

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

MICHAEL SCHWARTZ, et al. : CIVIL ACTION
 :
v. :
 :
LIBERTY MUTUAL INSURANCE CO., :
et al. : NO. 01-2049

MEMORANDUM

Dalzell, J.

December 18, 2001

Petitioners, Michael Schwartz and Terri Schwartz, filed a Petition for Appointment of Uninsured Motorist Arbitrators and to Compel Arbitration ("Petition") in the Court of Common Pleas of Philadelphia County. They named as respondents Liberty Mutual Insurance Company ("Liberty Mutual") and AAA Mid Atlantic Company a/k/a Keystone Insurance Co. ("Keystone"), which allegedly insured them for an automobile accident in which Michael Schwartz was injured. Liberty Mutual removed the Petition to this court. Before us are the motions of Liberty Mutual to realign and of Michael and Terri Schwartz to remand.

I. Facts and Procedural History

Michael Schwartz was injured in an automobile accident on June 5, 1998 in which the responsible third party was uninsured.¹ Liberty Mutual and Keystone allegedly provided concurrent insurance, including uninsured motorist coverage, to

¹ Pet. for Appointment of Uninsured Motorist Arbitrators and to Compel Arbitration, at ¶¶ 4-5 [hereinafter Petition].

Michael Schwartz and his wife, Terri Schwartz, for the accident.² An uninsured motorist arbitration was held on August 15, 2000. Keystone voluntarily participated. Liberty Mutual failed to attend despite being requested to do so.³

The arbitrators entered an award for \$495,000.00 in favor of Michael and Terri Schwartz.⁴ Keystone tendered petitioners \$400,000.00, said to be the limit of its policy coverage.⁵ The petitioners demanded that Liberty Mutual pay the \$95,000.00 balance of the arbitration award.⁶ Liberty Mutual failed to do so and the petitioners filed the instant Petition to compel arbitration.⁷ The Petition named Liberty Mutual as a respondent as well as Keystone, the latter being alleged to be an indispensable party because Keystone is said to be entitled to contribution from Liberty Mutual for the August 15, 2000 arbitration award against it.⁸

Liberty Mutual removed the Petition to this court and concomitantly filed a motion to realign Keystone, a citizen of Pennsylvania, as a petitioner. Michael Schwartz and Terri

² Id. at ¶ 6.

³ Id. at ¶¶ 10-11.

⁴ Id. at ¶ 12, Ex. B.

⁵ Id. at ¶ 13.

⁶ Id. at ¶ 15.

⁷ Id. at ¶ 16.

⁸ Id. at ¶ 19.

Schwartz, who like Keystone are citizens of Pennsylvania, filed a motion to remand.⁹

II. Discussion

Neither federal question nor diversity jurisdiction exists on the face of the Petition. The Petition moves to compel arbitration pursuant to insurance contracts and state law¹⁰. Since respondent Keystone is a citizen of Pennsylvania, the same state as petitioners, diversity jurisdiction is destroyed. 28 U.S.C. § 1332 (2001); Strawbridge v. Curtiss, 7 U.S. 267 (3 Cranch) (1806); Cipriani v. Fed. Ins. Co. Div. of Chubb Group of Ins. Cos., No. 99-1014, 1999 U.S. Dist. LEXIS 11405, at *3-4 (E.D. Pa. 1999) ("Section 1332 has been interpreted to require 'complete diversity' and 'thus applies only to cases in which the citizenship of each plaintiff is diverse from the citizenship of each defendant.'" (citation omitted).

Liberty Mutual maintains that we should "look beyond the pleadings" and realign the parties according to the interests in the "real dispute."¹¹ If the Court does so, Liberty Mutual

⁹ Keystone did not file a motion to remand, but requested remand in response to Liberty Mutual's motion for realignment. See Answer of Keystone to Liberty Mutual's Mot. to Realign Keystone as a Pet'r, at 2.

¹⁰ 42 Pa. C.S.A. § 7304(a) (requiring courts to compel performance of agreements to arbitrate).

