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

NICK DARDOVITCH	:	CIVIL ACTION
v.	:	
MARK S. HALTZMAN, ESQ., et al.	:	NO. 97-52

MEMORANDUM

Dalzell, J. January 13, 1998

Plaintiff Nicholas Dardovitch has filed this action against Glen Eagle Square Equity Associates, Inc. (hereinafter "GESEA"), and the co-trustees of the GESEA Trust, Mark S. Haltzman, Esq. and Catherine A. Backos. Dardovitch initially sought an account of the Trust, which we ordered the trustees to provide on October 30, 1997. Thereafter, Dardovitch filed objections and exceptions to the account, seeking reversal of several trust disbursements, surcharge of the trustees, and indemnification from the Trust. Pursuant to 20 Pa. Stat. Ann. § 7186(a), plaintiff also filed additional claims for attorneys' fees and costs, and wrongful use of civil proceedings.

After four days' hearing last month, this memorandum will constitute our findings of fact and conclusions of law under Fed. R. Civ. P. 52(a).[1]

[1] We have jurisdiction because the parties' citizenship is diverse and, as will be seen, Dardovitch's claims as a "Group 3" beneficiary of the Glen Eagle Square Equity Associates Trust (hereinafter "the Trust") exceed $75,000. See infra, note 27, and accompanying text. The parties do not dispute, nor do we disagree, that Pennsylvania law applies.

I. Background

GESEA, a Pennsylvania corporation,[2] was formed in 1992 to purchase and operate the Glen Eagle Square Shopping Center in Chadds Ford, Pennsylvania. GESEA was unsuccessful in completing the acquisition, however, primarily because companies financing the transaction backed away from their commitments. In December of 1992, the shopping center was sold to another entity.

Thereafter, GESEA's sole business consisted of pursuing RICO claims against those believed to have defrauded the corporation out of "placement fees" in connection with the attempted purchase of the shopping center. To pursue those claims, Catherine Backos -- in both her individual and corporate capacity (as majority shareholder of GESEA) -- retained Mark S. Haltzman and Associates (hereinafter "MSH&A") to represent her and GESEA.[3] The resulting litigation, Glen Eagle Square Equity Assoc., Inc., et al. v. DSL Capital Corp., et al., No. 93-CV-2441 (E.D. Pa. filed May 7, 1993)(Waldman, J.)(hereinafter "RICO

[2] Defendant Catherine Backos is the majority shareholder in GESEA, with 55% of the shares. Nicholas Dardovitch and two of Ms. Backos's siblings each own a 15% equity interest.

[3] MSH&A in turn enlisted as co-counsel Skadden, Arps, Slate, Meagher and Flom. The parties here, however, do not dispute any aspect of the Skadden firm's role in this litigation.

action"), reached final settlement[4] on the first day of trial, July 27, 1994. Under the terms of that settlement, Ms. Backos and GESEA received from the remaining RICO defendants notes with long-term payout schedules in the aggregate amount of $994,000.[5]

After settling the RICO action, and sometime in the fall of 1994,[6] Ms. Backos and GESEA, again in consultation with

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[4] The RICO plaintiffs also reached an earlier settlement with some of the defendants, referred to by both parties as the "First Pasco Bank Settlement." Under the First Pasco settlement, the RICO plaintiffs received payments of $155,000 on March 23, 1994 and $25,000 on April 8, 1994.

[5] Based on the defendant trustees' submissions, which Dardovitch does not dispute, the following promissory notes, all non-interest bearing, were conveyed to the RICO plaintiffs:

> 1) $750,000, payable over ten years, from DSL Capital Corp., Hampton Mercantile Corp., Francis Barros, Stuart MacFarlane, Daniel Heffernan, Susan Lechowicz, and Benjamin Zitron.
>
> 2) $100,000, payable over three years, from Stephen R. Woods.
>
> 3) $88,000, payable over two years, from Theodore Jefferson.
>
> 4) $36,000, payable over three years, from Arthur Carroll.
>
> 5) $20,000, payable over two years, from Arthur Domike.

See Defs.' Supp'l Resp. at Ex. A.

[6] The precise date of signing and execution of the GESEA "Irrevocable Trust Agreement" is unclear. The agreement states that it is "made as of the 1st day of July," Trust Account at Ex. A at 1, but does not specify a year. Furthermore, different pages of the Trust appear to be computer-stamped with different dates. Cf. id. at 1, 6 (stamped "8/1/94 9/30/94")

(continued...)

Haltzman, established the GESEA Trust. The Trust's stated purpose was "to collect and administer the proceeds of the [RICO action]." Trust Account at Ex. A at 1, at ¶1. In conformity with that purpose, Ms. Backos and GESEA conveyed the RICO action promissory notes into the Trust res. To date, the Trust has collected $199,418.22 on those promissory notes and disbursed most of those funds. See Trust Account at 1-3.

In addition to being a 15% shareholder in GESEA, Dardovitch is also a direct beneficiary of the GESEA Trust. See generally Our Order of October 10, 1997. On that basis, we granted plaintiff's motion for partial summary judgment and ordered defendant trustees to provide an account of the GESEA Trust pursuant to 20 Pa. Stat. Ann. § 7181 (West Supp. 1997) and in conformity with Pa. Orphan's Ct. R. 6.1 (1997). Id. Defendants provided that account on October 30, 1997, to which plaintiff filed objections and exceptions and made additional claims pursuant to Pa. Stat. Ann. § 7186(a) (West 1997), and to which defendants responded in turn. After four days' hearing on the matter, we find that both defendants Backos and Haltzman breached their fiduciary duty as trustees of the GESEA Trust, and therefore plaintiff is entitled to relief.

