

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

PRO DENT INC., et al.

v.

ZURICH U.S., et al.

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CIVIL ACTION
NO. 99-5479

O'Neill, J.

April , 2001

MEMORANDUM

I.

This case involves an insurance coverage dispute between plaintiffs Pro-Dent Inc. and George E. Frattali & Associates (“Pro-Dent”) and defendants Northern Insurance Company of New York and Zurich U.S. (“Northern”). Presently before me are the parties’ cross-motions for summary judgment. For the reasons stated below, summary judgment will entered in favor of defendants and against plaintiffs.

II.

Pro-Dent operates a dental facility in Bucks County. In 1995, it retained a contractor known as RACS Associates, Inc. to install plumbing lines during the renovation of its dental offices. The contract required RACS to supply plumbing installation services based in part on design drawings prepared by Benco Plumbing. Those designs specifically required the use of PVC plastic pipes, rather than copper pipes, in the portion of the facility where x-rays were taken because the x-ray solution would corrode metal.

Three to four months after the facility opened, leaks began to occur in the Pro-Dent

facilities because RACS had used copper piping. Thereafter, Pro-Dent sued RACS in the Court of Common Pleas for Bucks County alleging breach of contract, breach of warranty, and negligence. On September 14, 1999, the jury found for Pro-Dent on the negligence claim, but not on the breach of contract and breach of warranty claims. RACS is now out of existence and the judgment in the Bucks County action cannot be executed against it.

Thereafter, plaintiffs brought this action against defendants, who had insured RACS under a commercial general liability policy at the relevant times. By Order dated January 31, 2000, I dismissed plaintiffs' bad faith and "direct action" claims but allowed plaintiffs to proceed on their third-party beneficiary breach of contract claim. The parties have now filed cross-motions for summary judgment on that claim.

III.

The policy between RACS and Northern obligated the insurer to indemnify the insured for an "property damage" caused by an "occurrence" unless otherwise excluded. The policy defines the term "occurrence" to mean "an accident including continuous or repeated exposure to substantially the same general harmful conditions."

Pennsylvania courts that have interpreted the term "occurrence" in similar policies have focused the inquiry on whether the underlying damage was caused by a tort or breach of contract. For example, in Redevelopment Auth. of Cambria County v. Int'l. Ins. Co., 685 A.2d 581 (Pa. Super. 1996), the plaintiff had entered into a contract with a municipality to supervise improvements to the municipal water system. Id. at 583. In an underlying action, the municipality complained that the Redevelopment Authority had "failed to 'properly perform' the

duties it had assumed under the contract, had been negligent, and had been unjustly enriched as a result of the retention of the monies paid to it to administer the project.” Id. at 584. The Redevelopment Authority requested that its insurer defend and indemnify it. The insurer brought a declaratory judgment action claiming that it had no duty to defend or indemnify because there was no “occurrence” within the scope of the policy.

The Superior Court agreed with the insurer. It found that the insurer had no duty to defend or indemnify the Redevelopment Authority because “the underlying suit arises out of a breach of contract which is not an accident or occurrence contemplated or covered by the provisions” of the policy. Id. at 589. “The purpose and intent of such an insurance policy is to protect the insured from liability for essentially accidental injury to the person or property of another rather than coverage for disputes between parties to a contractual undertaking.” Id.

The Court went on to enunciate the appropriate test for distinguishing between claims that sound in tort (and therefore are an “occurrence” within the scope of policy coverage) and claims that sound in contract (and therefore are outside the scope of policy coverage). To be construed as a tort action, “the wrong ascribed to the defendant must be the gist of the action with the contract being collateral.” Id. at 590. A contract action “may not be converted into a tort action simply by alleging that the conduct in question was done wantonly.” Id. Finally, “the important difference between contract and tort actions is that the latter lie from the breach of duties imposed as a matter of social policy while the former lie for the breach of duties imposed by mutual consensus.” Id. The Court found that this test was consistent with the approach taken by courts of other jurisdictions, including New Jersey, Wyoming, and Alaska. Id. at 590-91. Applying this test, the Court concluded that the underlying action sounded in contract and was

outside the scope of the policy coverage, even though the underlying action included a claim for negligence. Redevelopment Authority has since been followed by other Pennsylvania courts. See Snyder Heating Co., Inc. v. Pennsylvania Mfr. Ass'n Ins. Co., 715 A.2d 483, 485 (Pa. Super. 1998).