¹¹ Mem. of Law in Supp. of Mot. to Realign Keystone as a Pet'r, at 4 (quoting Employers Ins. of Wasau v. Crown Cork & Seal Co., 942 F.2d 862, 864 (3rd Cir. 1991) (quoting City of Indianapolis v. Chase Nat'l Bank, 314 U.S. 63, 69 (1941))).

argues, Keystone emerges as a petitioner in light of the fact that "the primary issue" behind the petition to compel arbitration, it asserts, is "whether Liberty Mutual Fire is required to contribute to the arbitration award."¹² Since Keystone and Michael and Terri Schwartz agree that Liberty Mutual should contribute to the arbitration award, so the argument goes, they are not true adversaries. The parties assertedly should be realigned to reflect the fact that Michael Schwartz and Terri Schwartz and Keystone have "common adversity to Liberty Mutual" and "share a common goal which is against the interests of Liberty Mutual."¹³

A. Fraudulent Joinder

In the absence of a federal question or fraudulent joinder, a complaint which joins a non-diverse defendant must fail for lack of jurisdiction. See Batoff v. State Farm Ins. Co., 977 F.2d 848, 851 (3d Cir. 1992) ("When a non-diverse party has been joined as a defendant, then in the absence of a substantial federal question the removing defendant may avoid remand only by demonstrating that the non-diverse party was fraudulently joined."); accord Vogt v. Time Warner Entm't Co., No. 01-905, 2001 U.S. Dist. LEXIS 4260, at *2 (E.D. Pa. Apr. 4, 2001); Greco v. Beccia, No. 99-2136, 2001 U.S. Dist. LEXIS 2647, at *12-22 (M.D. Pa. Feb. 13, 2001); Cipriani, 1999 U.S. Dist.

¹² Id. at 6.

¹³ Id.

LEXIS, at *4 (E.D. Pa. July 19, 1999). As there is no federal question here, Liberty Mutual must show that Keystone, the non-diverse respondent, has been fraudulently joined. The burden upon Liberty Mutual is "heavy." Batoff, 977 F.2d at 851; Boyer v. Snap-On Tools Corp., 913 F.2d 108, 111 (3d Cir. 1990).

As our Court of Appeals has stated, "Because a party who urges jurisdiction on a federal court bears the burden of proving that jurisdiction exists, a removing party who charges that a plaintiff has fraudulently joined a party to destroy diversity jurisdiction has a 'heavy burden of persuasion.'" Boyer, 913 F.2d at 111. "It is logical that [the removing party] should have this burden, for removal statutes 'are to be strictly construed against removal and all doubts should be resolved in favor of remand.'" Batoff, 977 F.2d at 851; see also Boyer, 913 F.2d at 111; Greco, 2001 U.S. Dist. LEXIS, at *19.

The assessment of whether joinder has been fraudulent need not involve inquiry into the plaintiff's state of mind, but, rather, a determination of whether the claims the plaintiff has maintained against the non-diverse defendant are "colorable," Batoff, 977 F.2d 848, 851-55; Boyer, 913 F.2d at 111:

Joinder is fraudulent 'where there is no reasonable basis in fact or colorable ground supporting the claim against the joined defendant, or no real intention in good faith to prosecute the action against the defendants or seek a joint judgment.' But, 'if there is even a possibility that a state court would find that the complaint states a cause of action against any one of the resident defendants, the federal court must find that joinder was proper and remand the case to state court.'

Batoff, 977 F.2d at 851 (citations omitted); see also Boyer, 913 F.2d at 111. A "possibility" that a complaint states a claim against the resident defendant (which negates fraudulent joinder) exists if any claim is not "wholly insubstantial and frivolous." Batoff, 977 F.2d at 853.

In Batoff, Stephen B. Batoff, a practicing psychologist, commenced an action against State Farm, the automobile insurance carrier of Batoff's patients, and Leonard M. Paul, a psychological-services investigator of State Farm, for breach of contract and state law torts. Id. at 849-50. State Farm removed the action to federal district court despite the common citizenship of Batoff and Paul in Pennsylvania, and asserted that Paul was immune from suit under state law and was only "joined by Batoff to defeat diversity jurisdiction which the district court otherwise could exercise." Id. at 850. The district court concluded that Paul was legally immune from suit. Id. It held that the complaint "fails to state a valid claim against Dr. Paul" and proceeded to dismiss Paul as improperly joined and exercised diversity jurisdiction. Id.

