

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

GRANARY ASSOCIATES, : CIVIL ACTION
INC., et al., :
 :
v. :
 :
EVANSTON INSURANCE CO. : No. 99-5154

MEMORANDUM AND ORDER

J. M. KELLY, J.

DECEMBER 4, 2000

Presently before the Court are cross-motions for Summary Judgment filed by the Plaintiffs,¹ Granary Associates, Inc. ("GAI") and Granary Associates Architects, P.C. ("GAA"), and the Defendant, Evanston Insurance Company ("EIC"). This suit arises out of the alleged breach of an insurance policy by EIC, the insurer. EIC denied coverage to Plaintiffs' claim because it felt that the Plaintiffs, the insureds, had breached a consent clause in the insurance policy. EIC also denied coverage because it felt that the insureds' close relation to the injured party had triggered an exclusion in the insurance policy. Both parties now seek summary judgment as a matter of law pursuant to Federal Rule of Civil Procedure 56. For the following reasons, the motions are granted in part and denied in part.

I. BACKGROUND

Although the parties are in general agreement regarding the

¹ Joining in GAI and GAA's motion are Third-Party Defendants WJD, L.L.C. and Aegis Realty Development, Inc.

underlying facts of this case, the Court will note any relevant disparities where appropriate. The facts of this case are as follows.

A. The Construction Project and Business Entities Involved

West Jersey Health Systems ("WJHS"),² a New Jersey company, wanted to build a new medical facility in Sicklerville, New Jersey. WJHS hoped the facility would serve as a model for similar facilities built throughout the region. WJHS hired GAI to construct the new facility,

WJHS wanted to finance the construction project as an "off balance sheet" transaction, which would prevent any debt from appearing on its books. In order to allow its client to conduct this type of transaction, GAI created two new business entities, WJD, L.L.C. ("WJD") and Aegis Realty Development, Inc. ("Aegis"). After the creation of these new business entities, Aegis acted as the developer for the project. WJD acted, in essence, as the owner of the project. For example, WJD chose GAA as the architect for the project, retained GAI to manage the project and provide engineering and interior design services, and entered into a Development Agreement with Aegis under which Aegis would

² WJHS is the sole member of Southern New Jersey Medical Services. For simplicity's sake, the Court will refer solely to WJHS.

fulfill WJD's obligations.³ WJD also leased the Sicklerville property from its owner, Trinity Holdings Group, L.L.C., for twenty-one years, and entered into a twenty year operating lease with WJHS that would commence after the year-long construction of the facility.⁴

B. The Mistaken Masonry

The operating lease between WJHS and WJD provided that WJHS would select the color of the facility's exterior. WJHS's Director of Design Construction Management, Louis Moffa, decided that the new building should be constructed in white masonry with a pink trim. The Project Architect, Vince Girondi,⁵ transposed the colors that WJHS had ordered; he thought WJHS had ordered a pink building with white trim. Girondi relayed this mistake to the Project Director for GAI, E.J. Hedger. After Hedger relayed the mistaken order to the general contractor, construction of the new facility began.

Construction continued using the pink masonry for some time.

³ In other words, Aegis gave the lender, Summit Bank, N.A., a performance guarantee.

⁴ WJHS then entered into a sublease with Sicklerville Internal Medicine Associates, who would occupy the building as a tenant after its construction.

⁵ It is unclear for whom Girondi worked; EIC claims that he worked for GAI, while GAI and GAA state that he worked for GAA. As both GAI and GAA were covered by the insurance policy, however, this distinction is irrelevant.

One reason the parties did not immediately recognize the mistake was that GAI did not construct a model, or "mock-up," of the new facility. The contract required GAI to construct the mock-up, which, if viewed by WJHS, might have revealed the mistake before construction began.

On or about September 25, 1997, Robert Lazzaro of WJHS did notice the mistake. Although he immediately contacted GAI, masons had already erected 20-25% of the walls. Moreover, the masonry had been custom manufactured and could not be returned.

WJHS, which did not want to own a pink building, objected to the mistake. The parties began negotiating on October 4, 1997. During these negotiations, WJD, acting as the owner of the project, suggested correcting the mistake by painting the walls white or bleaching the walls to remove the pink color. WJHS rejected these ideas and insisted that the builders raze the pink walls entirely and erect white masonry walls in their place.

