

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

CHESTER PERFETTO : CIVIL ACTION  
AGENCY, INC. :  
 :  
v. :  
 :  
CHUBB & SON, a division :  
of Federal Insurance :  
Company, et al. : NO. 99-3492

M E M O R A N D U M

**Padova, J.**

October 21, 1999

This is a contract case initiated by Chester Perfetto Agency ("Chester") against Defendants Chubb & Son, Inc. ("CSI"), Chubb & Son ("Chubb"), and Ronald Spaulding ("Spaulding"), an officer of either CSI or Chubb.

Chester markets and sells insurance products, acting as a general agent for travel insurance underwritten by Chubb. Chester is compensated for its services in two ways: (1) regular sales commissions under the Agency Agreement; and (2) incentive payments for meeting specified performance goals under the Contingent Commission Point Program Agreement ("Incentive Agreement"). In this suit, Chester asserts that Chubb deliberately miscalculated the incentive commissions payable in 1998, resulting in underpayment by \$330,000.

Calculation of these incentive commissions is based on data for growth, loss ratio, and retention for each calendar year.

Loss ratio for a given calendar year is defined under the Incentive Agreement as the total reported losses and allocated loss adjustment expense for certain types of insurance products written by Chubb through Chester, divided by the gross earned premium for such business. The incentive commissions themselves are calculated as a multiple of reward points that are listed in a table attached to the Incentive Agreement. For each reward point, Chubb must pay one percentage of Chester's annual gross written premium for certain types of products written by Chubb.

In 1998, Chester believes it had a loss ratio of less than 49%, thus entitling it to receive an incentive commission of at least \$495,000.00. However, Chubb calculated Chester's loss ratio to be 68%, justifying payment of only \$165,970.48. Chester asserts that Chubb deliberately miscalculated this ratio by deducting commissions Chubb paid to travel agencies through whom Chester marketed and sold Chubb's insurance products, and by improperly including certain claims.

Chester asserts three claims in its Complaint. Count I alleges breach of contract against Chubb and CSI. Count II seeks tort recovery for breach of the principal's duty of good faith and fair dealing to its agent from Chubb, CSI, and Spaulding. Count III alleges breach of the implied contractual duty of good faith and fair dealing against Chubb and CSI.

Defendants have filed a Motion to Dismiss pursuant to Fed.

R. Civ. P. 12(b)(6) counts II and III in their entirety, and count I as against CSI only.

#### **I. STANDARD OF REVIEW**

This Court may dismiss a claim under Fed. R. Civ. P. 12(b)(6) only if the plaintiff can prove no set of facts in support of the claim that would entitle him to relief. ALA, Inc. v. CCAIR, Inc., 29 F.3d 855, 859 (3rd Cir. 1994). The reviewing court must consider only those facts alleged in the complaint and accept all of the allegations as true. Id.

#### **II. DISCUSSION**

##### **A. CSI**

Defendants seek to dismiss all counts as to CSI because CSI never signed or ratified any of Chester's agreements with Chubb, so it was not a party to the contract at issue.

In order to prove a breach of contract under Pennsylvania law, a plaintiff must show: (1) the existence of a valid and binding contract to which the plaintiff and defendants were parties; (2) the contract's essential terms; (3) that plaintiff complied with the contract's terms; (4) that the defendant breached a duty imposed by the contract; and (5) damages resulting from the breach. Bosum Rho, M.D. v. Vanguard OB/GYN Assoc., P.C., No. CIV. A. 98-1673, 1999 WL 228993, at \*3 (E.D.Pa. Apr. 15, 1999).

Because Defendant CSI was not a party to or signatory of any of the contracts involved in this dispute, Chester cannot show

the existence of a valid and binding contract to which CSI was a party. For this reason, counts I and III as against CSI are dismissed with prejudice.

Although count II alleges a cause of action sounding in tort, the underlying facts that form the basis for the claim arise from the parties' duties pursuant to the Incentive Agreement between Chester and Chubb. Since CSI was not a party to or signatory of this contract, it cannot be held liable on this count. For this reason, count II as against CSI is dismissed with prejudice.

**B. Tortious Breach of the Implied Duty of Good Faith  
from a Principal to an Agent**

Defendants further seek to dismiss Count II, tortious breach of the implied duty of good faith from a principal to an agent, in its entirety on the grounds that no such tort exists under Pennsylvania law. Chester concedes that Pennsylvania does not recognize this tort, but counters that New Jersey law does and should apply to this action. Because I find that New Jersey law does not recognize a generalized implied duty of good faith from a principal to an agent, there is no choice of law issue.

Although no New Jersey court has ever explicitly held that a duty of good faith runs from a principal to an agent, CPA cites language in dictum from one New Jersey case as authority for the proposition that such a cause of action exists, Louis Schlesinger Co. v. Wilson, 127 A.2d 13, 18 (N.J. 1956).