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[6](...continued)
with id. at 2-5, 7 (stamped "8/1/94 9/22/94"). Plaintiff has not challenged the legitimacy of the Trust instrument, however, and all agree that the Trust was in fact created sometime in September of 1994, and thus further inquiry into the precise date of the document's genesis is unnecessary.

II. Analysis

Dardovitch contends that his triple-faceted status as creditor and shareholder of GESEA, as well as direct beneficiary of the GESEA Trust, gives him standing to object to several transactions occurring both before and after establishment of the Trust. We will consider his claims in turn.

A. Pre-Trust Claims

Dardovitch objects to a number of transactions that occurred before establishment of the Trust, including, inter alia, the existence and terms of GESEA's representation agreement with MSH&A as well as payments GESEA made to a group of creditors known as the "Hanaway Group." We find, however, that Dardovitch does not have standing to challenge those transactions.

Plaintiff's status as trust beneficiary does not accord him standing because the Trust was not established at the time the transactions took place. Although defendants Haltzman and Backos at various times held funds in a fiduciary capacity, i.e. as attorney and corporate director, respectively, this implied "trust" relationship is separate from Dardovitch's status as beneficiary pursuant to the GESEA Trust. The scope of his rights under the GESEA Trust are governed by the Trust instrument. See generally George T. Bogert, Trusts § 37 (6th ed. 1987). Thus, as a trust beneficiary he may inquire into these transactions only insofar as they are necessary for the trustees to act under the

Trust instrument, see infra, but Dardovitch may not raise wholesale objections to them outside of this capacity.

We likewise find that Dardovitch's status as shareholder[7] of GESEA is insufficient to grant him standing to challenge pre-Trust transactions. Assuming that we may construe the present action as a shareholders' derivative suit[8] -- a dubious proposition at best -- "[b]oth the federal and Pennsylvania Rules of Civil Procedure require that, prior to filing a derivative suit, a shareholder must either make a demand on the corporation to obtain the desired action or allege in the complaint the reasons for not making the effort." Garber v. Lego, 11 F.3d 1197, 1201 (3d Cir. 1993)(citing Fed. R. Civ. P. 23.1; Pa. R. Civ. P. 1506). Dardovitch admits that he made no demand on GESEA's other directors regarding the transactions for which he has brought suit here, and he has also failed to comply with Pennsylvania's strict requirements for showing excuse for

[7] Dardovitch also avers that as a creditor of GESEA -- a status that defendants vigorously dispute -- he has standing to object to the pre-Trust transactions. Plaintiff did not, however, proffer any legal authority or other support for his claim that as a creditor of GESEA -- which the Trust's "disbursement schedule" recognizes him as -- he is entitled to challenge all agreements reached and payments GESEA made with third parties. We therefore reject this argument on its face.

[8] A shareholder derivative suit "permits an individual shareholder to bring 'suit to enforce a corporate cause of action against officers, directors, and third parties.'" Kamen v. Kemper Fin. Serv., 500 U.S. 90, 95, 111 S.Ct. 1711, 1716 (1991)(quoting Ross v. Bernhard, 396 U.S. 531, 534, 90 S.Ct. 733, 736 (1970)) (emphasis in original).

demand.[9] Dardovitch is thus foreclosed from challenging GESEA's pre-Trust corporate transactions.[10]

Even if Dardovitch had complied with Pa. R. Civ. P. 1506, we find that he would be barred by the doctrines of laches and equitable estoppel from asserting claims against GESEA's pre-Trust transactions. Laches arises when a party's rights have been so prejudiced by the delay of another in pursuing a claim that it would be an injustice to permit the assertion of the claim against the party so prejudiced. Sprague v. Casey, 520 Pa. 38, 44, 550 A.2d 184, 187 (1988). A party asserting laches must show a delay arising from the other party's failure to exercise due diligence, and resultant prejudice. Kehoe v. Gilroy, 320 Pa. Super. 206, 212, 467 A.2d 1, 4 (1983).

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[9] The substantive aspects of the procedural requirements of demand or excusal, embodied in Pa. R. Civ. P. 1506, are a "restatement of existing law," and we may therefore look for guidance to case law developed before the Rule's adoption in 1952. See Garber, 11 F.3d at 1203.

"The right of an individual stockholder to act for the corporation is exceptional, and only arises on a clear showing of special circumstances . . . ." Wolf v. Pennsylvania R.R. Co., 195 Pa. 91, 94, 45 A. 936, 937 (1900)(holding that plaintiff failed to aver "facts sufficient to excuse the want of demand, and to meet the requirement that plaintiff must show every reasonable effort to get the corporation to act."). See also Wilson v. Brown, 269 Pa. 225, 112 A. 1, 2 (1920)(holding that demand would only be excused in narrow circumstances). "[I]n order to excuse demand under Pennsylvania law, the plaintiff must allege that a majority of the board of directors engaged in acts that are fraudulent; not that they merely exercised erroneous business judgment." Garber, 11 F.3d at 1203 (internal citation omitted).

[10] It logically follows that Dardovitch is estopped from challenging properly documented Trust reimbursements to Ms. Backos for payments (in the amount of $23,025.95) she personally made to "the Hanaway Group" on the Trust's behalf.

"The application of the equitable doctrine of laches does not depend upon the fact that a certain definite time has elapsed, but whether, under the circumstances of the particular case, the complaining party is guilty of want of due diligence in failing to act to another's prejudice." In re Jones, 442 Pa. Super. 463, 475, 660 A.2d 76, 82 (1995)(quoting Estate of Marushak, 488 Pa. 607, 413 A.2d 649, 651 (1980))(citation omitted). Equitable estoppel is a doctrine that prevents one from doing an act differently from the manner in which another was induced by word or deed to expect. Council of Plymouth Township v. Montgomery County, 109 Pa. Cmwlth. 616, 625, 531 A.2d 1158, 1162 (1987). Its essential elements are inducement and justifiable reliance on that inducement exhibited by a change in one's condition to his or her detriment. Cosner v. United Penn Bank, 358 Pa. Super. 484, 488, 517 A.2d 1337, 1339 (1986).