Finally, on October 9, 1997, the parties compromised; WJD would pay for the construction of new white walls that would act as a veneer, completely concealing the pink walls. Pursuant to this plan, the "facade solution," construction would continue with the pink masonry in order to "close" the building and allow interior work to begin. When the white masonry arrived at the site, the builders would erect the veneer around the completed pink walls. This solution would add an additional \$300,000 to

the cost of construction, which WJD would bear.⁶ Before agreeing to the facade solution, neither GAI nor GAA had informed EIC, their professional liability insurer, about any possible liability for their mistake.

C. The Insurance Claim and Its Denial

Because WJD bore the additional costs of the facade solution, it demanded that GAI and GAA indemnify it. GAI and GAA then filed an insurance claim with its insurer, EIC. GAI and GAA were covered by an Architect's and Engineer's Professional Liability Insurance Policy ("the Insurance Policy") issued by EIC. The Insurance Policy listed GAI as a "named insured" and GAA as an "additional insured." The Insurance Policy had a limit of liability of \$1 Million per claim and in the aggregate, and had a \$35,000.00 deductible.

EIC received notice of GAI and GAA's mistake on November 5, 1997, almost one month after GAA, GAI, WJD, Aegis and WJHS had agreed to the facade solution.⁷ After receiving notice of the

⁶ The parties agree that tearing down the pink walls and replacing them entirely would have been a more expensive solution, while painting or bleaching the walls would have been less expensive solutions.

⁷ GAI notified its insurance agent of the claim made by WJD. On October 31, 1997, GAI's insurance agent submitted the claim to AllRisks, from whom GAI's insurance agent had purchased the Insurance Policy. On November 5, 1997, AllRisks forwarded the claim to EIC.

construction error and the facade solution, EIC sent a letter to GAI on November 10, 1997. The letter states that "your firm has already made a commitment to perform corrective work costing \$300,000.00. You should be aware that any commitment made by the Insured without prior authority from the Insurer is at the Insured's expense and would not be covered by the policy."

EIC then began investigating the proposed solution. EIC received a report from one of its investigators on March 13, 1998, nearly four months after receiving notice of the claim against GAI and GAA. The report concluded that building this facade was unreasonable because painting the building would have initially cost only \$8,000.00.⁸ By letter dated March 18, 1998, EIC denied coverage for the claim.

D. The Insurance Policy and its Alleged Breach

The terms of the Insurance Policy obligate EIC to "pay on behalf of the Insured all sums in excess of the deductible . . . which the Insured shall become legally obligated to pay as Damages by reason of any act, error or omission committed or alleged to have been committed by the Insured" The parties agree that the mistake of GAI and GAA comes within this broad contractual language. EIC nonetheless denied coverage for

⁸ This estimate did not include the cost of repainting the walls after the initial coat of paint wore off.

the claim, citing two portions of the Insurance Policy in support of its decision.

First, EIC found fault with GAI and GAA's settlement of the claim without obtaining its prior approval. Paragraph V(d) of the Insurance Policy, the "consent clause," states:

The Insured shall not with respect to any Claim covered under this Policy, except at the Insured's personal cost, make any payment, admit liability, settle claims, assume any obligation, waive any rights or incur Claims Expenses without prior written Company approval. Any costs and expenses incurred by the Insured prior to the Insured giving written notice of the Claim to the Company shall be borne by the Insured and will not constitute satisfaction of its deductible in whole or in part.

Moreover, the Insurance Policy's definition of "Damages," the only amounts EIC is obligated to cover, includes only settlements of a claim "entered into with the prior consent of [EIC]."

Second, EIC denied coverage because it felt that the injured party, WJD, was too closely related to the insureds, GAI and GAA. Exclusion III of the Insurance Policy, a "business enterprise exclusion," is triggered when an insured business entity is closely related to an injured party bringing a claim against the insured. Exclusion III states:

Notwithstanding anything contained in this Policy to the contrary, the coverage herein shall not apply to a Claim made against the Insured:
(1) by a person, firm or organization . . . that wholly or partly owns, operates, manages or otherwise controls an insured, whether directly or indirectly, or that is wholly or party owned, operated, managed or otherwise controlled by an

Insured, whether directly or indirectly; or
(b) by a firm or organization . . . of which any
principal, partner, director, officer or
stockholder of a Named Insured directly or
indirectly maintains ownership, or who directly or
indirectly operates, manages or otherwise controls
such firm or organization

In this case, Michael Eastwood owned both GAI and WJD, and
Salvatore Scelsi acted as the treasurer of GAA and WJD.