Applying the test enunciated in Redevelopment Authority, I conclude that Pro-Dent's underlying claims against RACS were essentially contractual and therefore were not "occurrences" within the scope of the policy. The contract between Pro-Dent and RACS was not collateral; the gist of Pro-Dent's claim was that RACS had violated the contract by using copper piping instead of the PVC piping that had been specified in the Benco design drawing. While RACS may have in some sense acted wantonly in ignoring those specifications, it cannot be said that RACS had a duty to use PVC piping as a matter of social policy.

Pro-Dent attempts to distinguish Redevelopment Authority and its progeny by pointing to the fact that unlike those cases the underlying action in this case has been tried to a jury, and the jury found RACS liable for negligence and not liable for breach of contract and breach of warranty. I find that argument unpersuasive for two reasons. First, insurance coverage "is a question of law for the Court to determine with reference solely to the complaint." Snyder, 715 A.2d at 487. Therefore, my conclusion that the gist of Pro-Dent's complaint was contractual should not be modified simply because the jury found as it did. Second, Redevelopment Authority dealt with both the duty to defend and the duty to indemnify. Since the duty to defend is broader than the duty to indemnify, Redevelopment Authority implicitly addressed this situation. In other words, when the Redevelopment Authority Court ruled that the insurer had no duty to defend against a complaint that asserted claims for breach of contract, negligence, and

unjust enrichment, it was implicitly ruling that the claims did not “potentially fall within the scope of coverage,” even though a finding of negligence but no breach of contract was possible and foreseeable. Cf. Snyder, 715 A.2d at 487 n.6.

For this reason, I find that if the Pennsylvania Supreme Court were confronted with the issue it would apply the reasoning of Redevelopment Authority to this case and hold that Northern had no duty to indemnify because there was no “occurrence.”

IV.

Pro-Dent also argues that Northern should be estopped from asserting that there is no coverage under the policy because the insurer did not make a timely reservation of its rights under the policy in a way that fairly informed RACS of its position. I disagree.

Initially, I note that it is unclear whether a third-party beneficiary can claim estoppel against an insurer. If so, there is no evidence on the record that either RACS or Pro-Dent was prejudiced by Northern’s alleged failure to make a timely reservation of its rights.

My rationale for rejecting the estoppel argument, however, is more straight-forward. I find that Northern made a timely reservation of its rights that fairly informed RACS of its position in its first reservation of rights letter. In a passage from that letter that Pro-Dent does not address in its brief, the insurer wrote:

For these reasons, we will be continuing our investigation into this incident without waiving our right to deny coverage in the future. We further reserve our right to assert additional policy defenses and/or amend this document if substantive information is received during the pendency of this matter. Further, should a potential breach of contract claim be alleged, this is not a covered claim as it does not meet the definition of “occurrence.”

See Reservation of Rights Letter dated April 17, 1997 at 4 (emphasis added).

This letter was written approximately two months after Northern was notified of the claim and approximately two and a half years prior to the Bucks County trial. Moreover, the final sentence clearly notified RACS of the same theory that Northern has asserted in this action. I therefore find that Northern is not estopped from asserting that defense.

An appropriate Order follows.

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ORDER

AND NOW, this day of April, 2001, after consideration of the parties' cross-motions for summary judgment, and for the reasons contained in the accompanying memorandum, it is ORDERED that judgment is entered in favor of defendants and against plaintiffs.

THOMAS N. O'NEILL, JR., J.