In her capacity as President of GESEA, Ms. Backos provided Dardovitch with advance notice and later minutes of shareholders' meetings and copies of documents, including the February 12, 1993 "Proposal for Representation"[11] and the January 25, 1994 "Amendment to Representation Agreement". Dardovitch thus was aware of and well understood GESEA's fee arrangements

[11] Although the February 12, 1993 letter is in fact titled "proposal for representation," for the reasons discussed later in this memorandum we find that the letter constitutes a valid representation agreement between the parties. Moreover, we note that plaintiff himself referred to this letter as a "Representation Agreement" in his communications with defendants. See Hrg. Ex. D-3.

with Haltzman and GESEA's dealings with the Hanaway Group. Despite this information, Dardovitch failed to raise a substantial objection to these pre-Trust transactions until some months into this litigation. See Hrg. Exs. D2-D4, D11, D14; Trial Transcript, Dec. 18, 1997, at 290-96, 298-307. In the meantime, Haltzman, justifiably relying upon the existence of a representation agreement with GESEA based on those documents, rendered significant services to the corporation and Dardovitch as a shareholder thereof. Having failed to object contemporaneously to (1) the representation agreement, (2) GESEA's dealings with the Hanaway Group, or (3) the other pre-Trust corporate activities to which he now takes exception, and having induced detrimental justifiable reliance on defendants' part, Dardovitch is estopped from asserting those objections before us.

B. Post-Trust Transactions

Dardovitch also challenges a number of Trust disbursements by defendant co-trustees Backos and Haltzman.[12]

The trustees argue that the doctrine of laches similarly limits or bars completely our scope of review of Trust activity. We agree with the trustees that the doctrine of laches

[12] We resolved the lion's share of plaintiff's objections and exceptions on the record during the four days of hearings in this matter. Of particular note is the parties' resolution of the many objections which plaintiff raised because of the absence of documentation to support certain Trust disbursements. Thus, we will address only the parties' unresolved differences here.

applies to actions regarding the enforcement and interpretation of trust agreements. See DiLucia v. Clemens, 373 Pa. Super. 466, 472, 541 A.2d 765, 768, alloc. denied, 520 Pa. 605, 553 A.2d 968 (1988). Here, however, Dardovitch has a clear and convincing reason to excuse his delay in objecting to disbursements under the Trust: the trustees steadfastly refused to provide plaintiff with any information about the Trust until after this suit began. Indeed, Dardovitch did not even receive a copy of the Trust instrument until April 29, 1997. See N.T. Dec. 19, 1997, at 420. Thus, his pre-suit failure to object to the trustees' administration of the Trust is wholly excusable.

Furthermore, it is axiomatic that in civil suits concerning a trust, all of a trustee's actions are subject to the court's scrutiny and control. See In re Estate of Thompson, 426 Pa. 270, 281, 232 A.2d 625, 630 (1967). Thus, Dardovitch having properly brought an account of the Trust before us, we need not look to Dardovitch's conduct to inquire into the validity of that account. To the contrary, we are compelled to exercise our supervisory power because Mark Haltzman, Esq. enjoys the double status of trustee and beneficiary of the GESEA Trust. The sentinel of judicial review must be more vigilant when a trustee engages in self-dealing which may result in a breach of his fiduciary duties: "He that is intrusted [sic] with the interest of others, cannot be allowed to make the business an object of interest to himself; because, from the frailty of nature, one who has the power, will be too readily seized with the inclination to

use the opportunity for serving his own interest at the expense of those for whom he is intrusted [sic]." Beeson v. Beeson, 9 Pa. 279, 284 (1848).

We now turn to a review of the account and Dardovitch's objections and exceptions to it. Once a trust account has been provided and a beneficiary has submitted his objections, the burden is on the trustee to justify his conduct with respect to those items in question. See Bogert at § 143; 2A Scott on Trusts § 172 at 452-3 (4th ed. 1987); see also In re Strickler's Estate, 354 Pa. 276, 277, 47 A.2d 134, 135 (Pa. 1946). All obscurities and doubts will be resolved against the trustees, and failure of the trustees to provide receipts, vouchers, or other documentation to support objected-to transactions is sufficient ground to disallow them. See Bogert at § 143, at 502; Scott at § 172, at 452.

1. Payment of legal fees and expenses to Mark S. Haltzman & Associates

The remaining objected-to Trust disbursements are those payments to co-trustee Mark Haltzman and his law firm for legal fees and expenses. Dardovitch has objected wholesale to payments for legal fees and expenses made from the Trust to defendant Haltzman, and to reimbursements to defendant Backos for payments she made to Haltzman.

As we explained above, Dardovitch may not raise plenary objections here to the GESEA's representation arrangement with MSH&A. A number of disbursements for legal fees and expenses

made under the Trust, however, were made either (1) pursuant to provisions of the Trust which reference the representation agreement, or (2) under color of the trustees' interpretation of the representation agreement. Thus, by the terms of the Trust, in order to assess the propriety of certain disbursements recorded in the Trust account, we must pierce the face of the document to the representation agreements incorporated by reference therein.[13]

a. Scope of Representation

As a preliminary matter, the parties disagree over the proper characterization of legal services rendered. In their trust account, the trustees segregate these disbursements to Haltzman for legal fees and expenses into two categories: (1) payments made pursuant to the contingent fee agreement and ¶2(b)(i) of the Trust for services in the RICO action prior to its settlement and dismissal; and (2) payments made pursuant to ¶3(i) of the Trust for services rendered, billed on an hourly basis.[14] Dardovitch objects to this segregation, arguing that

[13] Our consideration of the settlors' intent, which "is the guide primarily to be followed in interpreting the intended effect of the [trust]," In re Wolters' Estate, 359 Pa. 520, 525, 59 A.2d 147, 149 (1948), does not demand a different conclusion. The settlors of the Trust also were the litigants in the RICO action who approved the representation agreements referenced in the Trust.