GAI and GAA believe that EIC was nonetheless obligated to
cover the claim filed against them. On October 19, 1999, GAI and
GAA filed suit in this Court for breach of the Insurance Policy,
seeking damages in the amount of \$237,512.89. This amount
represents the costs incurred in implementing the facade
solution, specifically: (1) construction costs in the amount of
\$219,347.00; (2) structural engineer's fees in the amount of
\$10,500.00; (3) architecture fees owed to GAI in the amount of
\$30,750.00; (4) project management fees owed to GAI in the amount
of \$21,000.00; (5) construction interest in the amount of \$21,
267.00; and (6) pre-judgment interest totaling \$44,684.89. These
damages, less the \$35,000.00 deductible and a \$75,000.00
settlement with Biddle & Co., GAI's insurance agent,⁹ total the
\$237,512.89 sought by GAI and GAA.

EIC, the Defendant, brought WJD and Aegis into this suit as
Third-Party Defendants on December 2, 1999. EIC alleges that WJD

⁹ GAI, GAA, WJD and Aegis filed a related suit in state
court, alleging negligence on the part of their insurance agent,
Biddle. Biddle settled the case.

and Aegis were partially responsible for the mistaken masonry order that precipitated this suit. The parties have filed cross-motions for Summary Judgment, which the Court will now consider.

II. STANDARD OF REVIEW

Pursuant to Federal Rule of Civil Procedure 56, a court must grant summary judgment "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 movant bears the initial burden of showing the basis for its motion. Celotex Corp. v. Catrett, 477 U.S. 317, 323 (1986). If the movant fails to meet this burden under Rule 56(c), its motion must be denied.

If the movant adequately supports its motion, however, the burden shifts to the nonmoving party to defend the motion. To satisfy this burden, the nonmovant must go beyond the mere pleadings by presenting evidence through affidavits, depositions or admissions on file to show that a genuine issue of fact for trial does exist. Id. at 324; Fed. R. Civ. P. 56(e). An issue is considered genuine when, in light of the nonmovant's burden of proof at trial, the nonmovant produces evidence such that a reasonable jury could return a verdict against the moving party. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986). When

deciding whether a genuine issue of fact exists, the court is to believe the evidence of the nonmovant, and must draw all reasonable inferences in the light most favorable to the nonmovant. Anderson, 477 U.S. at 255. Moreover, a court must not consider the credibility or weight of the evidence presented, even if the quantity of the moving party's evidence far outweighs that of the nonmovant. Big Apple BMW, Inc. v. BMW of N. Am., Inc., 974 F.2d 1358, 1363 (3d Cir. 1992). Nonetheless, a party opposing summary judgment must do more than rest upon mere allegations, general denials, or vague statements. Trap Rock Indus., Inc. v. Local 825, 982 F.2d 884, 890 (3d Cir. 1992).

If the nonmoving party meets this burden, the motion must be denied. If the nonmoving party fails to satisfy its burden, however, the court must enter summary judgment against it on any issue on which that party will bear the burden of proof at trial. Celotex, 477 U.S. at 322-23.

That two parties file cross-motions for summary judgment under Rule 56(c) does not necessarily make summary judgment appropriate. Reading Tube Corp. v. Employers Ins. of Wausau, 944 F. Supp. 398, 401 (E.D. Pa. 1996). In such a situation, "each side essentially contends that there are no issues of material fact from the point of view of that party." Bencivenga v. Western Pa. Teamsters, 763 F.2d 574, 576 n.2 (3d Cir. 1985). Because each side therefore bears the burden of establishing that

no genuine issue of material fact exists, "the court must consider the motions separately." Id. (citing Rains v. Cascade Indus., Inc., 402 F.2d 241, 245 (3d Cir. 1968)).

III. DISCUSSION

A. Applicable Law

Both parties agree, however, that the law of the Commonwealth of Pennsylvania controls this case. EIC does contend, however, that the law of the State of New Jersey applies to the determination of damages. This disagreement is irrelevant, however, as the Court can resolve the damages issue without deciding whether Pennsylvania or New Jersey's laws apply. Accordingly, the Court will not rule on this issue. See Williams v. Stone, 109 F.3d 890, 893 (3d Cir. 1997); Lucker Mfg. v. Home Ins. Co., 23 F.3d 808, 813 (3d Cir. 1994).