The Court of Appeals reversed, holding that there were at least colorable claims maintainable against non-diverse defendant Paul. Id. at 854. The Court distinguished between the level of scrutiny applied in deciding the validity of claims on the merits and deciding whether the claims are colorable -- the standard in assessing fraudulent joinder -- and stated, "[t]he inquiry into the validity of a complaint triggered by a motion to

dismiss under Rule 12(b)(6) is more searching than that permissible when a party makes a claim of fraudulent joinder." See id. at 852-54; see also Boyer, 913 F.2d at 112-13; Lyall v. Airtran Airlines, Inc., 109 F. Supp. 2d 365, 368 (E.D. Pa. 2000). The Court of Appeals concluded that since there existed at least a legitimate question about whether Paul was entitled to immunity it was erroneous for the district court to disregard the claims against Paul in delimiting jurisdiction. Batoff, 977 F.2d at 852-53. The immunity of resident defendant Paul from suit was an issue for state court determination because "[o]verall, we are satisfied that this is not a case in which we can say with any confidence that Batoff's claims against Paul are 'so defective that they should never have been brought at the outset.'" Id. at 853-54.

Boyer held, similarly, that assertions by removal defendants that individual defendants were insulated from suit by privileges and release agreements went to the merits of the action and did not amount to the requisite jurisdictional showing that such claims were frivolous and insubstantial. Boyer, 913 F.2d at 111-13. It was thus error for the district court to disregard the plaintiff's joinder claims and to entertain diversity jurisdiction.

Since Boyer and Batoff, district courts in this Circuit have consistently have held removal defendants to the "heavy burden" of proving fraudulent joinder in cases in which the presence of non-diverse defendants frustrate jurisdiction. In

Vogt, Judge Padova remanded a case to state court when he rejected Time Warner's argument that Comcast Cable was fraudulently joined because it was entitled to the defenses of passive conduit and the First Amendment. Vogt, 2001 U.S. Dist. LEXIS 4260, at *5-6, 9. Judge Padova found that the claims of publicity and misappropriation are cognizable in Pennsylvania and reasoned that any defenses Comcast Cable may have should be entertained on the merits in state court. Id. at 8. In Cipriani, in which the plaintiff commenced an action against an insurance company and its non-diverse general contractor for bad faith under 42 Pa. C.S.A. § 8371, Judge Kauffman held that since section 8371 applies by its terms only to the bad faith of an insurer,¹⁴ and many cases confirm that interpretation, the removal defendant met its "heavy burden" of showing that the plaintiff's claims against the general contractor were "wholly insubstantial and frivolous." Cipriani, 1999 U.S. Dist LEXIS at *5-6.

¹⁴ Actions on insurance policies

In an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured, the court may take all of the following actions:

- (1) Award interest on the amount of the claim from the date the claim was made by the insured in an amount equal to the prime rate of interest plus 3%.
- (2) Award punitive damages against the insurer.
- (3) Assess costs and attorney fees against the insurer.

42 Pa. C.S.A. § 8371.

Here, Liberty Mutual does not claim that joinder of Keystone was fraudulent. See Batoff, 977 F.2d at 850 (removing defendant alleging non-diverse defendant fraudulently joined); Boyer, 913 F.2d at 110 (same); Lyall, 109 F. Supp. 2d at 366 (same); Cipriani, 1999 U.S. Dist. LEXIS at *4 (same) (and court finding fraudulent joinder). Rather, it maintains that the litigation between Keystone and Michael Schwartz and Terri Schwartz is not really adverse and therefore Keystone should be realigned as a petitioner. We canvass that argument below. See discussion infra Part II.B.

