.[9]

A decision on a motion to vacate a default judgment is discretionary and will not be disturbed unless the trial court abused its discretion.[10] "[W]here the determination of the trial court results in the denial of a trial on the merits an abuse of discretion may be more readily found than in those instances where the default judgment is set aside and a trial on the merits ensues."[11]

Here, the secondary factors for vacating a default judgment are met and are undisputed. First, Charlotte acted diligently upon notice of the default judgment. The court entered the default judgment on July 14, 2009, and IXC served the writs of garnishment on July 24, 2009. Charlotte learned of the default five days later and moved to vacate the default judgment five days after that. Second, IXC does not argue that it will suffer a substantial hardship if the default judgment is vacated. In any event, we see no such hardship. Thus, the primary factors are the only ones at issue in this appeal.

Substantial Evidence of a Defense

Charlotte argues that it has presented substantial evidence of a strong defense of duress to IXC's claims. We agree.

In Washington, "business compulsion" is a type of duress where a party is "compelled to suffer a serious business loss or make payment to his detriment."[12]

---

[9] Id. at 703 (citing Griggs, 92 Wn.2d at 582).

[10] Griggs, 92 Wn.2d. at 582.

[11] White, 73 Wn.2d at 351-52.

[12] Nord v. Eastside Ass'n Ltd., 34 Wn. App. 796, 798, 664 P.2d 4 (1983)

In order to prevail on this defense, the "victim" must prove "both that the offending party applied the immediate pressure and also that he caused or contributed to the underlying circumstances which led to the victim's vulnerability."[13] A party must show more than stress of pecuniary necessity to force entry into the contract.[14]

The Washington Pattern Jury Instructions on duress state that "[a] party may rescind a contract on the ground of duress if the party proves by clear, cogent, and convincing evidence that [it] agreed to the contract because of an improper threat by the other party that left no reasonable alternative."[15] The instruction is based in part on the Restatement (Second) of Contracts § 176(1), which states that a threat is improper if "the threat is a breach of the duty of good faith and fair dealing under a contract with the recipient."[16] A threat of non-performance of a contract is also improper if it is made "for some purpose unrelated to the contract, such as to induce the recipient to make an entirely separate contract."[17]

(citing Barker v. Walter Hogan Enters., Inc., 23 Wn. App. 450, 452, 596 P.2d 1359 (1979)).

[13] Id. (quoting Barker, 23 Wn. App. at 453).

[14] Puget Sound Power & Light Co. v. Shulman, 84 Wn.2d 433, 443, 526 P.2d 1210 (1974).

[15] WPI 301.10.

[16] WPI 301.10 cmt.

[17] Restatement (Second) of Contracts §176 cmt. e (1981).

Here, Charlotte has presented evidence that IXC threatened to allow its service to be cut-off without the notice required in the MSA in order to compel Charlotte to enter into a new contract. Charlotte was first notified of a potential disruption of service on March 25, 2009. Two days later Chaney and Hunsinger communicated to Durbhakula that Charlotte's service would be disrupted unless it agreed to enter into a multi-year extension of its contract. In an e-mail from Hunsinger to both Chaney and Durbhakula, Hunsinger thanked Durbhakula for his summary of the circumstances that "Telekenex has made it clear that service ***will be disconnected*** to nearly 200 of our stores if we do not sign a 36-month contract today."[18]

At that time, Charlotte's MSA with AuBeta required 60 days written notice before either party could cancel the contract. The five day notice given by IXC was a violation of the MSA. The threatened termination of services would have left 185 Charlotte stores not able to connect to the Internet, connect to the company data center, use the telephone, process customer purchases, track inventory, keep employee timecards, or access company e-mail. Aside from lost revenue from customer purchases, Charlotte's goodwill and business reputation would likely have suffered as a result of the disconnection of service. This was sufficient to demonstrate a serious business loss. In order to avoid these serious losses, Charlotte was forced to make a decision to its detriment by entering into a two-year contract extension with IXC.

[18] Clerk's Papers at 159 (emphasis added).

Additionally, IXC applied the immediate pressure and caused or contributed to the underlying circumstances. In an e-mail, Chaney explained that "AuBeta Networks has recently sold its assets to Telekenex and we are working with the underlying carriers to keep your services up. This will require us to commit to a multi-year agreement with them. Therefore, we need Charlotte Russe to commit to us as well."[19] By choosing to acquire AuBeta's assets and liabilities, IXC assumed negotiations with the underlying carriers. Charlotte was not a party to the purchase agreement. IXC should not have disregarded the MSA with Charlotte and threatened to terminate services without proper notice.

Given these facts, Charlotte has presented a strong defense against the breach of contract alleged by IXC. Therefore, it has met its burden to establish this prong of the White test.

