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

COREGIS INSURANCE COMPANY,	:	CIVIL ACTION
v.	:	
SALMANSON & FALCAO, LLC, et al.	:	NO. 00-5054

MEMORANDUM AND ORDER

HUTTON, J. May 10, 2002

Currently, before the Court are Plaintiff Coregis Insurance Company's Motion for Summary Judgment (Docket No. 17), Plaintiff's Statement of Undisputed Facts in Support of Its Motion for Summary Judgment (Docket No. 18), Defendants Salmanson & Falcao, LLC, Michael J. Salmanson and Linda P. Falcao's Answer to Plaintiff's Motion for Summary Judgment (Docket No. 21), Plaintiff's Motion to Compel Discovery Propounded to Michael J. Salmanson and Linda P. Falco at Deposition (Docket No. 28), Defendants' Response to Plaintiff's Motion to Compel Discovery and Emergency Cross-Motion for Sanctions (Docket No. 29), and Plaintiff's Response to Defendants' Cross-Motion for Sanctions (Docket Nos. 31, 34). For the reasons outlined below, Plaintiff's Motion for Summary Judgment is **GRANTED IN PART; DENIED IN PART**, Plaintiff's Motion to Compel is **DENIED AS MOOT**, and Defendants' Cross-Motion for Sanctions is **DENIED**.

I. BACKGROUND

Plaintiff Coregis Insurance Company ("Plaintiff" or "Coregis")

filed the instant Complaint for Declaratory Judgment on October 5, 2000 against Defendants Salmanson & Falcao, LLC, Michael J. Salmanson and Linda P. Falcao (collectively "the Defendants"). Coregis seeks a determination as to whether it is required to indemnify the Defendants from a quantum meruit judgment entered against Salmanson & Falcao, LLC ("Salmanson & Falcao") in the Court of Common Pleas of Philadelphia County on June 11, 2000.

Defendant Michael J. Salmanson ("Salmanson") was employed as an associate at the law firm of Mager, Liebenberg and White ("ML&W") from July of 1992 until June of 1997. In March of 1996, Lynn M. Bultena ("Bultena") retained the law firm of ML&W for representation in an action under the Federal False Claims Act. Salmanson drafted the contingent fee agreement under which ML&W agreed to represent Bultena and negotiated the terms on the firm's behalf. On June 10, 1997, Salmanson left ML&W and, along with Linda P. Falcao ("Falco"), established the law firm of Salmanson & Falcao, LLC. Bultena then terminated the services of ML&W and entered into an agreement with Salmanson & Falcao to complete any remaining legal services with regards to the False Claims Act case. In September of 1998, Bultena's claim settled for $2.88 million and Salmanson & Falcao received $864,000 in attorney's fees.

Following the settlement of Bultena's False Claims Act case, ML&W demanded that either Bultena or Salmanson & Falcao remit the attorney's fee to the firm. When no fee was remitted, ML&W filed

suit against Bultena, Salmanson & Falcao and its principals[1] alleging breach of contract and unjust enrichment/quantum meruit. Defendants turned to their Insurance Company, Coregis, to provide a defense. Previously, Coregis had issued Salmanson & Falcao a Lawyers Professional Liability Policy for the period from June 12, 1998 to June 12, 1999. Coregis defended the action on behalf of Salmanson & Falcao and appointed defense counsel. In June of 2000, a quantum meruit judgment was entered in favor of ML&W against Salmanson & Falcao in the amount of $183,600.[2]

On July 25, 2000, Salmanson & Falcao requested that Coregis appoint appellate counsel and post an appeal bond. Coregis refused on the grounds that the insurance policy did not cover the quantum meruit judgment and, therefore, Coregis was not obligated to fund an appeal. On October 5, 2000, Coregis filed the instant action seeking a declaratory judgment that the underlying judgment does not obligate Salmanson & Falco to pay a "loss" by reason of a "wrongful act." See Pl.'s Compl. at ¶ 26. In their Answer to Plaintiff's Complaint, Defendants included a counter-claim seeking a declaratory judgment requiring Plaintiff to pay the costs of

[1] Michael J. Salmanson and Linda P. Falco were dismissed as parties to the underlying lawsuit and the case proceeded against Salmanson & Falco, LLC and Bultena only.

[2] On March 26, 2002, the Superior Court of Pennsylvania vacated the judgment of the Court of Common Pleas of Philadelphia County and remanded the case "for the entry of judgment based on quantum meruit in conformity with Pennsylvania law . . ." Mager v. Bultena, 2002 WL 453209, at *7 (Pa. Super. Ct. March 26, 2002).

appealing the underlying judgment. See Defs.' Answer at 4-6. In addition, Defendants set forth a claim against Coregis for bad faith. See id. at 6-7. Coregis filed the instant Motion for Summary Judgment on October 1, 2001.

