

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

STEVEN LIEBERSON : CIVIL ACTION  
: :  
v. : :  
: :  
CHUBB LIFE INSURANCE COMPANY :  
OF AMERICA : NO. 97-5716

M E M O R A N D U M

Ludwig, J.

July 14, 1998

On August 18, 1997 plaintiff filed this action in the Montgomery County Court of Common Pleas for breach of a residual disability insurance policy, including bad faith, 42 P.C.S.A. § 8371 (Supp. 1998). On September 30, 1997 defendant removed. 28 U.S.C. § 1441 (1994).<sup>1</sup> On cross-motions for summary judgment, Fed R. Civ. P. 56,<sup>2</sup> defendant was found to be liable on the claim for residual disability benefits from December 2, 1996 to the present. At a hearing on April 27, 1997, the parties made proffers of

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<sup>1</sup> Jurisdiction is federal question. 28 U.S.C. § 1332 (1994).

<sup>2</sup> "[S]ummary judgment should be granted if, after drawing all reasonable inferences from the underlying facts in the light most favorable to the non-moving party, the court concludes that there is no genuine issue of material fact to be resolved at trial and the moving party is entitled to judgment as a matter of law." Kornegay v. Cottingham, 120 F.3d 392, 395 (3d Cir. 1997) (quoting Spain v. Gallegos, 26 F.3d 439, 446 (3d Cir. 1994) (citations omitted)).

evidence on plaintiff's bad faith claim and agreed that the facts presented were not in dispute. Tr. at 12, Apr. 27, 1997.<sup>3</sup>

1. Residual disability benefits (Count I) – The parties dispute the meaning of "monthly earned income" under the policy. The policy states that to qualify for residual disability benefits, the insured "must be earning at least 20% less than his or her monthly earned income base." Defendant's memorandum, exh. a, at 3. The policy defines "monthly earned income":

The amount of income, net of reasonable and necessary business expenses, earned in a calendar month by the insured from his regular occupation, based on accrual accounting as used for the federal income tax. . . . Earned income does not include . . . amounts deducted from gross income as business expenses for the federal income tax.

Id.

Defendant's motion asserts that plaintiff's monthly earned income for the relevant period should include losses from a corporation, Dumont Carpet, Inc., of which plaintiff was president and 90 percent owner. Id. at 10-14. If these amounts are included, plaintiff's monthly earned income in the period prior to his claim for disability is zero. Id. at 9. Defendant's motion argues:

"Plaintiff, as 90% owner and president of Dumont Carpet, dictated what his salary would be and what amount would be left in the busi-

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<sup>3</sup> The April 22, 1997 order did not rule on the amount of benefits due under the policy. At the proffer hearing, the parties stated that the amount due – while still subject to verification and calculation – was no longer in dispute. Tr. at 4, Apr. 27, 1997.

ness. It was entirely up to him as to what amount was disclosed as salary on his personal tax return versus what figure was recorded as income on the business return. . . . Fundamental fairness dictates that an insurer be permitted to consider an insured's wholly-owned business in making policy decisions. Otherwise, an insured is free to manipulate policy determinations in a manner different from other insureds.

Id. at 12-13.

While that position may comport with a popular conception, Pennsylvania law stringently distinguishes between corporations and individuals. "[T]here is a strong presumption in Pennsylvania against piercing the corporate veil." Lumax Industries, Inc. v. Aultman, 543 Pa. 38, 669 A.2d 893, 895 (1995) (citing Wedner v. Unemployment Board, 449 Pa. 460, 464, 296 A.2d 792, 794 (1972) ("[A]ny court must start from the general rule that the corporate entity should be recognized and upheld, unless specific, unusual circumstances call for an exception.") (further citation omitted)). Lumax listed the following factors to be considered in disregarding the corporate form: (1) undercapitalization; (2) failure to adhere to corporate formalities; (3) substantial intermingling of corporate and personal affairs; and (4) use of the corporate form to perpetrate a fraud. Id. (citation omitted).

Here, adopting defendant's position would be tantamount to piercing Dumont Carpet's corporate veil. Defendant, however, offers no evidence of fraud - or, indeed, of any of the above-listed factors - during the relevant insurance period. That

plaintiff owned 90 percent of the corporation does not by itself establish that he and the corporation should be treated as a single entity.<sup>4</sup> Id. (citing College Watercolor Group, Inc. v. William H. Newbauer, Inc., 468 Pa. 103, 117, 360 A.2d 200, 207 (1976) (general rule is that corporation shall be regarded as an independent entity even if its stock is owned entirely by one person)). Defendant's rationale for calculating plaintiff's monthly earned income is, therefore, insufficient as a matter of law. Plaintiff is entitled to residual benefits under the policy.<sup>5</sup>

2. Bad faith (Count II) – To establish a claim for bad faith under 42 P.C.S.A. § 8371, plaintiff must prove by clear and convincing evidence that the insurer (1) lacked a reasonable basis for denying benefits; and (2) knew or recklessly disregarded its lack of reasonable basis. Klinger v. State Farm Mutual Automobile

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<sup>4</sup> Defendant's motion admits that no case law directly supports its position, defendant's memorandum, at 10, but cites two cases, Gonzalez-Marin v. Equitable Assurance Society of the United States, 845 F.2d 1140 (1st Cir. 1988), and Lichtman v. Massachusetts Casualty Ins. Co., No. 94-CV-2255, 1994 WL 470337 (E.D. Pa. Aug. 18, 1994), for the proposition that income or losses from a business can be included in an individual's income calculation for an insurance claim. The former case, however, does not identify the legal status of the business in question, Gonzalez-Marin, 845 F.2d at 1144-45, while the latter refers to the business as a partnership, Lichtman, 1994 WL 470337, at \*2.

<sup>5</sup> While this is not the typical piercing case – i.e., a plaintiff attempting to hold an individual liable for the debts of a corporation – defendant here would do substantially the same thing. By including the losses of Dumont Carpet, Inc., in plaintiff's monthly earned income, defendant would make plaintiff responsible for them. Defendant argues for an equating of legal interests that federal income tax law does not require and – given defendant's lack of evidence – Pennsylvania law does not allow.

Ins. Co., 115 F.3d 230, 233 (3d Cir. 1997) (citing Terletsky v. Prudential Property & Cas. Ins. Co., 437 Pa. Super. 108, 649 A.2d 680, 688 (1994), appeal denied, 540 Pa. 641, 659 A.2d 560 (1995)). In this case, there was a proffer of creditable evidence that defendant believed its view of the applicable law was consistent with insurance company standards. It was placed on notice by plaintiff's counsel that its interpretation of the law was incorrect. However, that by itself is not clear and convincing evidence that it knew or recklessly disregarded the lack of a reasonable basis for the denial of plaintiff's benefits. Given the circumstances, what was proved was a negligent, albeit self-serving, first-time mistake. There was no history adduced of a culpable repetition of denials on the same or similar sets of facts or that defendant's view was not commonplace among disability benefit insurers.

Accordingly, summary judgment on the bad faith claim will be entered against plaintiff and in favor of defendant.

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Edmund V. Ludwig, J.