We note that the California Superior Court granted Charlotte's request for a TRO on June 29, 2009, prior to the entry of default in Washington. In order to obtain a TRO in California, the court must balance the likelihood that the moving party will ultimately prevail on the merits and the relative interim harm to each party if the injunction is granted or denied.[20] Charlotte argued that the Amendment was void due to economic duress. Although the trial court in this case was not bound by the California Superior Court decision that Charlotte was likely to prevail on its claim of economic duress, we conclude that the decision

[19] Clerk's Papers at 169.

[20] Butt v. State of California, 4 Cal. 4th 668, 677-78 (1992).

lends support to the view that Charlotte has, at least, a prima facie defense in this action.

IXC argues that Charlotte cannot prove duress because IXC was not responsible for the underlying circumstances which led to Charlotte's vulnerability. IXC relies on Nord v. Eastside Association Ltd.,[21] Barker v. Walter Hogan Enterprises, Inc.,[22] Puget Sound Power & Light Co. v. Shulman,[23] and TMT Bear Creek Shopping Center v. Petco Animal Supplies, Inc.,[24] in making this argument. None of these cases are persuasive.

TMT Bear Creek is unpersuasive because it does not address the defense of business compulsion at all. Rather, the defendant relied upon the defenses of waiver and immaterial breach in response to the plaintiff's breach of contract claim.[25]

In Nord, the plaintiff was awarded amounts due on a contract and promissory note that the defendants' failed to honor.[26] The defendants argued that the contract and note were voidable because they were executed under business compulsion.[27] The agreement specified that the defendants would buy

---

[21] 34 Wn. App. 796, 664 P.2d 4 (1983).

[22] 23 Wn. App. 450, 596 P.2d 1359 (1979).

[23] 84 Wn.2d 433, 526 P.2d 1210 (1974).

[24] 140 Wn. App. 191, 204-05, 165 P.3d 1271 (2007).

[25] Id. at 207, 209.

[26] Nord, 34 Wn. App. at 797.

[27] Id. at 798.

out the plaintiff's shares of stock in a closely held business, which plaintiff managed as president. A promissory note was executed to reflect the unpaid balance for the stock.[28] There was evidence that the business was in financial peril and the defendants believed it would be more successful if the plaintiff were removed.[29] Additionally, the defendants had other investors who were willing to pay more for the stock than the price they bought it for from the plaintiff.[30] Finally, both parties engaged in extensive negotiations and were each represented by counsel throughout the process.[31] Under these circumstances, the court held that the defendants did not meet their burden to show that the plaintiff caused or contributed to the defendants' vulnerability or exerted the pressure that brought about the decision to enter into the agreement.[32]

Here, Charlotte did not benefit by entering into the Amendment with IXC, as the plaintiff in Nord did. Additionally, the evidence here shows that the negotiations were conducted quickly, over a few days, and consistently opposed by Charlotte. As such, Nord is distinguishable.

In Barker, the parties entered into a ten year lease which required the plaintiff to contribute fifty percent of any additional septic system installations

---

[28] Id. at 797.
[29] Id. at 799.

[30] Id.

[31] Id.

[32] Id.

required by the county.[33] During the course of the lease, the county twice required septic systems to be installed.[34] The plaintiff contributed money for the first system, but not for the second.[35] During the last year of the lease, the plaintiff decided to sell his business.[36] As part of the sale, the purchaser required that the lease continue for several more years.[37] However, the landlord refused to enter into a lease extension unless the plaintiff paid his share for the second septic system installation.[38] The plaintiff sued his landlord for money damages claiming that he was wrongfully compelled to pay additional fees in order to enter into a new lease.[39] The court held that there was no business compulsion because the landlord did not contribute to the underlying circumstances which caused the plaintiff's vulnerability.[40] Rather, the circumstances were "caused by the normal and expected termination of his 10-year lease without any contractual basis for renewal on any terms, coupled with his unilateral attempts to sell his business and the conditions of sale imposed by

---

[33] Barker, 23 Wn. App. at 451.

[34] Id. at 451-52.

[35] Id. at 452.

[36] Id.

[37] Id.

[38] Id.

[39] Id.

[40] Id. at 453.

his buyer."[41]

Here, Charlotte did not contribute to its own vulnerability in the way that the plaintiff in Barker did. First, the contract between Charlotte and AuBeta was not expiring because it would have automatically continued month-to-month. Second, the contract required AuBeta to give Charlotte notice before services could be terminated, so IXC did not have the same renegotiation position as the landlord in Barker. Third, Charlotte did not have any self-imposed outside pressure to enter into a new agreement with IXC. Had IXC given Charlotte the proper notice for termination under the contract and then renegotiated the amendment, Barker might be persuasive. However, that was not the case.

