

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

Atlas Communications, Ltd. : CIVIL ACTION
 :
 v. :
 :
 Lyman E. Waddill and Integrity :
 Telecom, Inc. : No. 97-1373

MEMORANDUM OF DECISION

Norma L. Shapiro J.

August 12, 1997

This breach of contract action was brought by Atlas Communications Ltd. ("Atlas") against Integrity Telecom, Inc. ("Integrity") and its principal agents, Lyman E. Waddill ("Waddill") and Paul Dugan ("Dugan"). Jurisdiction is conferred upon this court by 28 U.S.C. §1332.¹ At the commencement of this action, Atlas was incorporated in Pennsylvania and defendants Waddill, Dugan and Integrity resided in California. Plaintiff's alleged damages are in excess of the statutory requirement of \$75,000.

On April 24, 1997, Atlas filed a motion for default against defendant, Waddill. This motion was granted, pursuant to Fed.R.Civ.P. 55(a)² by order of April 24, 1997. On June 16,

1. 28 U.S.C. § 1332 states: "The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of \$75,000, exclusive of interest and costs, and is between. . .(1) citizens of different States. . ."

2. Fed.R.Civ.P. 55(a) states: "When a party against whom a judgment for affirmative relief is sought has failed to plead or otherwise defend as provided by these rules. . . the clerk shall enter the party's default."

1997, defendant Waddill filed a motion under Fed.R.Civ.P. 55(c)³ to set aside the default because mistake and excusable neglect caused delay in answering the complaint. Upon consideration of defendant Waddill's motion to set aside the default, the plaintiff's emergency opposition, and a hearing held on July 28, 1997, the court will grant defendant Waddill's motion setting aside the default.

BACKGROUND

Atlas is a telephone company dealing primarily in domestic long-distance service provided to customers that resell the service; Atlas provides some international service if it is a small portion of the reseller's overall need. Atlas' service derives from Sprint's long-distance network. Integrity specializes in servicing companies that sell prepaid debit card service to long-distance telephone users. Atlas alleges that in mid-December, 1996, Integrity's agents contracted to purchase long-distance phone service from Atlas to resell to its customers as a result of Integrity's financial problems with its original supplier. In February, 1997, a dispute arose over the amount of money Integrity owed to Atlas. Service was terminated by Atlas on February 12, 1997.

3. 28 U.S.C. Fed.R.Civ.P. 55(c): Setting Aside Default. For good cause shown the court may set aside an entry of default and, if a judgment by default is entered, may likewise set it aside in accordance with Fed.R.Civ.P. 60(b).

On February 24, 1997, Atlas filed this action against Integrity⁴ and its principal agents, Paul Dugan⁵ and Lyman E. Waddill. On or about April 1, 1997, Waddill was served by Atlas with a summons and a verified complaint.⁶ No response having been filed, the court entered a default against Waddill three days later on April 24, 1997. Plaintiff then filed a motion for judgment by default under Fed.R.Civ.P. 55(b)(2). On June 16, 1997, before judgment had been entered for Atlas, Waddill filed a pro se motion to set aside the default. Oral argument on whether to set aside the default was heard by the court on July 22, 1997.

DISCUSSION

It is in the court's discretion to decide if entry of default is proper. A default is not favored and doubt should be resolved in favor of setting aside the default and reaching a decision on the merits. Gross v. Stereo Component Systems, Inc., 700 F.2d 120, 122 (3rd Cir. 1983), citing Farnese v. Bagnasco, 687 F.2d 761, 764 (3rd Cir. 1982).

4. Integrity was served with a complaint on February 24, 1997. Default was entered against Integrity under Fed.R.Civ.P. 55(a) for failure to plead or otherwise defend on March 21, 1997. Plaintiff moved for judgment by default under Fed.R.Civ.P. 55(b). This motion is still pending.

5. Defendant Dugan was served with a complaint on April 17, 1997. Default was entered against Dugan on May 8, 1997 for failure to file a responsive pleading or enter an appearance. On May 9, 1997, Dugan filed a motion to strike and/or set aside entry of default. There was a challenge made as to this court's exercise of personal jurisdiction over Dugan and he was voluntarily dismissed by the plaintiff on May 23, 1997.

6. Service was accepted by Waddill's wife.

Under Fed.R.Civ.P. 55(c), a court may set aside a default for good cause. The court must consider: (1) whether lifting the default would prejudice the plaintiff, (2) whether the defendant has a prima facie meritorious defense, and (3) whether the defaulting defendant's conduct is excusable or culpable. Spurio v. Choice Sec. Sys., Inc., 880 F.Supp 402, 404 (E.D.Pa. 1995); Emcasco Ins., Co., v. Sambrick, 834 F.2d 71, 73 (3rd Cir. 1987); \$55,518.05 in U.S. Currency, 728 F.2d 192 (3rd Cir. 1984); Feliciano v. Reliant Tooling Co., 691 F.2d 653, 656 (3rd Cir. 1982).

The court must first consider whether opening the default would disadvantage plaintiff's case to its prejudice. Prejudice can be shown through loss or destruction of evidence, increased potential for fraud and collusion, or substantial reliance upon the entry of default. Feliciano, 691 F.2d at 657; Gross, 700 F.2d at 123. In the present action, no such facts were alleged. Plaintiff argued that Waddill has lied under oath in the past and this would increase the chance for fraud and collusion if the default were set aside and that Waddill will consume his assets if given more time. These arguments do not explain how the plaintiff would be harmed by defending the action on the merits. The prejudice alleged by the plaintiff addresses credibility issues and does not rise to the level of prejudice needed to sustain an entry of default.

"The showing of a meritorious defense is accomplished when allegations of defendant's answer, if established at trial, would

constitute a complete defense." Hritz v. Woma Corp., 732 F.2d 1178, 1181 (3rd Cir. 1984). To determine whether the defendant's defense is meritorious, the court looks at the plaintiff's allegations. See \$55,518.05 in U.S. Currency, 782 F.2d at 195. The claims against Waddill are for breach of contract and fraudulent misrepresentation. In Waddill's motion to set aside the default and affidavit in support of the motion, he alleges that he is only a 5% shareholder in Integrity and was not an officer at the time of the contract between Atlas and Integrity. He also denies making fraudulent statements in negotiating the contract. Defendant's proffered defense, if proven at trial, would provide a complete defense.

In evaluating whether the defendant's conduct is culpable in causing default, the court must decide if defendant's actions were caused by mistake or excusable neglect. See Feliciano, 691 F.2d at 656. "Appropriate application of the culpable conduct standard requires that as a threshold matter more than mere negligence be demonstrated." Hritz, 732 F.2d at 1183. Wilfulness or bad faith is required to defeat vacating the default.

Waddill's motion alleges that he was ignorant of federal law concerning the time limit for filing a responsive pleading. He also claims that counsel, because of his limited assets, had trouble finding local counsel. These proffered reasons demonstrate there was no "flagrant bad faith" and no culpable conduct. Emcasco Ins., Co., 834 F.2d at 75. Because there is a

strong preference to decide cases on the merits rather than by default, defendant's actions are excusable and not sufficient to preclude vacating a default that has not yet been entered as a judgment.

For the reasons stated in this opinion, the defendant's motion to set aside the default was granted by Order filed July 28, 1997.