II. LEGAL STANDARD

A. Summary Judgment

Summary judgment is appropriate "if 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). The party moving for summary judgment has the initial burden of showing the basis for its motion. Celotex Corp. v. Catrett, 477 U.S. 317, 323, 106 S.Ct. 2548, 91 L.Ed.2d 265 (1986). Once the movant adequately supports its motion pursuant to Rule 56(c), the burden shifts to the nonmoving party to go beyond the mere pleadings and present evidence through affidavits, depositions, or admissions on file to show that there is a genuine issue for trial. See id. at 324. A genuine issue is one in which the evidence is such that a reasonable jury could return a verdict for the nonmoving party. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S.Ct. 2505, 91 L.Ed.2d 202 (1986).

When deciding a motion for summary judgment, a court must draw all reasonable 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, 113 S.Ct. 1262, 122 L.Ed.2d 659 (1993). Moreover, a court may not consider the credibility or weight of the evidence in deciding a motion for summary judgment, even if the quantity of the moving party's evidence far outweighs that of its opponent. Id. Nonetheless, a party opposing summary judgment must do more than just rest upon mere allegations, general denials or vague statements. Saldana v. Kmart Corp., 260 F.3d 228, 232 (3d Cir. 2001).

B. Contract Interpretation

Under Pennsylvania law,[3] the interpretation of the terms of an insurance contract is a question of law to be decided by the court. See PECO Energy Co. v. Boden, 64 F.3d 852, 855 (3d Cir. 1995); Travelers Cas. & Sur. Co. v. Castegnaro, 772 A.2d 456, 458 (Pa. 2001). Accordingly, where no genuine issue of material fact exists, the issue before the court need not be submitted to a jury. See Reliance Ins. Co. v. Moessner, 121 F.3d 895, 900 (3d Cir. 1997); Standard Venetian Blind Co. v. Am. Empire Ins. Co., 469 A.2d 563, 566 (Pa. 1983). When construing an insurance policy, the court must ascertain the intent of the parties as evidenced by the language of the written agreement. Castegnaro, 772 A.2d at 459;

[3] Neither party disputes the applicability of Pennsylvania law to the policy at issue. See Centennial Ins. Co. v. Meritor Sav. Bank, Inc., 1992 WL 164906, at *2 (E.D. Pa. July 6, 1992) (holding that "an insurance contract is governed by the law of the state in which the contract was made"), aff'd, 993 F.2d 876 (3d Cir. 1993).

Riccio v. Am. Republic Ins. Co., 705 A.2d 422, 426 (Pa. 1997). "When the policy language is clear and unambiguous, the court must give effect to the language in the contract." Castegnaro, 772 A.2d at 459; see also Med. Protective Co. v. Watkins, 198 F.3d 100, 103 (3d Cir. 1999). Conversely, where the policy is ambiguous, the ambiguous word or phrase must be construed in favor of the insured. Med. Protective Co., 198 F.3d at 103; Moessner, 121 F.3d at 900-01; Standard Venetian Blind, 469 A.2d at 566. The court must nonetheless interpret the policy with an eye toward avoiding ambiguities and giving effect to all of the provisions in the policy. Med. Protective Co., 198 F.3d at 103 (citing Little v. MGIC Indem. Corp., 836 F.2d 789, 793 (3d Cir. 1987)).

III. DISCUSSION

Coregis argues that it has no duty to indemnify Salmanson & Falcao's with regards to the quantum meruit judgment because such a judgment does not constitute a "loss" resulting from a "wrongful act" within the terms of the insuring agreement. See Pl.'s Mot. Summ. J. at ¶ 7. According to Coregis, the judgment is the result of Salmanson & Falcao's quasi-contractual obligation to pay ML&W for the work it performed on the Bultena matter and is therefore outside the scope of the policy provisions. See id. Defendants counter that the quantum meruit judgment "was by reason of at least one [w]rongful [a]ct within the meaning of the policy," and therefore Coregis is responsible for indemnifying Salmanson &

Falcao for the entire judgment. Defs.' Answer to Pl.'s Mot. Summ. J. at 4. The Court agrees with Coregis that the judgment at issue is not a "loss" incurred as a result of a "wrongful act" and therefore enters judgment in Plaintiff's favor on that ground.