In Puget Sound Power & Light, sellers of real estate entered into a contract with the purchaser because they were in a "desperate financial condition" and needed to unload the property.[42] There was evidence that they sought out the purchaser and solicited his aid specifically because of their financial difficulties.[43] The court refused to find that the purchase agreement was invalid on grounds of business compulsion because there was no evidence that the purchaser caused their underlying financial difficulties.[44] Additionally, there was no evidence that the duress resulted from the purchaser's wrongful

---

[41] Id.

[42] Puget Sound Power & Light, 84 Wn.2d at 442.

[43] Id.

[44] Id.

and oppressive conduct rather than the sellers' financial needs.[45]

In contrast, here the record shows that IXC's wrongful and oppressive conduct resulted in Charlotte's duress. IXC made the independent decision to acquire the assets and the liabilities of AuBeta. A purchaser corporation is liable for the debts of the seller corporation if "the purchaser expressly or impliedly agrees to assume liability."[46] As such, IXC was not simply a middle-man trying to help Charlotte and the carriers come to a workable solution: it acquired contractual agreements with both groups. IXC was responsible for satisfying the debts of the underlying carriers. While IXC may not have caused underlying service providers to threaten cancellation of services, it did cause Charlotte to enter into the Amendment by threatening to allow such cancellation without proper notice. Therefore, Puget Sound Power & Light is unpersuasive.

Finally, IXC implies that Charlotte was not under duress because the Amendment was executed before IXC agreed to take on the MSA and related liabilities of AuBeta. IXC claims that Charlotte made a business choice between staying with AuBeta and facing an inevitable and immediate termination of service or entering into an extension with IXC. IXC states that it only agreed to take over the MSA and the related underlying carrier contracts because Charlotte agreed to enter into the extension. This is not credible.

---

[45] Id. at 442-43.

[46] See Eagle Pac. Ins. Co. v. Christensen Motor Yacht Corp., 135 Wn.2d 894, 901, 959 P.2d 1052 (1998) (quoting Hall v. Armstrong Cork, Inc., 103 Wn.2d 258, 261-62, 692 P.2d 787 (1984).

AuBeta assigned the MSA to IXC effective as of March 30, 2009, and AuBeta's representative signed the agreement on March 27, 2009. Similarly, AuBeta assigned its contract with Qwest Communications Company, LLC (one of the underlying carriers) effective as of March 27, 2009. In contrast, the Amendment was effective as of March 30, 2009, and signed by both Chaney and Durbhakula that same day. Given this timeline, IXC's argument is unpersuasive. AuBeta agreed to assign the MSA to IXC before Charlotte signed the Amendment. Further, IXC assumed both the MSA and the underlying service contract the same day that the Amendment was executed. There is no evidence that IXC waited until the Amendment was signed by Charlotte to negotiate with AuBeta and the underlying carriers.

Mistake

Charlotte argues that its failure to answer IXC's complaint was a mistake and not inexcusable neglect. We agree.

Whether a defendant presents a strong defense or a prima facie defense will affect how much scrutiny the trial court gives to the other White factors.

> [W]here the moving party is able to demonstrate a strong or virtually conclusive defense to the opponent's claim, scant time will be spent inquiring into the reasons which occasioned entry of the default, provided the moving party is timely with his application and the failure to properly appear in the action in the first instance was not willful. On the other hand, where the moving party is unable to show a strong or conclusive defense, but is able to properly demonstrate a defense that would, prima facie at least, carry a decisive issue to the finder of the facts in a trial on the merits, the reasons for his failure to timely appear in the action before the default will be scrutinized with greater care, as will the seasonability of his application and the element of potential hardship on the opposing party.[47]

Presentation of a strong defense justifies vacation of a default judgment even when other factors are not as persuasive because it serves the principals of equity.[48] "If a default judgment on a meritless claim is allowed to stand, justice has not been done."[49]

In Washington, courts have held that failure to respond is due to mistake in varying circumstances. In Boss Logger, Inc., v. Aetna Casualty & Surety Co., the defendant failed to respond to the complaint because "someone in the process lost the papers."[50] This court held that it was a mistake and not inexcusable neglect because there was a system in place for handling litigation, rather than a "systemic failure which would prevent all litigants from achieving actual notice to the [defendant]."[51] In Pfaff v. State Farm Mutual Automobile Insurance Co.,[52] the court held that the defendant's failure to answer the complaint resulted from a mistake where the defendant received service of the complaint, but an administrative assistant faxed the complaint to a wrong number and it never reached the person responsible for processing incoming complaints.[53] In Showalter v. Wild Oats,

---

[47] White, 73 Wn.2d at 352-53.

[48] TMT Bear Creek, 140 Wn. App. at 204-05.

[49] Id. at 205.

[50] 93 Wn. App. 682, 689, 970 P.2d 755 (1998).

[51] Id.

[52] 103 Wn. App. 829, 14 P.3d 837 (2000).

[53] Id. at 831, 836.