Schlesinger involved a suit brought by a real estate broker seeking to recover commissions based upon an oral contract. Id. at 14. The broker and the owner had entered into an oral agreement whereby the broker promised to find a purchaser for the owner's land in exchange for 10% of the purchase price of the completed sale. Id. After the broker found a buyer, he learned that the owner had previously entered into an option contract with another party. Id. at 15. The broker then sued to obtain payment of his commission based on breach of contract and the tort of misrepresentation. Id.

The Schlesinger court held that the broker could not sue on a contract theory because the statute of frauds prevented enforcement of the oral agreement. Id. at 18. However, the court allowed the broker to proceed under tort on a fraud and deceit theory. Id. In so holding, the court stated:

Although we think the fraud complained of is insufficient to remove the bar of the statute, there is no reason why the defendant should not be directed to respond to the second court which sounds in tort. The charge is not made to enforce the contents of the oral agreement but to compensate the plaintiff for its loss engendered by the deceit. **The confidence arising from a principal-agent relationship is not charted on a one-way street. Good faith works in both directions.**

Id. (internal citations omitted; emphasis added). Chester asserts that through those last two sentences the New Jersey Supreme Court created a tort for breach of the duty of good faith by a principal.

This Court believes that two sentences in dictum is too flimsy a hook on which to hang a newly-created tort. No New Jersey court has ever cited Schlesinger as authority for the creation of such a duty, nor has a court ever made use of this tort. See McCann v. Biss, 322 A.2d 161, 166 (N.J. 1964) (explaining Schlesinger as holding that owners could be liable for misrepresentation to their brokers). The Restatement of Torts (Second) is also silent on this alleged duty.

The Restatement (Second) of Agency identifies the general duty of a principal to keep and render accounts of the amount due from him to an agent, and the corollary duty to permit the agent to ascertain the amount due. Restatement (Second) of Agency § 436 (1958). However, breach of this duty opens the principal to liability under contract law principles only, not tort. Id. cmt. b (1958).

The only other duty of a principal to an agent that is remotely applicable is the duty to give the agent information:

Unless otherwise agreed, it is inferred that a principal contracts to use care to inform the agent of risks of physical harm or pecuniary loss which, as the principal has reason to know, exist in the performance of authorized acts and which he has reason to know are unknown to the agent.

Restatement (Second) of Agency § 435 (1958). The commentary states that the duty arises from the common understanding that the principal will use care to prevent harm coming to the agent in the pursuit of the enterprise. Id. cmt. a (1958). However,

the circumstances in which this duty applies are inapposite to those in this case. See Restatement (Second) of Agency cmts. a-c (1958)(citing as examples warning a sales agent of unsound products if the agent could incur personal liability for misrepresentation to a buyer; providing information regarding product quality and price to sales agents working on commission; and informing the agent of termination of the agency contract).

This Court can find no authority under New Jersey law to support the application of such a cause of action to this case. Therefore, the Court finds that count II does not allege a cause of action upon which relief may be granted under the facts of this case, and accordingly dismisses the count with prejudice.

**C. Breach of Implied Contractual Duty of Good Faith and Fair Dealing**

Defendants seek dismissal of Count III, breach of the implied contractual duty of good faith and fair dealing, on the grounds that Pennsylvania law does not recognize this cause of action where the plaintiff has other sufficient causes of action to vindicate its rights. Defendants are correct in that the Third Circuit Court of Appeals has established that under Pennsylvania law, no duty of good faith and fair dealing can be implied where adequate remedies under an established cause of action based on the same conduct are available to the plaintiff. Parkway Garage, Inc. v. City of Philadelphia, 5 F.3d 685, 702

(3rd Cir. 1993).

In that case, the Court held that Pennsylvania law does not imply a duty of good faith into every contract; but rather will only do so when there is no other viable cause of action under which the party can seek relief. Id. at 701-2. Thus, where a plaintiff has an independent cause of action that he can invoke to vindicate his interests, no duty of good faith attaches to the contract. Id.; Bagasra v. Thomas Jefferson Univ., No. CIV. A. 99-CV-2321, 1999 WL 517404, at \*1 (E.D.Pa. July 20, 1999); Fremont v. E.I. Dupont DeNemours & Co., 988 F. Supp. 870, 875 (E.D.Pa. 1997).

District courts are bound to follow the predictions and interpretations of state law made by their appellate court. Fremont, 988 F. Supp. at 875. Here, Chester may seek relief on a breach of contract theory based on the same conduct for which it alleges breach of the implied duty. Thus, under Parkway, the duty would not be implied.