A. Duty to Indemnify

Under Pennsylvania law, the duty to defend is distinct from the duty to indemnify. See Erie Ins. Exch. v. Transamerica Ins. Co., 533 A.2d 1363, 1368 (Pa. 1987). The duty to defend arises whenever the complaint filed by the injured party may potentially come within the policy's coverage. See Diloreto v. CNA Ins. Co., No. Civ. A. 98-3488, 2000 WL 45994, at *2 (E.D. Pa. Jan. 21, 2000). The duty to indemnify, however, is more limited and arises "only if it is established that the insured's damages are actually within the policy coverage." Lucker Mfg. v. Home Ins. Co., 23 F.3d 808, 821 (3d Cir. 1994). In the instant case, Coregis defended the underlying action subject to a reservation of rights, but now asserts that it has no duty to indemnify Defendants for the underlying judgment. Accordingly, the question before the Court is whether the quantum meruit judgment issued against Salmanson & Falcao constitutes a "loss" that resulted from a "wrongful act" within the terms of the policy, thus triggering Coregis' duty to indemnify. The Court holds that it does not.

Under the terms of the Insuring Agreement, Coregis agreed to "pay on behalf of any INSURED all LOSS . . . which any INSURED

becomes legally obligated to pay as a result of CLAIMS . . . made against any INSURED . . . by reason of any WRONGFUL ACT . . ." Pl.'s Statement of Undisputed Facts in Support of Mot. Summ. J., Ex. A ("Lawyers Professional Liability Coverage Unit"), at ¶ I.A. The policy defines "wrongful act" as

> any act, error, omission, circumstance, PERSONAL INJURY or breach of duty in the rendition of legal services for others in the INSURED'S capacity as a Lawyer, and arising out of the conduct of the INSURED'S profession as a Lawyers, or as a Lawyer acting in the capacity of an Arbitrator, Mediator or Notary Public.

Id. at ¶ VII.G. In the underlying case, the trial court imposed a quantum meruit judgment on Salmanson & Falco. Quantum meruit is an equitable, quasi-contractual remedy by which a contract is implied in law under a theory of unjust enrichment. See Hershey Foods Corp. v. Ralph Chapek, Inc., 828 F.2d 989, 998 (3d Cir. 1987). Under the facts of the instant case, the quantum meruit judgment does not constitute a "loss" resulting from any "wrongful act" of Salmanson & Falcao or its principals.

It is axiomatic that a client may terminate an attorney-client relationship at any time and for any reason, "notwithstanding a contract for fees." Mager v. Bultena, 2002 WL 453209, at *6 (Pa. Super. Ct. March 26, 2002). Upon termination, however, the former attorney has an action in quantum meruit to recover a reasonable fee for the time spent on the former-client's case. See id. Here, Bultena exercised his prerogative and decided to terminate his attorney-client relationship with ML&W in favor of representation

by Salmanson & Falcao. Salmanson & Falcao and its partners did not commit a "wrongful act" as defined by the terms of the policy by accepting Bultena's patronage. Equity merely demanded that ML&W be compensated for the time spent on Bultena's case prior to the termination of their services. Salmanson & Falcao did not dispute this entitlement and offered ML&W an amount based upon a reasonable fee multiplied by the hours Salmanson worked on Bultena's case while in ML&W's employ, but ML&W rejected this amount and pursued litigation. See Defs.' Answer, Exhibit B.

In support of their contention that the judgment at issue constitutes a "loss" resulting from a "wrongful act" within the meaning of the policy, Defendants point to the trial court's calculation of the quantum meruit judgment. See Defs.' Answer to Pl.'s Mot. Summ. J. at 5. According to Defendants, if the trial court intended to enter a judgment based solely on quantum meruit, the recovery should have been "based on a calculation of the hours worked by Salmanson while at ML&W multiplied by a reasonable hourly rate." Id. "Instead, the [c]ourt decided to enter a judgment based on a pro-rata split of the fee award . . .." Id. Defendants thus conclude that the trial court's judgment "must be based upon at least one predicate wrongful act of Salmanson[]" – namely, the failure to properly document all of his hours worked on the Bultena case. Id. Furthermore, Defendants allege that the trial court justified the "'pro rata' fee apportionment based upon the premise

that ML&W should be entitled to the same benefit of the bargain which Salmanson had secured for Salmanson & Falco." Id. at 6. Both of these actions, the Defendants argue, "would fall within either the 'breach of duty' or 'omission' prong of the wrongful act definition set forth in the policy." Id.