[14] As a preliminary matter, we reject defendants' half-hearted contention that some payments made for services rendered to the Trust are separable because they were rendered by Michael J. Harrington, Esq., who also represented defendant Backos in (continued...)

collection and protection of proceeds from the RICO action is within the scope of the representation agreement, and therefore should be properly included in the calculus of the contingent fee pursuant to ¶2(b)(ii) of the Trust.

In order to determine the scope of MSH&A's representation of GESEA, we turn to the documents[15] comprising the representation agreement itself. Among other things which

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[14](...continued)
this suit. The trustees made no attempt to separate these disbursements between Harrington and Haltzman in their trust account, listing disbursements for legal fees only to "MSH&A," or "Mark S. Haltzman and Associates." see Trust Account at 1. Moreover, Harrington shares offices with Haltzman, which perhaps explains the uncanny similarity of all of their respective submissions to the Court. Whatever their true business relationship, we have little trouble concluding that their services are not analytically severable here.

[15] Although defendant Backos testified at length regarding her understanding of agreements made between GESEA and defendant Haltzman, we do not accord that aspect of her testimony much weight. We do not question Ms. Backos's level of sophistication in business affairs -- quite to the contrary, her testimony showed her to be an intelligent and very capable businesswoman -- but it is evident from these proceedings that in legal matters she relied exclusively on Haltzman and his firm. Indeed, Haltzman's firm represented her even in this litigation. See supra. Thus, it is perhaps not surprising that Ms. Backos's testimony proceeded in virtual lockstep to support defendant Haltzman's various arguments before us.

Furthermore, to the extent that Ms. Backos's testimony is derived from her own understanding -- rather than Haltzman's influence on that understanding of legal matters -- we also reject it as self-serving. At the time that Ms. Backos entered into representation agreements with Haltzman, she was most influenced by the financial pressures which eventually forced her to file for bankruptcy. See Hrg. Ex. P-25; N.T. Dec. 16, 1997, at 157-167. Accordingly, we find that her construction of these agreements arose almost wholly out of her own individual financial interests, and improperly ignored the interests of GESEA, which she as majority shareholder is required to consider.

Haltzman omitted from his contingent fee agreement with GESEA, see infra, is an explicit statement of the scope of representation that the fee agreement embraces. As a matter of contract law, Haltzman's status as drafter of the document requires that all ambiguities be construed against him. All-Pak, Inc. v. Johnson, 694 A.2d 347, 351 n.7 (Pa. Super. 1997)(citing Gallagher v. Fidelcor, Inc., 441 Pa. Super. 223, 657 A.2d 31, alloc. denied, 544 Pa. 675, 678 A.2d 365 (1996)).

Furthermore, in failing explicitly to set forth the scope of representation in the contingent fee agreement, Haltzman also breached his duty of professional responsibility as set forth in Pa. R. Prof. Conduct 1.5(c), which provides, inter alia, that:

> A contingent fee agreement shall be in writing and shall state the method by which the fee is to be determined, including the percentage or percentages that shall accrue to the lawyer in the event of settlement, trial or appeal, litigation and other expenses to be deducted from the recovery, and whether such expenses are to be deducted before or after the contingent fee is calculated.

Id. (emphasis added). In addition, although Haltzman stridently asserts that the agreement should be construed to have terminated upon settlement of the RICO action, he has to date still not provided GESEA with a written statement to that effect required

by Rule 1.5(c).[16] We therefore decline to endorse an interpretation of the representation agreement which would place Haltzman in further violation of the Pennsylvania Rules of Professional Conduct.

As stated earlier, we are also mindful of defendant Haltzman's status as co-trustee of the Trust. Thus, we must examine these self-dealing transactions -- wherein Haltzman passes funds from his trustee's pocket to his attorney's pocket -- for possible breach of fiduciary duty. The test of forbidden self-dealing is whether the fiduciary had a personal interest in the subject transaction of such a substantial nature that it might have affected his judgment in material connection. In re Downing's Estate, 162 Pa. Super. 354, 359, 57 A.2d 710, aff'd 359 Pa. 534, 59 A.2d 903 (1948)(per curiam)(citing 2 Scott on Trusts, § 170.12 at 877; Restatement (Second) of Trusts, § 170(1) at comment h (2d ed. 1959)). "[T]he rule [forbidding self-dealing] is inflexible, without regard to the consideration paid, or the honesty of intent. Public policy requires this, not only as a shield to the parties represented, but as a guard against temptation on part of the representative." Chorpenning's Appeal, 32 Pa. 315, 316 (1858). Here, as long as Haltzman's interests are fixed by the contingent fee, they align with the interests of

[16] "Upon conclusion of a contingent fee matter, the lawyer shall provide the client with a written statement stating the outcome of the matter and, if there is a recovery, showing the remittance to the client and the method of its determination." Id.

the Trust, i.e. both parties equally benefit on collection of the Trust's promissory notes, and thus his actions as trustee are unimpeachable on this basis. Were we also to allow him to pay himself on an hourly basis to represent the Trust, Haltzman might be influenced more by the accumulation of hours spent in the Trust's service rather than the discipline on those hours that his self-interest would impose under the contingent fee regimen.[17]

Lastly, as a matter of common sense the contingent fee cannot be read to exclude collection of the settlement proceeds.[18] We suspect that few lawyers would rest with the hope

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[17] In so stating, we need not reach the question of whether Haltzman was actually motivated by self-interest in interpreting the representation as he did. The extent of the fiduciary's disqualifying interest need not be such as "did affect his judgment" but merely such as "might affect his judgment." Downing's Estate, 162 Pa. Super. at 360.