We first note that we agree that the joinder of Keystone is not fraudulent. The claim of Michael and Terri Schwartz against Keystone to compel arbitration is colorable as it is cognizable under state law. See Vogt, 2001 U.S. Dist. LEXIS 4260, at *8; Lyall, 109 F. Supp. 2d at 370, 373. Section 7304 of the Pennsylvania Consolidated Statutes provides:

On application to a court to compel arbitration made by a party showing an agreement described in section 7303 (relating to validity of agreement to arbitrate) and a showing that an opposing party refused to arbitrate, the court shall order the parties to proceed with arbitration. If the opposing party denies the existence of an agreement to arbitrate, the court shall proceed summarily to determine the issue so raised and shall order the parties to proceed with arbitration if it finds for the moving party. Otherwise, the application shall be denied.

42 Pa. C.S.A. § 7304(a). The Schwartzes filed an application to compel arbitration pursuant to § 7304. It is "possible," and, indeed, does not appear to be in dispute, that the policies

between the claimants and their insurers contain agreements to arbitrate. That ends the jurisdictional inquiry.

If Keystone or Liberty Mutual, or both, wish to challenge the applicability of arbitration to the June 15, 1998 accident (and there is no indication that they do), that is for adjudication on the merits. The insistence of Liberty Mutual that we look behind the pleadings to ascertain whether a genuine dispute exists between the petitioners and respondent Keystone on liability takes us well beyond the "threshold jurisdictional issue into a decision on the merits." Boyer, 913 F.2d at 112. Not only does precedent in this Circuit prevent us from taking that route, but the Pennsylvania statute itself throws up its own barrier. Section 7304 specifies, "An application for a court order to proceed with arbitration shall not be refused...by the court on the ground that the controversy lacks merit or bona fides or on the ground that no fault or basis for the controversy sought to be arbitrated has been shown." 42 Pa. C.S.A. § 7304(e). In other words, under governing state law, the inquiry into whether the Petition states a valid claim -- much less whether it states a colorable claim -- is distinct from the question of whether the insurance claims are subject to arbitration.

This is not to say that we credit Liberty Mutual's argument that there are no genuine issues in dispute between the petitioners and Keystone on liability to be resolved in

arbitration. The strength of petitioners' liability claims are simply irrelevant in a petition to compel arbitration.

However, even if the inquiry into fraudulent joinder (and, thus, whether the claims against Keystone are frivolous and insubstantial) encompassed the ultimate insurance arbitration, we still would conclude Liberty Mutual has not met its "heavy burden". Petitioners joined Keystone, whom they had obtained an arbitration award against, in the Petition to compel arbitration because they allege under state law that Keystone is entitled to contribution from Liberty Mutual for the arbitration award. Petition, at ¶ 24. They cite 75 Pa. C.S.A. § 1733, which provides, "The insurer...shall process and pay the claim as if wholly responsible. The insurer is thereafter entitled to recover contribution pro rata from any other insurer for the benefits paid and the costs of processing the claim." 75 Pa. C.S.A. § 1733(b). Furthermore, a seasonable dispute may well exist between petitioners and Keystone in that they may contest who is entitled to any award entered against Liberty Mutual, and, if so, how much that award should be.

As this foray into uninsured motorist law shows, the Schwartzes' claims against Keystone are colorable. See Batoff, 977 F.2d at 853 ("A claim which can be dismissed only after an intricate analysis of state law is not so wholly insubstantial and frivolous that it may be disregarded for purposes of diversity jurisdiction.").

B. City of Indianapolis v. Chase National Bank

Liberty Mutual cites City of Indianapolis v. Chase National Bank, 314 U.S. 63 (1941), for the proposition that "It is our duty...to look beyond the pleadings and arrange the parties according to their sides in the dispute." Id. at 69 (quotations omitted); Mem. Law in Supp. of Mot. to Realign Keystone as Pet'r, at 4. It contends that under Third Circuit precedent construing the case "a court must first identify the primary issue in the controversy and then determine whether there is a real dispute by opposing parties over that issue." Id. (quoting Employers Ins. of Wasau v. Crown Cork & Seal Co., 942 F.2d 862, 864 (3d Cir. 1991)).