B. Breach of the Consent Clause

Both sides seek summary judgment based on the alleged breach of the Insurance Policy's consent clause. EIC contends that the breach of the consent clause relieves it of any obligation to cover the claim. GAI and GAA contend that EIC must prove prejudice as well as breach and, because EIC cannot, summary judgment should be granted in their favor.

It is undeniable that the Insurance Policy required the

insureds to notify EIC of any claims against them and to obtain EIC's consent before settling those claims. It is also undeniable that the insureds did not comply with the literal language of the Insurance Policy.

The law of Pennsylvania, however, requires more than a literal breach of this type of contractual language. Because most insureds do not have an opportunity to draft or negotiate the terms of insurance policies, the Supreme Court of the Commonwealth of Pennsylvania has established a rule that requires the insurer, not the insured, to show that a lack of notice justifies non-coverage. Brakeman v. Potomac Ins. Co., 371 A.2d 193 (Pa. 1977); see also Trustees of the Univ. of Pa. v. Lexington Ins. Co., 815 F.2d 890, 897 (3d Cir. 1987) (extending Brakeman rule to insurance policies between sophisticated parties). Specifically, the Brakeman decision established an affirmative defense to coverage that is satisfied if the insurer can show that the insured has breached the notice clause of the policy and that the insured's breach has prejudiced the insurer. The Pennsylvania Supreme Court explained that, because notice provisions are intended to prevent prejudice to an insurer, "[w]here the insurance company's interests have not been harmed by a late notice . . . the reason behind the notice condition in the policy is lacking, and it follows neither logic nor fairness to relieve the insurance company of its obligations under the

policy in such a situation." Brakeman, 371 A.2d at 197.

Strictly speaking, though, this case does not merely involve deficient notice. While the Insurance Policy in the case at bar does contain a notice provision, EIC seeks relief because of the insureds' breach of a consent clause. The Brakeman decision and its progeny deal exclusively with instances of deficient notice, not absence of consent to the settlement of a claim.

This is, however, a distinction without a difference; the Brakeman rule extends to consent clauses. See, e.g., Harrisburg Area Cmty. Coll. v. Pacific Employees Ins. Co., 682 F. Supp. 805, 809 (M.D. Pa. 1988). Because notice and consent provisions both seek to prevent prejudice to the insurer, it would be illogical to require a showing of prejudice for one but not the other. See id.; see also Cooper v. Government Employees Ins. Co., 237 A.2d 870, 873-74 (N.J. 1968). Both notice and consent provisions are subject to the requirement that the insurer demonstrate some form of prejudice to its interests before avoiding liability.

Having found that EIC must make some showing of prejudice, the question then becomes whether the Court can render summary judgment on this issue. The precise contours of the requirements for establishing prejudice in the context of the breach of a consent clauses are less than certain. Indeed, "[w]hether and under what circumstances prejudice can be granted as a matter of law is a contested issue in Pennsylvania." Hyde Athletic Indus.,

Inc. v. Continental Cas. Co., 969 F. Supp. 289, 300 (E.D. Pa. 1997). There appears to be no dispute, however, that a court may find prejudice to an insurer as a matter of law. See, e.g., Champion v. Chandler, No. 96-7263, 1999 WL 820460, at *2 (E.D. Pa. Sep. 29, 1999); Life and Health Ins. Co. of America v. Federal Ins. Co., No. 92-6736, 1993 WL 326404, at *2 (E.D. Pa. Aug. 25, 1993) (stating that prejudice can be found as matter of law but finding otherwise on facts presented); Clemente v. Home Ins. Co., 791 F. Supp. 118, 120 (E.D. Pa. 1992); Harrisburg Area Cmty. Coll., 682 F. Supp. at 809.