We recognize that a trustee's conflict of interest may be excused if it was within the contemplation of the settlor when she created the Trust. See, e.g., In re Flagg's Estate, 365 Pa. 82, 88-89, 73 A.2d 411, 414-15 (1950). Here, however, we reject any such ratification by Ms. Backos -- who speaks for both settlors in her individual and corporate capacity -- because of Haltzman's excessive influence on her views. See supra, note 15.

[18] Although MSH&A's representation agreement was later amended to allow him to receive the first $150,000 of settlement proceeds received, see Trust Account at Ex. B at 5, he retained a contingent fee percentage on funds collected in excess of $300,000. See Trust Account at Ex. B, at 5 (January 25, 1994 Amendment to Representation Agreement), at ¶4 ("In addition to [expenses and the priority, MSH&A] will be entitled to receive thirty . . . percent of the next $1,700,000 received in the [RICO action], whether by settlement or otherwise."); id. at ¶5 ("In addition to [the amounts set forth in ¶4], MSH&A shall be entitled to receive fifteen . . . percent of any amount received in the [RICO action] in excess of $2,000,000, whether by settlement or otherwise."). The amendment does not change the

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of 30% of a paper settlement, but not promptly seek collection of the real money that will turn that paper into cash. Indeed, the documents upon which Haltzman seeks to rely notably confirm our suspicion, stating that Haltzman is to receive his fees only on moneys actually "recovered" or "received." See Trust Account at Ex. B at 2 (February 12, 1993 Representation Agreement)(limiting contingency to "30% of any amount recovered"); id. at 5 (January 25, 1994 Amendment to Representation Agreement), at ¶2 (providing for $150,000 priority "of any recovery received in the [RICO action]"); id. at 6, at ¶4 (providing for 30% contingency "of the next $1,700,000 received in the [RICO action]"); id. at ¶5 (providing for 15% contingency "of any amount received in the [RICO action] in excess of $2,000,000").

Thus, we conclude that the contingent fee representation agreement between defendant Haltzman and GESEA should be construed to cover the collection of the RICO settlement notes. To permit Haltzman to "double-dip"[19] on the

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[18](...continued)
contingent nature of Haltzman's fee, but only the order of payment. Moreover, to permit Haltzman drastically to change the scope of the contingent fee agreement in mid-representation would also be contrary to his duties of professional responsibility. See Pa. R. Prof. Conduct 1.5(c) at comment 2 (stating that a lawyer should not structure a fee agreement "whose terms might induce the lawyer improperly to curtail services for the client or perform them in a way contrary to the client's interest").

[19] Indeed, Haltzman may even be "triple-dipping" on some of the settlement proceeds, thanks to a 25% attorney's fee assessed on certain late payments by the RICO defendants. See Defs.' Supp'l Resp. at Ex. A.

collection efforts would be illogical, unethical, and contrary to the parties' agreement.

b. Payment of Legal Fees and Expenses

Having determined that all payments Haltzman received in this action are governed by the contingent fee agreement,[20] we will now assess the propriety of disbursements made for legal fees and expenses, which is provided for in the Trust instrument at paragraphs 2(b)(i)-(ii):

> [A]t such time and from time to time as the Trustees shall determine in their sole discretion [the Trustees shall] dispose of the corpus and income of the Trust in accordance with Exhibit B[21] as follows:
> (i) to the payment of all expenses incurred by the law firm of Mark S. Haltzman and Associates in

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[20] Dardovitch also argued that we should consider two shareholders' agreements, dated May 14, 1993 and August 31, 1993, in our interpretation of the representation agreement between Haltzman and GESEA. These documents, however, are not relevant to the determination of the contractual relationship between those two parties. Rather, they are appropriate to evaluating the directors' corporate authority in entering into such an agreement on behalf of GESEA. As we emphasized supra, note 8 and accompanying text, such contentions are more properly the subject of a shareholders' derivative action, for which an allegation of demand or showing of futility is required by Pennsylvania law.

Moreover, plaintiff's argument in relying on these agreements was that the defendant Haltzman's fees were capped at 30%, including expenses. That provision appears only in the May 14, 1994 shareholders' agreement, which was superseded by the August 31, 1994 shareholders' agreement and therefore appears to be without legal effect.

[21] Although the instrument references "Exhibit B," no such exhibit was appended to any copy of the Trust submitted to us by the either party.

> connection with the prosecution of the [RICO action],
> (ii) to the payment of all legal fees in strict accordance with the engagement agreement entered into that provides for the payment to Mark S. Haltzman and Associates of the first $150,000 received, the second $150,000 shall be allocated to the Trust and thereafter, thirty percent (30%) of all proceeds coming into the Trust by virtue of the Promissory Notes listed on

> Schedule A[22] shall be paid to Mark S. Haltzman and Associates provided, however, that this amount shall not exceed, including the $150,000, the sum of $352,201[.]

Trust Account at Ex. A.

As to the payment of legal expenses, the trustees are authorized to reimburse them in full, whether they occur in connection with the RICO action or with administration of the Trust. See id. at ¶2(b); id. at ¶3(i)(providing that the trustees may "pay the ordinary and necessary expenses of administration"). The trustees produced sufficient documentation of these Trust disbursements, including itemized legal bills, checks written on account of the Trust, and extensive testimony at the hearing by both trustees, and thus we find that they are allowable.[23]

Second in priority of Trust disbursements is the payment of legal fees. In addition to being governed by the directions provided in ¶2(ii) of the Trust, the parties agreed at the hearing that the $150,000 priority payment to MSH&A provided thereunder includes non-retainer payments made to Skadden, Arps, Slate, Meagher, and Flom, as well as payments made from the pre-Trust "First Pasco Bank Settlement." Thus, having received

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[22] Again, we note that though the Trust instrument references "Schedule A," neither party included such a schedule in their Trust submissions.