After the parties filed the instant motion and respective responses, the Superior Court of Pennsylvania vacated the quantum meruit judgment in the underlying lawsuit. See Mager v. Bultena, 2002 WL 453209 (Pa. Super. Ct. March 26, 2002). Specifically, the Superior Court took exception with the trial court's calculation of the fees owed to ML&W. In the underlying lawsuit, the trial court awarded ML&W a fee of twenty-five percent (25%) of the total amount based upon the thirty (30) documented hours of time, as well as other time that was undocumented, because the trial court concluded that it could not determine the total number of hours Salmanson worked on Bultena's case while with ML&W. See id. at *5. According to the Superior Court, such a calculation is "unsound as it fails to take into consideration the fact that under Pennsylvania law, upon Mr. Bultena's discharge of ML&W, the contingent fee agreement no longer existed and could not be revived, in while or in part, by the court." Id. at *6. As the court explained, "[w]hile the termination of the contract by Mr. Bultena created an immediate right in ML&W to compensation for all work performed and costs incurred pursuant to that contract, the

right included only quantum meruit compensation which is to be calculated based on the number of hours worked multiplied by a fair fee." Id. Therefore, the court vacated the judgment and remanded the case "for the entry of judgment based on quantum meruit in conformity with Pennsylvania law, namely, the number of hours devoted by ML&W to the cause of Mr. Bultena." Id. at *7.

Accordingly, the Court finds that the "loss" in this case did not result from any "wrongful act" of Salmanson & Falcao or its principals. Defendants themselves admit that if the trial court did not predicate the judgment on an alleged "wrongful act," "the judgment would have been limited to . . . the amount . . . based upon the amount of hours recorded by Salmanson while at ML[&]W multiplied by his regularly hourly rate." Defs.' Answer to Pl.'s Mot. for Summ. J. at 5. This is the exact calculation the Superior Court has instructed the trial court to apply on remand. See Mager v. Bultena, 2002 WL 453209, at *7 (Pa. Super. Ct. March 26, 2002).

Under Pennsylvania law, "[a]n insurer has a duty to indemnify its insured only if it is established that the insured's damages are actually within the policy coverage." Lucker Mfg. v. Home Ins. Co., 23 F.3d 808, 821 (3d Cir. 1994). Because the quantum meruit judgment cannot be properly considered a "loss" resulting from any "wrongful act," Coregis was not required to fund the appeal of the quantum meruit judgment, or indemnify Defendants for the amount of the judgment. Moreover, because no genuine issue of material fact

exists, the issue before the court need not be submitted to a jury. See Reliance Ins. Co. v. Moessner, 121 F.3d 895, 900 (3d Cir. 1997); Standard Venetian Blind Co. v. Am. Empire Ins. Co., 469 A.2d 563, 566 (Pa. 1983). Therefore, Coregis' Motion for Summary Judgment is granted with regards to Coregis' duty to indemnify.

B. Defendants' Bad Faith Counter-Claim

Plaintiff also seeks the entry of summary judgment in its favor with regards to Defendants' bad faith counter-claim. Section 8371 of the Pennsylvania Code creates a statutory cause of action for bad faith on the part of an insurer for actions that arise under the insurance contract. See 42 Pa. C.S. § 8371.[4] Bad faith on the part of an insurer has been defined as "'any frivolous or unfounded refusal to pay proceeds of a policy . . . [that] imports a dishonest purpose and means a breach of a known duty (i.e., good faith and fair dealing), through some motive of self-interest or ill will; mere negligence or bad judgment is not bad faith.'" Williams v. Nationwide Mut. Ins. Co., 750 A.2d 881, 887 (Pa. Super. Ct. 2000) (quoting MGA Ins. Co. v. Bakos, 699 A.2d 751, 754-55 (Pa. Super. Ct. 1997)).

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[4] Pennsylvania's bad faith statute provides:

> In an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured, the court may . . .
>
> (1) Award interest on the amount of the claim . . .
>
> (2) Award punitive damages against insurer.
>
> (3) Assess court costs and attorney's fees against the insurer.

42 Pa.C.S. § 8371; see also Marks v. Nationwide Ins. Co., 762 A.2d 1098, 1100 (Pa. Super. Ct. 2000).

Defendants claim that Coregis acted in bad faith by failing to pay for an appeal bond. See Defs.' Answer and Counter-Claim at ¶¶ 27-28. As noted above, Coregis properly denied coverage of the appeal of the quantum meruit judgment since the judgment was not a "loss" that resulted from a "wrongful act" and, therefore, was not covered by the policy. Since Coregis' denial of indemnification was proper and reasonable, Defendants cannot maintain a bad faith claim on this ground. "The court of appeals has consistently dismissed bad faith denial of coverage claims in cases in which there is no duty to defend and indemnify." Hyde Athletic Indus., Inc. v. Cont'l Cas. Co., 969 F.Supp. 289, 306 (E.D. Pa. 1997) (citing Kiewit E. Co. Inc. v. L&R Constr. Co., Inc., 44 F.3d 1194, 1206 n.39 (3d Cir. 1995)). Therefore, Defendants are unable to sustain a bad faith claim on this ground.

