

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

<b>DANIEL P. FUSS BUILDERS- CONTRACTORS INC.,</b>	:	
<b>Plaintiff,</b>	:	<b>CIVIL ACTION</b>
	:	
<b>v.</b>	:	
	:	
<b>ASSURANCE COMPANY OF AMERICA and ZURICH AMERICAN</b>	:	<b>No. 06-1182</b>
<b>INSURANCE COMPANY,</b>	:	
<b>Defendants.</b>	:	

**MEMORANDUM AND ORDER**

**Schiller, J.**

**August 11, 2006**

This insurance action arises from Defendants’ alleged bad faith in delaying the settlement of a third party claim brought against their insured, Plaintiff Daniel P. Fuss Builders-Contractors Inc. (“Fuss Builders”). Plaintiff asserts claims for breach of contract, breach of fiduciary duty, and violation of Pennsylvania’s insurance bad faith statute. Plaintiff presents this Court with a novel issue: whether Pennsylvania law recognizes a bad faith cause of action against an insurer who ultimately settles a third party insurance claim within policy limits before an excess verdict has been entered. Presently before the Court is Defendants’ motion to dismiss Plaintiff’s Complaint. For the reasons below, the Court grants Defendants’ motion.

**I. BACKGROUND**

Fuss Builders, a Pennsylvania corporation, is a construction contractor with its principal place of business in Newtown Square, Pennsylvania. (Compl. ¶¶ 1, 9.) Assurance Company of America and its parent corporation Zurich American Insurance Company (“Defendants”) are New York corporations located in Schaumburg, Illinois. ( *Id.* ¶¶ 2-3.) Defendants, who transact business

throughout Pennsylvania, provided Fuss Builders with a speciality contractors insurance policy. (*Id.* ¶¶ 3, 5-6, 18; *see also* Defs.’ Mot. to Dismiss Ex. 2 (Insurance Policy).)

Plaintiff asserts the following facts. Prior to August of 1999, Mitchell Morgan frequently hired Fuss Builders to provide construction services for numerous investment properties in the Philadelphia area. (Compl. ¶ 9.) In the summer of 1999, Morgan hired Fuss Builders to build an addition to Morgan’s personal residence. (*Id.* ¶ 10.) In constructing an extension to Morgan’s finished basement, Fuss Builders failed to build a sufficient berm to retain excess water runoff. (*Id.* ¶¶ 11-13.) As a result, on August 27, 1999, heavy rains flooded the basement area and caused extensive damage. (*Id.* ¶ 14.) Fuss Builders’ president, Daniel Fuss (“Fuss”), admitted his company’s negligence to Morgan the following day, and Morgan retained Fuss Builders to repair the damage. (*Id.* ¶¶ 16-17.) Fuss Builders notified Defendants that its negligence resulted in a claim by Morgan that was covered by the insurance policy Fuss Builders maintained with Defendants. (*Id.* ¶ 19.) The total cost of the repairs was \$168,000, which included work by Fuss Builders in the amount of \$104,131, additional work by other contractors, and “the contents loss.” (*Id.* ¶ 20.) Morgan made a claim against Fuss Builders upon receiving the repair bill and withheld payment to Fuss Builders pending the outcome of the claim. (*Id.* ¶¶ 21-22.)

Defendants asserted their right and duty under the policy to defend Morgan’s claim against Fuss Builders. (*Id.* ¶ 23.) Defendants handled the claim but refused to offer Morgan more than \$70,000, despite Fuss Builders’ admission of negligence. (*Id.* ¶¶ 25-26.) After ten months of failed negotiations, Morgan filed suit against Fuss Builders. (*Id.*) Defendants hired the law firm of Post & Schell to handle the third party claim asserted by Morgan. (*Id.* ¶ 27.) Despite Fuss Builders’ admission of error and its pleas to promptly settle the claim, Post & Schell filed an answer denying

Fuss Builders' liability, without Fuss Builders' knowledge. (*Id.* ¶¶ 28-30, 35.)

Throughout the litigation, Post & Schell employed delay tactics, failed to update Fuss Builders regarding the litigation, and continued to deny Fuss Builders' liability despite the company's numerous admissions to the contrary. (*Id.* ¶¶ 32-33, 37-38, 41, 44-45.) As a result, Fuss Builders retained independent counsel, Joseph T. Mallon. (*Id.* ¶ 39.) Post & Schell's actions led to a court order directing Fuss Builders to respond without objections to discovery requests, to make Fuss available for deposition, and to pay a fine of \$750. (*Id.* ¶¶ 46-47.)