[54] the court held that the defendant's failure to file an answer was mistake where a paralegal at defendant's company asked another employee to deliver the complaint to the person responsible for processing such documents but the employee misunderstood the paralegal's request and never delivered the documents.[55]

Here, Charlotte's Registered Agent of Service sent IXC's summons and complaint to Charlotte via FedEx on June 12, 2009. It was received in Charlotte's mailroom on June 15, 2009. Charlotte's Controller is the designated liaison with the Registered Agents of Service in each state and is usually forwarded copies of all summons and complaints received from them. However, she did not receive IXC's complaint and it appears that the documents were lost in the mailroom. As in the cases cited above, the failure to respond was due to a mistake, not the willful intent to ignore the lawsuit or a systematic failure in the process. Further, Charlotte presented a strong defense to IXC's claims, acted diligently to vacate the judgment, and IXC will suffer no substantial harm upon vacation. Therefore, the reason for default should receive "scant" inquiry because equity requires a trial on the merits. Based upon the facts presented, the trial court abused its discretion in refusing to vacate the default judgment.

IXC argues that under Prest v. American Bankers Life Assurance Co.[56]

---

[54] 124 Wn. App. 506, 101 P.3d 867 (2004).

[55] Id. at 514.

[56] 79 Wn. App. 93, 900 P.2d 595 (1995).

and TMT Bear Creek,[57] Charlotte's failure to answer the complaint was inexcusable neglect. Neither case supports that argument.

In Prest, the person usually responsible for handling incoming complaints was assigned other duties and out of town when the plaintiff's complaint was forwarded from the insurance commissioner.[58] The court held that this was inexcusable neglect because the defendant had a duty to designate the responsibility for receiving complaints to another employee and to notify the state insurance commissioner of the change.[59] However, this court distinguished Prest in Boss Logger, pointing out that "the Prest court had already determined that the insurer had no defense to the plaintiff's claim prior to its discussion of inexcusable neglect" and that its holding was based on the fact that there was a systematic failure.[60]

Here, as we explained earlier in this opinion, Charlotte has a strong defense on the merits and there is no evidence of a systematic failure preventing Charlotte from receiving notice of all lawsuits filed.

For the same reasons, IXC's reliance on TMT Bear Creek is unpersuasive. In that case, the defendant did not respond to the complaint because the legal assistant in charge of processing the complaints was on an

---

[57] 140 Wn. App. at 191.

[58] Prest, 79 Wn. App. at 100.

[59] Id.

[60] Boss Logger, 93 Wn. App. at 689.

extended vacation and the temporary replacements were not trained on how to calendar incoming complaints.[61] This court held that the default was due to inexcusable neglect.[62] However, as in Prest, the defendant did not have a strong defense on the merits and the breakdown in internal procedure was not a one-time mistake, but would result in the defendant failing to receive any incoming notices during the time the legal assistant was on vacation.

Because of our resolution of the case on the above grounds, we need not address Charlotte's alternative argument that it was entitled to notice of the motion for order of default because it appeared below. Likewise, we need not address whether the priority of action rule applies to this case. Finally, we need not address whether IXC's allegedly inequitable conduct affects the determination of the issues in this case**.**

Charlotte also requests, pursuant to ER 201, that we take judicial notice of pleadings in the California Superior Court.[63] This request is based on Vandercook v. Reece.[64]

We decline the request because it is, in effect, an attempt to supplement the appellate record without complying with the provisions of RAP 9.11.[65]

---

[61] TMT Bear Creek, 140 Wn. App. at 213.

[62] Id.

[63] Request for Judicial Notice in Support of Appellant's Opening Brief at 1.

[64] 120 Wn. App. 647, 651, 86 P.3d 206 (2004).

[65] RAP 9.11(a):

> **Remedy Limited**. The appellate court may direct that additional

Specifically, the information in this pleading is not needed to fairly resolve this appeal and the additional evidence will not change the outcome of this case.

Vandercook,[66] on which Charlotte relies, is distinguishable because the issue there involved the trial court taking judicial notice of certain matters. That is not the case here because we are an appellate court, not a trial court. Accordingly, we do not consider the pleadings in that California case that are not in this appellate record.

We reverse and remand for further proceedings.

Cox, J.

WE CONCUR:

---

evidence on the merits of the case be taken before the decision of a case on review if: (1) additional proof of facts is needed to fairly resolve the issues on review, (2) the additional evidence would probably change the decision being reviewed, (3) it is equitable to excuse a party's failure to present the evidence to the trial court, (4) the remedy available to a party through postjudgment motions in the trial court is inadequate or unnecessarily expensive, (5) the appellate court remedy of granting a new trial is inadequate or unnecessarily expensive, and (6) it would be inequitable to decide the case solely on the evidence already taken in the trial court.

[66] Vandercook, 120 Wn. App. at 651.

Appelwick, J. Becker, J.