GAI and GAA apparently contend that Continental Casualty Co. v. Castlewood Corp., No. 88-4152, 1990 WL 131073, at *3-4 (E.D. Pa. Sep. 6, 1990) calls into question whether finding prejudice as a matter of law is appropriate under any circumstance. The Court rejects this broad interpretation of Continental Casualty. In Continental Casualty, the insurer claimed it had suffered prejudice as a matter of law because of the insured's deficient notice. The insurer, who had no right to control the defense of the claim, argued it had been prejudiced by the denial of its contractual right to "associate" with the insured's defense counsel at trial. The Continental Casualty decision quoted a Third Circuit decision that stated that the "mere interference with [the insurer's] right to 'associate' in the defense of the claim is too amorphous and cannot itself constitute prejudice

unless [the insurer] can demonstrate that earlier notice would probably have led to a more advantageous result." Id. at *2 (citing Trustees, 815 F.2d at 899). The insurer in Continental Casualty contended that Metal Bank of America v. Insurance Co. of North America, 520 A.2d 493 (Pa. Super. Ct. 1987) advocated a different result. Deflecting the insurer's argument, the Continental Casualty decision correctly stated that Metal Bank was not controlling in federal court because it was a lower state court opinion.¹⁰ Any language in Continental Casualty that calls into question the applicability of Metal Bank is found in this limited discussion of whether an insurer with no rights to control the litigation or settlement of claims can be prejudiced as a matter of law by late notice.

The Continental Casualty decision does not advocate a broader holding that prejudice as a matter of law can never be established. Indeed, the remainder of the decision implicitly acknowledges that a court may, if appropriate under the circumstances, find prejudice to an insurer as a matter of law. Continental Casualty, 1990 WL 131073, at *2 ("[The insurer's]

¹⁰ See Continental Casualty, 1990 WL 131073, at *3 ("Federal courts are not bound by intermediate appellate state courts in determining state law issues in diversity cases, nor do federal courts attempt to predict what intermediate appellate courts will hold. Decisions of the Pennsylvania Superior Court are relevant only because they are 'indicia of how the state's highest court might decide' the issue. They are given 'significant weight . . . in the absence of any indication that the highest state court would rule otherwise.'" (citations omitted).

assertions are insufficient to establish prejudice as a matter of law."). By distinguishing Metal Bank from the case then at bar, the Continental Casualty decision recognized that, as in Metal Bank, prejudice can be found as a matter of law. Id. at *4, n.7. For example, the case implicitly suggests that late notice can result in prejudice as a matter of law if the insurer does have the contractual right to conduct the defense of the claim or give its approval before settlement. See id. Accordingly, this Court may, if appropriate under the facts presented, find prejudice or the lack thereof as a matter of law.

Having found that the Court may enter summary judgment on the issue of prejudice, the Court must determine whether it should. The United States District Court for the Middle District of Pennsylvania has discussed when deficient notice justifies a finding of prejudice as a matter of law. It wrote:

In protracted litigation where negotiating skill would be of crucial importance, especially where damages are unliquidated, the insurer has a valid claim of prejudice when notice comes after the insured has informally settled the matter. The insurance company would justifiably resist paying a settlement in those circumstances when it was deprived of counsel of its choosing to oversee the matter and to negotiate, if possible, an acceptable resolution of the controversy. On the other hand, [when liability] is clear and the calculation of damages [is] merely an arithmetical exercise, [the insurer does not have a valid claim of prejudice].

Harrisburg Area Cmty. Coll., 682 F. Supp. at 809. Moreover, insurers seeking to avoid their obligations to cover a claim

because of deficient notice must show not only the loss of a substantial defense opportunity but also a likelihood of success in defending liability or damages if that opportunity had been available. See Trustees, 815 F.2d at 898.

In the instant case, the Court finds that genuine issues of fact exist, which precludes summary judgment on the issue of prejudice for either party. On EIC's motion for summary judgment, EIC has satisfied its initial burden that it is entitled to summary judgment as a matter of law. In this case, the technical breach of the consent clause is clear. Moreover, EIC has put forward facts tending to show that the facade solution prejudiced EIC because it was unreasonably expensive in light of alternate solutions. As the non-moving parties, GAI and GAA have also met their burden of defending the motion by showing that genuine issues of fact do exist for trial. For example, GAI and GAA have presented evidence that WJHS would not have accepted a painted or bleached building, and would have sued to enforce their rights under the contract, resulting in protracted litigation that could have cost WJD more than the facade solution itself. This evidence, if believed by the trier of fact, would show that the facade solution, although more expensive than painting or bleaching the masonry, was the least expensive solution available. In that scenario, adopting the facade solution could not have prejudiced EIC's interests.