[23] In particular, those expense-related disbursements allowable here are $3,338.05 to Catherine Backos, and $2,254.46 to MSH&A for "Trust Litigation" unrelated to the RICO settlement. See Trust Account at 1.

$145,848.97 toward that $150,000 prior to the Trust's creation, MSH&A was entitled to the next $4,151.03 the Trust received. See Trust Account at 2; id. at Ex. A at 8; Defs.' Resp. Exceptions at Ex. 1 at 3. After that, the next $150,000 of settlement proceeds should have been paid to next-in-line beneficiaries, with MSH&A resuming participation through its 30% fee contingency -- up to an additional $202,201 -- on all funds received thereafter.[24] See ¶2(b)(ii). Given that $199,418.22 has through the date of hearing been received by the Trust, see Trust Account at 1, the amount to date which should have been properly paid to MSH&A was:

Item	Charge	Res
Total Received:		$199,418.22
Less ¶2(b)(i) Expenses:	$ 5,592.51	$193,825.71
Less ¶2(b)(ii)MSH&A Priority:	$ 4,151.03	$189,674.68
Less ¶2(b)(ii)Trust Priority:[25]	$150,000	$ 39,674.68
¶2(b)(ii)Contingent Fee:	$39,674.68 x 30% = $11,902.40	
Total due MSH&A to date:	$11,902.40 + $4,151.03 =	$16,053.43

This order of payment was not followed. Instead, MSH&A received a total of $62,799.17 in Trust disbursements, an excess

[24] In this regard, we note that the Amended Representation Agreement and the Trust provision appear inapposite. Here, however, we are concerned only with the scope of the trustees' duties, which are dictated by the Trust Agreement, and authorize payment to MSH&A up to $352,201. We leave for another day the resolution of any conflict between the Trust instrument and the fee agreement.

[25] As we read the instrument, the $150,000 Trust priority should be disbursed to the ¶2(b)(iii) creditors, i.e. "Lynn and Connie Hanaway, Craig Howe, and Charlene Chaffee . . . but only to the extent such person has executed an agreement granting to such party an assignment of proceeds from the Promissory Notes," id., and then to ¶2(b)(iv) "Group 3 creditors on Schedule B on a pro rata basis." Id.

we suspect is largely due to Haltzman's claim that "Trust litigation" fees were not included in the contingent fee representation agreement and correlative Trust provision. Thus, we will surcharge[26] defendant co-trustee Mark Haltzman, who received these payments on behalf of MSH&A, for the difference between these two amounts (minus reimbursement for expenses), or $43,407.69, and this surcharge shall be paid to the Trust.

C. Attorney's Fees for Failure to Account

Dardovitch also moves for surcharge of the trustees or, in the alternative, indemnification from the Trust for attorney's fees incurred in this action. See Pl.'s Exceptions and Objections at ¶¶ 55-59.

We agree that plaintiff is entitled to attorney's fees for pressing this litigation. Backos and Haltzman spent the better part of this long, acrimonious litigation resisting

[26] Surcharge is the penalty imposed for failure of a trustee to exercise common prudence, skill and caution in the performance of his fiduciary duties, and is imposed to compensate beneficiaries for the loss caused by the fiduciary's want of care. Estate of Munro v. Commonwealth Nat'l Bank, 373 Pa. Super. 448, 452, 541 A.2d 756, 758 (1988), alloc. denied, 520 Pa. 607, 553 A.2d 969 (1989) (citing Estate of Stephenson, 469 Pa. 128, 138, 364 A.2d 1301, 1306 (1976)). The standard of care imposed upon a trustee is that which a man of ordinary prudence would practice in the care of his own estate. In re Estate of McRea, 475 Pa. 383, 387, 380 A.2d 773, 775 (1977). One seeking to impose a surcharge has the burden of proving that the fiduciary failed to meet the duty of care owed to the estate. In re Bard's Estate, 339 Pa. 433, 437, 13 A.2d 711, 713 (1940); In re Estate of Dobson, 490 Pa. 476, 417 A.2d 138 (1980). The purpose of surcharge, however, "is reimbursement for losses, not punishment of the fiduciary guilty of nonfeasance." In re Francis Edward McGillick Foundation, 406 Pa. Super. 249, 266, 594 A.2d 322, 331 (1991), rev'd on other grounds, 642 A.2d 467 (1994).

Dardovitch's demand to provide an account or even a copy of the Trust instrument, insisting from the beginning that he was not a beneficiary of the Trust. See, e.g., Hrg. Ex. P-18 ("Please be advised that Nick Dardovitch is not a beneficiary of the Trust Agreement, as the beneficiaries of the Trust are [GESEA] and Catherine Backos. Accordingly, even if the information you requested in your letter was appropriate (which it is not), he is not entitled to an accounting."). Moreover, to this day the trustees continue to deny that plaintiff is entitled to an accounting -- though, notably, they have retreated to claiming that he is an "incidental beneficiary" -- despite our Order of October 10, 1997, in which we stated that "[i]t would be hard to imagine a clearer example" of a trust beneficiary than one in plaintiff's position. Id. at ¶l.[27] In light of the fact that Haltzman is himself a practicing attorney, and we have, as a result of the account, uncovered significant instances of his improper self-dealing, the trustees' failure to recognize basic principles of trust law is a breach of fiduciary duty that can only have resulted from bad faith or, at a minimum, gross negligence. Thus, we find that the trustees' refusal to provide an account to Dardovitch alone is sufficient grounds to surcharge

[27] Indeed, we noted in that Order that the "disbursement schedule" incorporated into the Trust listed Dardovitch as receiving disbursements from the Trust of $104,995.97. See Trust Account at Ex. A at 8. We further note that Dardovitch shared equal priority with Ms. Backos, who are both listed for distribution as Group 3 claimants under the same Trust provisions. Id.

them with attorney's fees and costs for this account. See In re Lewis' Estate, 349 Pa. 455, 462, 37 A.2d 559, 563 (1944); In re Estate of Vaughn, 315 Pa. Super. 354, 361, 461 A.2d 1318, 1321 (1983); Tonuci v. Lennon, 186 Pa. Super. 522, 524, 142 A.2d 745, 746 (1958).