Although Fuss testified at his deposition in March of 2001 that Fuss Builders was at fault for the damages that Morgan's home suffered, Post & Schell continued to deny Fuss Builders' liability against the protests of Mallon and Fuss. (*Id.* ¶¶ 50-51, 53.) In October of 2001, Mallon informed Defendants via letter that their failure to reasonably resolve Morgan's claim was damaging Fuss Builders' business relationship with Morgan. (*Id.* ¶ 54.) Defendants never responded to Mallon's letter, which also explained the lack of evidence to contest Fuss Builders' liability. (*Id.* ¶¶ 55-57.) In January of 2002, Defendants offered Morgan \$90,000 to settle the claim, but Morgan refused the offer. (*Id.* ¶ 58.) Later that month, Post & Schell advised Mallon that Fuss' admission of liability might trigger an exclusion under Fuss Builders' insurance policy. (*Id.* ¶ 59.) Mallon informed Defendants that they were acting in bad faith and requested that Post & Schell be discharged as Fuss Builders' counsel. (*Id.* ¶¶ 61-63.) Defendants failed to respond to Mallon, but they made Morgan a second settlement offer of \$126,680 to Morgan in May of 2002. (*Id.* ¶¶ 62, 64.) This offer did not include Fuss Builders' profit or overhead, although these items were legitimate damages items for which Fuss Builders would have been liable had Morgan hired another contractor to repair his damaged basement. (*Id.* ¶¶ 65, 67-68.) When Mallon subsequently learned of Defendants'

settlement offer and omission of Fuss Builders' profit and overhead, he informed Defendants that Fuss Builders would not agree to the settlement. (*Id.* ¶ 71.)

At a pretrial conference in July of 2002, the judge advised Post & Schell that Defendants should pay the full \$168,000 in damages and cautioned Post & Schell about the risk of bad faith. (*Id.* ¶ 72.) Post & Schell reported the judge's advice to Defendants, but they refused to raise their settlement offer of \$126,680. (*Id.* ¶ 74.) Despite Fuss and Mallon's continued requests to resolve Morgan's claim, Post & Schell proceeded to file an untimely expert report as well as an untimely summary judgment motion. (*Id.* ¶¶ 73, 78, 81-82.) The court excluded the proposed expert testimony and denied the summary judgment motion. (*Id.* ¶¶ 75-76, 86.) However, Post & Schell's delay tactics forced a postponement of the January 2003 trial date. (*Id.* ¶¶ 84, 86.) A new trial date was set for the October 2003 term, but Post & Schell filed ten motions in limine a week prior to the start of the term, causing the trial date to be continued again. (*Id.* ¶¶ 87-88.) On January 21, 2004, the day before the trial was set to begin, the court denied Defendants' motions in limine as baseless, and Defendants made a settlement offer of \$156,240, which Morgan accepted. (*Id.* ¶¶ 89-90.)

As a result of this protracted four-year litigation, Morgan never resumed business with Fuss Builders, and Fuss Builders has lost substantial revenue and incurred additional attorneys' fees. (*Id.* ¶¶ 93-95.) Fuss Builders asserts that Defendants: (1) breached their contractual duty of good faith by unreasonably delaying the resolution of Morgan's claim; (2) acted in bad faith in violation of Pennsylvania's insurance bad faith statute, 42 Pa. Cons. Stat. § 8371; and (3) breached their fiduciary duty owed to Fuss Builders when handling third party claims. (*Id.* ¶¶ 98, 106-108, 114.) On May 22, 2006, Defendants filed a motion to dismiss the Complaint for failure to state a claim.

## II. STANDARD OF REVIEW

In considering a motion to dismiss for failure to state a claim upon which relief may be granted, courts must accept as true all factual allegations plead in the complaint and must draw all reasonable inferences in favor of the non-moving party. *Bd. of Trs. of Bricklayers & Allied Craftsmen Local 6 of N.J. Welfare Fund v. Wettlin Assocs., Inc.*, 237 F.3d 270, 272 (3d Cir. 2001). Courts are not obligated, however, to credit the complaint's "bald assertions" or "legal conclusions." *In re: Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1429 (3d Cir. 1997) (citation omitted). A motion to dismiss will only be granted if it is clear that relief cannot be granted to the plaintiff under any set of facts that could be proven consistent with the complaint's allegations. *Hishon v. King & Spalding*, 467 U.S. 69, 73 (1984) (citing *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957)).