On GAI and GAA's motion for summary judgment, the insureds argue that no prejudice can be found because there is no doubt as to GAI and GAA's liability for the masonry mistake. Assuming arguendo that GAI and GAA are solely liable, and accordingly that EIC could not have shifted some of the liability to WJD or Aegis, EIC can still make out prejudice. Even if GAI and GAA were solely liable, the extent of their liability remained unclear at the time they negotiated the facade solution. Because effective negotiation of the claim against them could have reduced the expenses incurred in correcting their mistake, EIC can make a colorable claim of prejudice by showing that the facade solution was more expensive than a solution EIC could have reached had it been allowed to take part in the settlement negotiations. See Harrisburg Area Cmty. Coll., 682 F. Supp. at 809. As EIC has presented evidence showing that the facade solution was unreasonably costly under the circumstances, it has satisfied its burden of defending the Motion for Summary Judgment.

Genuine issues of fact exist concerning the expense, viability and reasonableness of the facade solution and other proposed solutions rejected by the parties. A reasonable jury could find for either party on the issue of whether EIC was prejudiced by its inability to consent to the settlement of the claim against the insured. Accordingly, summary judgment is not appropriate on this issue for either party.

C. The Business Enterprise Exclusion

Both sides also seek summary judgment based on the Insurance Policy's business enterprise exclusion, Exclusion III. Business enterprise exclusions like the one at issue in this case are intended "to prevent collusive suits whereby malpractice coverage could be used to shift [an insured's] business loss onto his or her [insurer]." Niagara Fire Ins. Co. v. Pepicelli, Pepicelli, Watts & Youngs, P.C., 821 F.2d 216, 221 (3d Cir. 1987). This can happen when uninsured business partners collusively convert their own business losses into malpractice claims that are then covered by their insured partner's insurance policies. While EIC argues that the relationship between GAI, GAA and WJD triggered the exclusion, the insureds contend that EIC cannot prove that collusion actually occurred in this case.

A business enterprise exclusion will provide an insurer with relief if, after examining the nature of the insurance claim rather than the mere factual background, it seems that "the actions or interests of the insured . . . in his business enterprise were at issue in the underlying litigation [where he committed malpractice] and whether the resolution of the underlying claims would affect those interests." Coregis Ins. Co. v. LaRocca, 80 F. Supp. 2d 452, 456 (E.D. Pa. 1999). This rule derives from the Pepicelli decision, in which the Third

Circuit considered legal malpractice liability exclusions similar to Exclusion III in this case. See Pepicelli, 821 F.2d 220-21. Pepicelli, a lawyer, represented Perma Tread, a tire manufacturer. Pepicelli also owned a business that had entered into an agreement to purchase a manufacturing plant from Perma Tread, his client. After the contract was signed but before closing, the plant burned down. In Perma Tread's efforts to secure insurance coverage from its fire insurer for damages to the plant, Pepicelli represented Perma Tread. Perma Tread was unable to obtain coverage. Perma Tread then sued Pepicelli and his law firm for malpractice. Pepicelli sought coverage under his own malpractice insurance policy. Pepicelli's insurer denied coverage, citing an exclusion similar to the one at bar. The Third Circuit stated that: "the crucial distinction here [is that the] exclusions speak of excluded claims, and thus the character of the specific legal claims, rather than the malpractice suit's general factual background, must be analyzed to determine the exclusion issue." Pepicelli, 821 F.2d at 220.

Importantly, neither Pepicelli nor its progeny require an explicit showing of actual collusion by an insurer. Rather, they merely require that courts scrutinize the language of the business enterprise exclusions in the context of the insurance claim. These cases do, however, place an emphasis on at least the possibility of collusive loss-shifting to an insured from an

uninsured. See, e.g., LaRocca, 80 F. Supp. 2d at 458 ("In the present case, despite [the insured's] protestations to the contrary, it is possible that the collusive purpose discussed in Pepicelli could come into play, and that by securing the professional liability coverage under the [insurance policy, the insured] could offset the liabilities he might incur").

In the instant case, therefore, summary judgment may be granted if the Court finds that the character of the insurance claim implicates the language of Exclusion III and a possibility of collusion by the insured. Under Pennsylvania law, the interpretation of the terms of an insurance contract like this one is a question of law to be decided by a court. Pacific Indem. Co. v. Linn, 766 F.2d 754, 760 (3d Cir. 1985). Where there is no genuine issue of material fact, there is no need to submit the issue to a trier of fact. Id.