Liberty Mutual's reliance on City of Indianapolis is misplaced. On its face, City of Indianapolis does not apply to a case in which a complaint joins a non-diverse party. In City of Indianapolis, the plaintiffs joined diverse defendants and the Court concluded that it had to look beyond the pleadings to determine whether the limited jurisdiction of the federal courts was indeed validly invoked. Id. at 69, 76-77. Liberty Mutual cites it for the converse proposition, i.e., that a court must look beyond the pleadings to assess whether it may extend its diversity jurisdiction over an essentially state law conflict, despite extensive language in that case that the duty of a federal court to scrutinize the parties' alignment flows from its limited jurisdiction. Id. But the proper test when the plaintiff sues non-diverse defendants is fraudulent joinder. See

supra Part II.A. In fact, in Boyer, when the Court of Appeals articulated fraudulent joinder it disclaimed reliance on City of Indianapolis when it first observed, "There are substantially more cases dealing with a plaintiff's attempt to manufacture diversity than to destroy it." Boyer, 913 F.2d at 110.

A review of City of Indianapolis only confirms the propriety of remand here. The Supreme Court emphasized that "the dominant note in the successive enactments of Congress relating to diversity jurisdiction, is one of jealous restriction, of avoiding offense to state sensitiveness, and of relieving the federal courts of the overwhelming burden of business that intrinsically belongs to the state courts, in order to keep them free for their distinctive federal business" and that "in defining the boundaries of diversity jurisdiction, this Court must be mindful of this guiding Congressional policy." City of Indianapolis, 314 U.S. at 76-77 (quotations omitted). A petition to compel uninsured motorist arbitration is an intrinsically state law matter that, in the absence of diversity or fraudulent joinder, squarely "belongs to the state courts."

Furthermore, the Supreme Court in City of Indianapolis was guided by the policy of preventing parties from manipulating federal jurisdiction.¹⁵ That concern weighs against realignment

¹⁵ Id. at 69 ("Diversity jurisdiction cannot be conferred upon the federal courts by the parties' own determination of who are plaintiffs and who are defendants Litigation is the pursuit of practical ends, not a game of chess.").

here. As discussed, the petitioners have a non-frivolous basis for joining Keystone. It is true that had Liberty Mutual and Keystone both agreed to arbitration, or had both refused to arbitrate, their interests would well be adverse to the petitioners as the alleged responsible insurers. But neither of these events occurred. It was only Liberty Mutual's unilateral decision not to participate that led Keystone to hold the insurance bag at the arbitration. This result of Liberty Mutual's refusal does not change the reality that Keystone's ultimate responsibility to the Schwartzes remains to be determined. Thus, it is Liberty Mutual that seeks to move the chess pieces in ways that the "real" contest does not permit.

C. Costs and Attorney Fees

Petitioners Michael Schwartz and Terri Schwartz request reimbursement of costs and attorney fees under 28 U.S.C. § 1447(c), which provides, in relevant part, "An order remanding the case may require payment of just costs and any actual expenses, including attorney fees, incurred as a result of the removal". "A district court has broad discretion and may be flexible in determining whether to require the payment of fees under section 1447(c)." Mints v. ETS, 99 F.3d 1253, 1260 (3d Cir. 1996). As our extended discussion suggests, the issues presented in the notice of removal were not entirely clear-cut. Since Liberty Mutual presented a bona fide claim that removal

jurisdiction existed, we decline to exercise our discretion to order payment of fees and costs.

An Order follows.

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ORDER

AND NOW, this 18th day of December, 2001, upon consideration of the motion of respondent Liberty Mutual for realignment and the motion of petitioners for remand and fees and costs, and the responses thereto, and for the reasons set forth in the accompanying Memorandum, it is hereby ORDERED that:

1. The motion of Liberty Mutual for realignment is DENIED;
2. The motion of petitioners for remand and fees and costs is GRANTED IN PART;
3. This case is REMANDED to the Court of Common Pleas of Philadelphia County;
4. Liberty Mutual is not required to pay petitioners' attorney fees and expenses; and
5. The Clerk shall CLOSE this case statistically.

BY THE COURT:

Stewart Dalzell, J.