## III. DISCUSSION

Defendants assert that Fuss Builders' claims are time-barred and that no cause of action exists if an insurer settles a third party claim within policy limits and before an excess verdict has been entered. (Defs.' Mem. of Law in Supp. of Mot. to Dismiss at 2-12.) Because the Court concludes that Fuss Builders has failed to state a cognizable cause of action for bad faith or breach of fiduciary duty under Pennsylvania law, the Court need not address the statute of limitations issue.

Pennsylvania's bad faith insurance statute provides:

In an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured, the court may 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 court costs and attorney fees against the insurer.

42 PA. CONS. STAT. ANN. § 8371 (2006). In order to establish bad faith under Section 8371, a plaintiff must prove the following by clear and convincing evidence: (1) the insurer lacked a reasonable basis for denying benefits; and (2) the insurer knew or recklessly disregarded its lack of reasonable basis. *Klinger v. State Farm Mut. Auto. Ins. Co.*, 115 F.3d 230, 233 (3d Cir. 1997) (citing *Terletsky v. Prudential Prop. & Cas. Ins. Co.*, 649 A.2d 680, 688 (Pa. Super. Ct. 1994)). Section 8371 does not supplant the common law remedy for breach of contract in bad faith actions. *See Birth Ctr. v. St. Paul Cos., Inc.*, 787 A.2d 376, 386 (Pa. 2001). Accordingly, an insured may recover compensatory damages for an insurer's bad faith breach of contract. *Id.* at 386 n.12, 387 n.15.

The novel issue now before the Court is whether Fuss Builders may assert a bad faith cause of action stemming from Defendants' delay in settling Morgan's third party claim, even though such claim was ultimately settled within policy limits and without the entry of an excess verdict.<sup>1</sup> Generally, courts have recognized bad faith actions stemming from an insurer's denial of coverage, delay of payment of a first party claim, or refusal to settle a third party claim which results in an excess verdict.<sup>2</sup> The Pennsylvania Supreme Court, however, has not directly addressed whether

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<sup>1</sup> As the Pennsylvania Supreme Court has not spoken on this issue and the parties have invoked the Court's diversity jurisdiction, this Court must predict how the Pennsylvania Supreme Court would resolve the issue. *See Robertson v. Allied Signal, Inc.*, 914 F.2d 360, 378 (3d Cir. 1990) ("In cases where the state's highest court has not considered the precise question to be answered, the federal court is called upon to predict how the state court would resolve the issue should it be called upon to do so.").

<sup>2</sup> The Third Circuit has explained the distinction between first and third party insurance claims as follows:

The primary aim of third-party insurance is to defend and indemnify insureds against liability for claims made against them as a result of their own conduct. First-party coverage, on the other hand, protects against loss caused by injury to the insured's own property. Wholly different interests are protected by the two distinct forms of coverage. Moreover, the parties to each form of insurance

Section 8371 can be applied to any insurer conduct beyond basic denial of coverage. Defendants argue that the Pennsylvania Supreme Court's definition of "bad faith" as "any frivolous or unfounded refusal to pay proceeds of a policy" embraces only the outright denial of coverage by an insurer. (Defs.' Mem. of Law in Supp. of Mot. to Dismiss at 9 n.14 (*quoting Terletsky*, 649 A.2d at 688), 15 n.18.)

In the context of first party claims or under-insured motorist claims, both the Pennsylvania Superior Court and the Third Circuit Court of Appeals have interpreted Section 8371 to include delay of payment by an insurer. *See, e.g., Polselli v. Nationwide Mut. Fire Ins. Co.*, 23 F.3d 747, 750-52 (3d Cir. 1994); *Condio v. Erie Ins. Exchange*, 899 A.2d 1136, 1144-45 (Pa. Super. Ct. 2006). However, the Court has failed to uncover a single federal or state court in Pennsylvania that has recognized a cause of action for an insurer's delay of payment in the context of a third party claim brought under Section 8371 or a contractual bad faith claim. With respect to actions arising from an insurer's refusal to settle that result in the entry of a verdict in excess of the insured's policy limits, numerous federal and state courts have recognized a cause of action for bad faith. (*See* Pl.'s Mem. of Law in Opp'n to Defs.' Mot. to Dismiss at 6 (listing cases).) Fuss Builders analogizes its cause of action to these cases, and draws heavily on the Pennsylvania Supreme Court's decision in *Birth Center* in support of its arguments. (*Id.* at 5, 11-12, 15-16.)