Exclusion III(b) of the Insurance Policy states that:

[T]he coverage herein shall not apply to a Claim made against the Insured: . . . (b) by a firm or organization . . . of which any principal, partner, director, officer or stockholder of a Named Insured directly or indirectly maintains ownership, or who directly or indirectly operates, manages or otherwise controls such firm or organization.

WJD brought the claim against the insured, either GAI or GAA.

Michael Eastwood owns both WJD and GAI, and Salvatore Scelsi acts as the treasurer for both WJD and GAA. Therefore, irrespective of whether WJD brought its claim against GAI or GAA, the language of

Exclusion III(b) is still technically implicated.¹¹ In light of Pepicelli, however, the Court finds that the business enterprise exclusion does not apply to this claim. WJD, the claimant, was created solely for the benefit of WJHS so that it could finance the construction project as an off-balance sheet transaction. As such, WJD was merely a "player in the factual background" of the insurance claim that was precipitated by GAI and GAA's mistake. See Pepicelli, 821 F.2d at 221. The relation between WJD's business activities and the insurance claim is too tenuous to allow the insurer to avoid its liability under the Insurance Policy; WJD was not created as a means of collusively shifting losses from an uninsured to an insured, and neither GAI nor GAA should be penalized merely because they intended to assist their client.

Moreover, WJD had no added incentive to agree to an unreasonably costly solution in order to avoid personal liability because WJD believed it could have sought indemnification from GAI and GAA. WJD concedes that it and Aegis may have suffered a loss if the construction project was not completed on time. But even if WJD had no relation to GAI or GAA, it would still, as the owner of the project, seek relief from the architects and project managers for their mistake. No threat of collusion exists on

¹¹ The parties disagree about whom the claim was brought against, GAA or GAI. This distinction is irrelevant, however, as both parties implicate Exclusion III.

these facts. Accordingly, the Court will enter summary judgment on this issue against EIC and in favor of GAI and GAA.

D. Damages

EIC seeks summary judgment based on the damages claimed by the insureds, GAI and GAA. First, EIC contends that the facade solution was economically wasteful. Second, EIC argues that partial summary judgment limiting the insureds' recovery is appropriate because the Insurance Policy precludes coverage for the insureds' services rendered to other parties.

EIC's argument regarding the economic wastefulness of the facade solution lacks merit. Although the alleged wastefulness of the solution is relevant to whether EIC has been prejudiced by the breach of the consent clause, that wastefulness does not in and of itself justify summary judgment against GAI and GAA. That the insureds purportedly seek unreasonably high damages does not resolve whether EIC must cover the insurance claim; it would only serve to mitigate the extent of coverage required. Assuming without deciding that, as EIC contends, the Second Restatement of Contracts section 348(2) would control this case, that provision would only serve to limit the amounts recoverable to "the diminution in the market price of the property caused by the breach." See Restatement (Second) of Contracts § 348(2)(a). In other words, GAI and GAA could still recover the difference between the building's market price without the defect and its

market price with the defect. Assuming that the Court found the facade solution to be economically wasteful, that finding would not dispose of the matter before the Court.

Moreover, the Court can only determine the reasonableness of the facade solution upon considering all of the facts of this case. The cost of painting or bleaching the pink walls, although clearly less than the cost of constructing the white facade, is only one consideration. For example, had WJD, GAI and GAA insisted on painting the walls white rather than constructing the white facade, they might have incurred other damages; WJHS might have refused to accept that defective performance and instituted a breach of contract action against them. As discussed above, genuine issues of material fact exist regarding the reasonableness of the facade solution in light of its alternatives. Accordingly, the Court will not grant summary judgment on this issue.

Second, EIC seeks partial summary judgment excluding from the damages recoverable by the insureds any sums owed to them for their own services rendered. Specifically, EIC seeks to limit the damages recoverable by \$51,750.00. The Insurance Policy clearly excludes from the "Damages" recoverable "the restitution, return, withdrawal or reduction of fees, profits, charges for services rendered, consideration and/or expenses paid to the Insured for services or goods." The insured included in their

calculation of damages \$51,750.00 for their own services rendered to the injured party.¹² EIC has therefore met its burden under Rule 56.