We hasten to add, however, that we do not find both trustees equally liable. Haltzman has contrived to become the dominant influence in the Trust's dealings with Dardovitch, both before and after the filing of this action. See supra notes 13, 14. Throughout that time, he has maintained an arrogant and cavalier attitude towards his duties as trustee, alternately stonewalling and threatening plaintiff, a beneficiary of the Trust, at every turn. Exemplary of his conduct and tone is a letter written to plaintiff's counsel shortly before the institution of this suit, which warns that

> to the extent that your office decides to bring litigation which would be improper based upon the fact that Mr. Dardovitch is not a beneficiary of the Trust, the Trust will seek to hold your firm, as well as Mr. Dardovitch, liable for all of its costs and expenses and will seek damages for malicious prosecution and abuse of process. Your letter is apparently a continuation of Mr. Dardovitch's past guerilla tactics in attempting to extort money to which he was not entitled.

Hrg. Ex. P-18.

While Ms. Backos's conduct as co-trustee[28] may have resulted from excusable negligence -- and improperly influenced legal advice -- Haltzman's conduct is not similarly pardonable. Thus, we will surcharge defendant co-trustee Haltzman for the full amount of Dardovitch's attorney's fees and costs.[29]

D. Wrongful Use of Civil Proceedings and Abuse of Process

Dardovitch also argues that the counterclaims filed by the defendants in this action support a statutory claim of wrongful use of civil proceedings.[30] See Pl.'s Objections and

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[28] "It is the general rule that '[a] trustee is not liable to the beneficiaries for a breach of trust committed by a co-trustee'." Herr v. United States Cas. Co., 347 Pa. 148, 150, 31 A.2d 533, 534 (Pa. 1943)(quoting Restatement (Second) of Trusts, § 224(1) (2d ed. 1959)); see also In re Clabby's Estate, 338 Pa. 305, 310, 12 A.2d 71 (1940). A co-trustee will be held responsible, however, if she "improperly delegates the administration of the trust to [her] co-trustee; or . . . by [her] failure to exercise reasonable care in the administration of the trust . . . [enables her] co-trustee to commit a breach of trust." Herr, 347 Pa. at 150 (citing Restatement at § 224(2)(b), (d)). While there is ample evidence of Ms. Backos's neglect as trustee which might be construed to support such a claim, for the reasons stated supra note 15 we think that her co-trustee's malfeasance should not be imputed to Ms. Backos.

[29] In addition, we rely on Fed. R. Civ. P. 54(d)(2), which grants courts broad discretion in awarding costs and attorney's fees when a defendant acts "in bad faith, vexatiously, wantonly, or for oppressive reasons." Alyeska Pipeline Serv. Co. v. Wilderness Soc'y, 421 U.S. 240, 258, 95 S.Ct. 1612, 1622 (1975)(quoting F.D. Rich Co., Inc. v. United States for the Use of Indus. Lumber Co., Inc., 417 U.S. 116, 129, 94 S.Ct. 2157, 2165 (1974); cf. 42 Pa. Cons. Stat. § 2503 (allowing attorney's fees and costs under similar circumstances).

[30] Plaintiff also claimed common law abuse of process, but provided no argument or case law in support thereof. We therefore reject that claim on its face.

Exceptions at ¶¶ 60-72. 42 Pa. Cons. Stat. § 8351 (West 1982) sets forth the elements required for this cause of action:

> (a) Elements of action.-- A person who takes part in the procurement, initiation or continuation of civil proceedings against another is subject to liability to the other for wrongful use of civil proceedings:
>
> (1) He acts in a grossly negligent manner or without probable cause and primarily for a purpose other than that of securing the proper discovery, joinder of parties or adjudication of the claim in which the proceedings are based; and
>
> (2) The proceedings have terminated in favor of the person against whom they are brought.

Id. The burden of proof for this claim is prescribed by 42 Pa. Cons. Stat. § 8354 (West 1982), which provides:

> In an action brought pursuant to this subchapter the plaintiff has the burden of proving, when the issue is properly raised, that:
> (1) The defendant has procured, initiated or continued the civil proceedings against him.
> (2) The proceedings were terminated in his favor.
> (3) The defendant did not have probable cause for his action.
> (4) The primary purpose for which the proceedings were brought was not that of securing the proper discovery, joinder of parties or adjudication of the claim on which the proceedings were based.
> (5) The plaintiff has suffered damages as set forth in section 8353 (relating to damages).

Id. We dismissed the counterclaims of defendants Backos and GESEA against plaintiff by Order of March 27, 1997,[31] and the counterclaims of defendant Haltzman by Order of August 12, 1997. Thus, Dardovitch has satisfied elements one and two of the claim.

The third element of lack of probable cause is also easily resolved. In dismissing defendants' counterclaims,[32] we found them to be completely meritless. See Our Order of August 12, 1997 at ¶f ("[I]t is clear that nowhere in his answer or in his response to plaintiff's motion to dismiss the counterclaims does [Haltzman] aver that the plaintiff is using legal process to seek anything other than the relief the plaintiff requests in his complaint . . . .").