In *Birth Center*, an insurer unreasonably refused to settle a third party claim and, as a result,

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contract assume vastly different roles. In the third-party setting, the insurer and insured may generally be considered allies, but in the first-party context, the insured and carrier are placed in an adversarial position. We are persuaded that the time-honored distinction between the two types of insurance coverage is valid and should be maintained.

*Port Auth. of N.Y. & N.J. v. Affiliated FM Ins. Co.*, 311 F.3d 226, 233 (3d Cir. 2000).

an excess verdict was entered against the insured at trial. 787 A.2d at 379-81, 384. Although the insurer paid the excess verdict, the court also allowed the insured to recover its lost profits and compensatory damages under a contractual bad faith theory. *Id.* at 384-88. Fuss Builders contends that *Birth Center* eliminated the prerequisite of an excess verdict to establish a statutory or contractual bad faith claim for unreasonable failure to settle a third party claim. (Pl.'s Mem. of Law in Opp'n to Defs.' Mot. to Dismiss at 12, 15.) The Court rejects this interpretation. Indeed, the Court agrees with the more narrow reading of *Birth Center* espoused by Defendants. (*See* Defs.' Mem. of Law in Supp. of Mot. to Dismiss at 13.) The Pennsylvania Supreme Court did not address an insurer's *delay* in settling a third party claim in *Birth Center*, but instead it maintained the insured's right to recover compensatory damages for contractual bad faith when its insurer unreasonably *refused* to settle such claim. *See Birth Center*, 787 A.2d at 384-88. The Pennsylvania Supreme Court simply did not address the situation the Court confronts here, nor has any other federal or state court in Pennsylvania. This Court will not create a cause of action not yet recognized by Pennsylvania law.

Under Pennsylvania law, the Court finds that there is no recognized cause of action against an insured for delaying settlement of a third party claim.<sup>3</sup> While Fuss Builders paints a disturbing picture of improper conduct on the part of Defendants, the Pennsylvania legislature has not yet

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<sup>3</sup> The Court concludes that no cause of action exists for Fuss Builders' novel breach of fiduciary duty claim. Numerous courts applying Pennsylvania law have held that breach of fiduciary duty claims are subsumed under statutory and/or contractual bad faith claims. *See, e.g., Johnson v. Northland Ins. Co.*, Civ. A. No. 05-927, 2005 WL 3488712, at \*5 (W.D. Pa. Dec. 21, 2005); *Belmont Holdings Corp. v. Unicare Life & Health Ins. Co.*, Civ. A. No. 98-2365, 1999 WL 124389, at \*4 (E.D. Pa. Feb. 5, 1999); *Wood v. Allstate Ins. Co.*, Civ. A. No. 96-4574, 1996 WL 637832, at \*2 (E.D. Pa. Nov. 4, 1996). Indeed, Fuss Builders' three claims all seek to recover for the same alleged bad faith conduct of Defendants, conduct for which a cause of action has not been recognized in Pennsylvania.

created a cause of action for Defendants' conduct, nor has the Pennsylvania Supreme Court found that one exists under current law. Accordingly, the Court dismisses Fuss Builders' action for failure to state a claim upon which relief may be granted.

#### **IV. CONCLUSION**

For the foregoing reasons, Defendants' motion to dismiss the Complaint is granted. An appropriate Order follows.

**IN THE UNITED STATES DISTRICT COURT  
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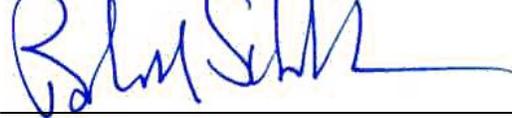
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<b>Plaintiff,</b>	:	<b>CIVIL ACTION</b>
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<b>INSURANCE COMPANY,</b>	:	
<b>Defendants.</b>	:	

**ORDER**

**AND NOW**, this 11<sup>th</sup> day of **August, 2006**, upon consideration of Defendants' Motion to Dismiss Plaintiff's Complaint, Plaintiff's response thereto, Defendants' reply thereon, and for the foregoing reasons, it is hereby **ORDERED** that:

1. Defendants' motion (Document No. 6) is **GRANTED**.
2. The Clerk of Court is directed to close this case.

**BY THE COURT:**



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**Berle M. Schiller, J.**