Defendants, however, further allege that Coregis violated its duty of good faith in its defense of the underlying litigation. First, Defendants claim that Coregis violated its duty of good faith by "steering" the defense from a covered claim to an arguably uncovered claim. See Defs.' Answer to Pl.'s Mot. Summ. J. at 16. According to Defendants, defense counsel, who was appointed by Coregis, argued that the judgment in the underlying action should be entered solely against the client, Lynn Bultena, so that Coregis would not have a duty to defend or indemnify. See id. Second, Defendants argue that Coregis acted in bad faith when its appointed

defense counsel failed to conduct adequate discovery. See id. at 21. Finally, Defendants assert that Coregis, in bad faith, failed to contribute an appropriate amount towards settlement of the underlying claim. See id. at 28.

While bad faith claims are generally predicated on an insurer's failure to pay the proceeds of an insurance policy, Pennsylvania courts have recognized that the statute applies to an insurance company's conduct during the pendency of the underlying litigation. See O'Donnell v. Allstate Ins. Co., 734 A.2d 901, 906 (Pa. Super. Ct. 1999). Specifically, the Pennsylvania Superior Court has found that "the broad language of section 8371 was designed to remedy all instances of bad faith conduct by an insurer, whether occurring before, during or after litigation. . . . [A]n insurer's duty to act in good faith [does not] end[] upon the initiation of suit by the insured." Id. The Court, therefore, agrees with Defendants that the scope of section 8371 encompasses bad faith actions on the part of the insurer during the pending litigation. In order to defeat a motion for summary judgment on a bad faith count, however, "a plaintiff must show that a jury could find by the stringent level of clear and convincing evidence, that the insurer lacked a reasonable basis for its handling of the claim and that it recklessly disregarded its unreasonableness." Williams v. Hartford Cas. Ins. Co., 83 F.Supp.2d 567, 570 (E.D. Pa. 2000), aff'd 261 F.3d 495 (3d Cir. 2001) (internal citation omitted).

Because Defendants have requested leave of this Court to file a supplemental response and because the bad faith issue has not been fully briefed by both parties, the Court denies with leave to renew Plaintiff's motion for summary judgment as to Defendants' bad faith counter-claim. An appropriate Order follows.

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

COREGIS INSURANCE COMPANY,	:	CIVIL ACTION
	:	
v.	:	
	:	
SALMANSON & FALCAO, LLC, et al.	:	NO. 00-5054

O R D E R

AND NOW, this 10th day of May, 2002, upon consideration of Plaintiff Coregis Insurance Company's Motion for Summary Judgment (Docket No. 17), Plaintiff's Statement of Undisputed Facts in Support of Its Motion for Summary Judgment (Docket No. 18) Defendants Salmanson & Falcao, LLC, Michael J. Salmanson and Linda P. Falcao's Answer to Plaintiff's Motion for Summary Judgment (Docket No. 21), Plaintiff's Motion to Compel Discovery Propounded to Michael J. Salmanson and Linda P. Falco at Deposition (Docket No. 28), Defendants' Response to Plaintiff's Motion to Compel Discovery and Emergency Cross-Motion for Sanctions (Docket No. 29), and Plaintiff's Response to Defendants' Cross-Motion for Sanctions (Docket Nos. 31, 34), IT IS HEREBY ORDERED that:

(1) Plaintiff's Motion for Summary Judgment is **GRANTED IN PART; DENIED IN PART**.

IT IS FURTHER ORDERED that Plaintiff Coregis Insurance Company's Motion for Summary Judgment is **GRANTED** with regards to Coregis' duty to indemnify.

IT IS FURTHER ORDERED that Plaintiff Coregis Insurance Company's Motion for Summary Judgment is **DENIED WITH LEAVE TO RENEW** with regards to Defendants' bad faith counter-claim.

The parties may renew the motion for summary judgment on Defendants' bad faith counter-claim within **thirty (30) days** of the date of this Order.

(2) Plaintiff's Motion to Compel Discovery is **DENIED AS MOOT**.

(3) Defendants' Cross Motion for Sanctions is **DENIED**.

BY THE COURT:

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HERBERT J. HUTTON, J.