That flaw, however, is to be distinguished from the fourth requirement of § 8354, which requires not only lack of probable cause but malicious ulterior motive. See Mi-Lor, Inc. v. DiPentino, 439 Pa. Super. 636, 639-40 654 A.2d 1156, 1157-58 (1995); Ludmer v. Nernberg, 433 Pa. Super. 316, 323, 640 A.2d

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[31] By Order of August 5, 1997, we amended our Order of March 27, 1997 to dismiss without prejudice the counterclaims of defendants Backos and GESEA. See id. at 2. A dismissal without prejudice, however, still may constitute favorable termination under 42 Pa. Cons. Stat. § 8351. See Robinson v. Robinson, 362 Pa. Super. 568, 525 A.2d 367 (1987), appeal dismissed 518 Pa. 63, 540 A.2d 529 (1988); Morris v. Scardelletti, Civ. A. No. 94-3557, 1994 WL 675461 at *9 (E.D. Pa. Nov. 23, 1994).

[32] Although we dismissed the counterclaims of defendants GESEA and Backos by separate Order for failure to respond to plaintiff's motion to dismiss, all of the defendants set forth verbatim identical counterclaims. Thus, our analysis of the merit of Haltzman's counterclaims applies equally to those of the other two defendants.

939, 942 (1994). A showing of actual malice, however, is not required under the statute. Catania v. Hanover Ins. Co., 389 Pa. Super. 144, 151-51, 566 A.2d 885, 888-89 (1989).

Although there is no shortage of blood in the waters of this litigation, we do not find that the counterclaims of which Dardovitch complains were unambiguously rooted in malicious ulterior motive. This is particularly true in light of the Pennsylvania Superior Court's admonition that "[a]n action for the wrongful use of a counterclaim demands that courts examine such claims closely, lest a defendant be punished for nothing more than defending himself or herself against a claim made by another." Mi-Lor, Inc. v. DiPentino, 439 Pa. Super. 636, 640 654 A.2d 1156, 1158 (1995). Furthermore, although a showing of actual malice is not required under § 8354, we have already granted plaintiff full attorney's fees and costs for that portion of the litigation. Although we are empowered to award punitive damages for this claim, see 42 Pa. Cons. Stat. § 8353(6), we do not find that defendants' conduct quite meets this more stringent standard.[33]

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[33] The Pennsylvania Supreme Court has adopted the Restatement's view regarding the imposition of punitive damages. See Rizzo v. Haines, 520 Pa. 484, 507, 555 A.2d 58, 69 (1989); Feld v. Merriam, 506 Pa. 383, 485 A.2d 742 (1984); Chambers v. Montgomery, 411 Pa. 339, 192 A.2d 355 (1963). Section 908(2) of the Restatement (Second) of Torts provides that: "Punitive damages may be awarded for conduct that is outrageous, because of the defendant's evil motive or his reckless indifference to the rights of others." Id.

Our Court of Appeals noted that Pennsylvania has adopted a very strict interpretation of "reckless indifference to (continued...)

E. Prospective Relief

We find that the trustees' hearing testimony regarding prospective execution of the Trust -- when adjusted to disburse funds which we have herein restored -- properly reflects the Trust's terms and intent.[34] Thus, we find it unnecessary to reach sua sponte the question of further relief. See, e.g., 42 Pa. Cons. Stat. § 7121 (court removal of trustee).

We caution defendants, however, that courts will not tolerate the trustees' wilful evasion of their fiduciary obligations by hugger-mugger self-dealing, arbitrary and capricious enactment of the Trust's terms, see, e.g., October 10, 1997 Order at ¶q, and preferential treatment of beneficiaries. See Estate of Pew, 440 Pa. Super. 195, 655 A.2d 521 (1994). The

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[33](...continued)
the rights of others." Burke v. Maasen, 904 F.2d 178, 181 (3d Cir. 1990). In Pennsylvania, punitive damages must be based on conduct which is malicious, wanton, reckless, willful, or oppressive. Rizzo, 555 A.2d at 69; Feld, 485 A.2d at 747-48; Chambers, 192 A.2d at 358. Negligence, even gross negligence, will not sustain an award of punitive damages. Smith v. Celotex Corp., 387 Pa. Super. 340, 564 A.2d 209, 211 (1989).

[34] In so doing, we specifically reject any averment by defendants that the Trust is insolvent or unable to pursue the claims in its res. It is well-settled that one of Haltzman's duties as trustee is to pursue claims of the Trust. See Restatement (Second) of Trusts § 177 (2d ed. 1959). In that capacity, the GESEA Trust instrument explicitly forbids him from receiving compensation. See Trust Account at Ex. A at ¶9. That duty is all the more conspicuous here, where the Trust's sole assets are uncollected notes. Furthermore, the payment of "all necessary expenses incident to the administration of the Trust or the collection of the Trust Property assets" is accorded priority over all other disbursements. See Trust Account at Ex. A at ¶2(b). Thus, the trustees cannot in their discretion make disbursements of Trust funds without first ensuring that the Trust's collection activities remained adequately funded.

office of a trustee demands far more than that, and it is our role to see that those requirements are fulfilled. In this respect, no one has improved on the words of then-Chief Judge Cardozo seventy years ago in Meinhard v. Salmon, 249 N.Y. 458, 463, 164 N.E. 545, 546 (Ct. App. 1928):

> A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the disintegrating erosion of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.

Id. (internal quotations omitted). To that end, and having clarified the fiduciary standard to which the trustees must adhere, we have also in our accompanying Order and Decree taken steps to minimize any further temptation on the trustees' part impermissibly to self-deal.