GAI and GAA failed to address this issue in either their Response to EIC's motion or in their own Motion for Summary Judgment. Accordingly, they have not satisfied their burden of opposing EIC's motion. Rule 56 nevertheless requires the Court to conduct its own examination of whether granting summary judgment on this matter is appropriate. Fed. R. Civ. P. 56(e) ("If the [nonmovant] does not so respond, summary judgment, if appropriate, shall be entered against the [nonmovant]."). The Court finds that entering summary judgment on this issue is appropriate. The contractual language excluding these amounts from damages recoverable is clear, and both sides agree to the relevant underlying facts. Therefore, the Court will enter summary judgment excluding these amounts from the damages recoverable by the insureds.

E. EIC's Third-Party Suit Against WJD and Aegis

Finally, GAI and GAA contend that EIC's Third-Party Complaint against WJD and Aegis cannot stand. EIC brought WJD and Aegis into this matter because it felt they were partially responsible for the mistaken order of pink masonry. The gravamen

¹² The insureds seek coverage for architecture fees owed to GAI in the amount of \$30,750.00 and project management fees owed to GAI in the amount of \$21,000.00.

of EIC's Third-Party Complaint was that WJD or Aegis had directed GAI not to construct a mock-up that, if made, would have alerted the parties to the mistake before construction began. EIC therefore feels that WJD and Aegis are at least partially responsible for any damages to WJD.

GAI and GAA contend that no facts support EIC's Third-Party Complaint against WJD and Aegis. In support of their Motion for Summary Judgment, they point to depositions indicating that neither WJD nor Aegis had any employees or any direct supervision over the construction project. They also note that the deposition of Cheryl Williams indicates that GAI and GAA, without any input from either WJD or Aegis, made the decision to forego the mock-up. Accordingly, the insureds have met their initial burden under Rule 56 of showing that they are entitled to summary judgment on this issue.

In opposition to this motion, EIC points to no facts that would establish any cognizable liability on the part of either WJD or Aegis. Instead, EIC attacks the insureds' legal argument that a subrogation claim cannot be made against an injured party. The Court need not address the merits of that legal argument, however, as EIC has failed to point to any evidence outside of the pleadings that would allow a jury, irrespective of the type of claim brought, to find liability on the part of either WJD or Aegis. EIC has therefore failed to meet its burden under Rule

56. Furthermore, the Court is satisfied that summary judgment is appropriate on this issue; absent some evidence tending to show that WJD or Aegis had acted negligently, or indeed had acted at all, no reasonable jury could find in EIC's favor on its Third-Party Complaint. Accordingly, the Court will enter summary judgment against EIC on its Third-Party Complaint.

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

GRANARY ASSOCIATES,	:	CIVIL ACTION
INC., et al.,	:	
	:	
v.	:	
	:	
EVANSTON INSURANCE CO.	:	No. 99-5154

O R D E R

AND NOW, this day of December, 2000, in consideration of the Motion for Summary Judgment filed by the Plaintiffs, Granary Associates, Inc. ("GAI") and Granary Associates Architects, P.C. ("GAA"), and Third-Party Defendants WJD, L.L.C. ("WJD") and Aegis Realty Development, Inc. ("Aegis") (Doc. No. 16), and the Motion for Summary Judgment filed by the Defendant, Evanston Insurance Company ("EIC") (Doc. No. 17), and the Responses thereto filed by the parties, it is **ORDERED** that:

1. The cross-motions for Summary Judgment are **DENIED** in part as to the consent clause of the Insurance Policy, paragraph V(d).
2. GAI and GAA's Motion for Summary Judgment is **GRANTED** in part as to the issue of the business enterprise exclusion of the Insurance Policy, Exclusion III. Judgment is **ENTERED** in favor of GAI and GAA and against EIC on the issue of the business enterprise exclusion, Exclusion III.
3. EIC's Motion for Summary Judgment is **GRANTED** in part as to the issue of reducing the Plaintiffs' damages recoverable by \$51,750.00. Judgment is **ENTERED** in favor of EIC and against GAI

and GAA reducing the Plaintiffs' damages recoverable by \$51,750.00.

4. GAI's and GAA's Motion for Summary Judgment, in which WJD and Aegis joined, is **GRANTED** in part as to EIC's Third-Party Complaint filed against WJD and Aegis. Judgment is **ENTERED** in favor of WJD and Aegis and against EIC on EIC's Third-Party Complaint.

BY THE COURT:

JAMES MCGIRR KELLY, J.