However, CPA also advances another theory that could authorize a court to infer a duty of good faith. CPA argues that the doctrine of necessary implication requires that an implied duty to act in good faith be read into the express terms of the agreement. Slagan v. John Whitman & Assoc., No. Civ. A. 97-3961, 1997 WL 587354, at \*4 (E.D.Pa. Sept. 10, 1997); Doylestown Assoc. v. Street Retail, Inc., No. CIV. A. 96-CV-4367, 1996 WL

601679, at \*2 (E.D.Pa. Oct. 18, 1996); Killian v. McCullough, 850 F. Supp. 1239, 1250-51 (E.D.Pa. 1994). Pennsylvania courts explain the doctrine of necessary implication as follows:

In the absence of an express provision, the law will imply an agreement by the parties to a contract to do and perform those things that according to reason and justice they should do in order to carry out the purpose for which the contract was made and to refrain from doing anything that would destroy or injure the other party's right to receive the fruits of the contract.

Somers v. Somers, 613 A.2d 1211, 1214 (Pa. Super. Ct. 1992)(quoting Frickert v. Deiter Bros. Fuel Co., 347 A.2d 701, 705 (Pa. 1975)(Pomeroy, J., concurring).

This doctrine imposes a requirement of good faith that allows a court to imply a term into a contract where the term was contemplated by the parties at the time of contracting or is necessary to carry out the intention of the parties, even when the express terms of the contract are unambiguous. Slagan, 1997 WL 587354, at \*4. However, the implied duty of good faith cannot defeat a party's express contractual rights by imposing obligations that the party expressly contracted to avoid. Southern Ocean Seafood Co. v. Holt Cargo Sys., Inc., No. CIV. A. 96-5217, 1997 WL 539763, at \*11 (E.D.Pa. Aug. 11, 1997); Creeger Brick & Bldg. Supply, Inc. v. Mid-State Bank & Trust Co., 560 A.2d 151, 153 (Pa. Super. Ct. 1989).

The implied covenant of good faith and fair dealing

"involves an implied duty to bring about a condition or exercise discretion in a reasonable way." USX Corp. v. Prime Leasing, Inc., 988 F.2d 433, 438 (3rd Cir. 1993). Bad faith performance of contractual duties varies with the context, but includes evasion of the spirit of the bargain and abuse of a power to specify terms. Somers, 613 A.2d at 1213.

The Incentive Agreement between Chubb and Chester contains a clause that states:

You agree that our records, computations and other procedures will be used to evaluate and compute your contingent commission, and will be binding.

This clause expresses Chubb's intent to retain unfettered discretion to use its own method of calculation to compute Chester's incentive commissions that would then be binding upon Chester. However, Pennsylvania courts have held that even where a party has expressly contractually agreed to allow another party to set the amount to be paid under the contract, the latter party has an implied duty of good faith in setting the amount.

Germantown Mfg. Co. v. Rawlinson, 491 A.2d 138, 148 (Pa. Super. Ct. 1985). A court may imply a promise "to act in good faith in determining and setting the amount owed." Id. Therefore, the Court finds that Pennsylvania law would imply a duty of good faith in the setting of the amount payable under the Incentive Agreement. Because Chester has stated a claim upon which relief could be granted, the Court will not dismiss count III.

### **III. CONCLUSION**

For the above reasons, the Court grants in part and denies in part Defendants' Motion to dismiss. The Court dismisses with prejudice counts I and III as against CSI, and count II in its entirety. However, the Court declines to dismiss count III as against Chubb & Son.

The Court's decision leaves Chubb & Son as the sole remaining defendant, since the Court is dismissing all of Plaintiff's claims against CSI and Spaulding was only named as a Defendant in count II. Therefore, count I for breach of contract and count III for breach of implied duty of good faith and fair dealing will proceed against Chubb & Son. All other claims and defendants are dismissed from the suit.

An appropriate order follows.

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O R D E R

**AND NOW**, this day of October, 1999, upon consideration of Defendants' Motion to Dismiss (Doc. No. 7), Plaintiffs' Response thereto (Doc. No. 11), and Defendants' Reply thereto (Doc. No. 15), **IT IS HEREBY ORDERED** that Defendant's Motion is **GRANTED** in part and **DENIED** in part<sup>1</sup>:

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<sup>1</sup>By this Order, Chubb & Son, Inc. and Ronald Spaulding are dismissed entirely from this suit. Thus, Chubb & Son, a division of Federal Insurance Company, is the sole remaining Defendant.

The remaining claims in this suit are count I, breach of contract, and count III, breach of implied duty of good faith and

1. Count I is **DISMISSED WITH PREJUDICE** as against Chubb & Son, Inc.;
2. Count II is **DISMISSED WITH PREJUDICE**;
3. Count III is **DISMISSED WITH PREJUDICE** as against Chubb & Son, Inc.;
4. Ronald Spaulding is **DISMISSED** from this suit as a Defendant;
5. Chubb & Son, Inc. is **DISMISSED** from this suit as a Defendant.

BY THE COURT:

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John R. Padova, J.

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fair dealing.