

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

MORTON'S RESTAURANT GROUP, INC. : CIVIL ACTION  
: :  
v. : :  
: :  
DANIEL CHAREST and CORSICA, INC. : No. 97-7013

**MEMORANDUM AND ORDER**

Yohn, J.

November , 1998

Corsica, Inc. [hereinafter "Corsica"] is the lessee of a restaurant property and restaurant equipment. Morton's Restaurant Group, Inc. [hereinafter "Morton"] is the guarantor of both leases. Corsica agreed to indemnify Morton if Corsica defaulted on either lease. When Corsica failed to pay its rent, Morton sued Corsica. Corsica responded that the leasing contracts were fraudulently induced and, therefore, no indemnification payments were due. Morton filed a motion for summary judgment. Because no evidence of any fraud has been produced, I will grant plaintiff's motion for summary judgment.

**I. FACTS**

On December 2, 1993, Peasant at Locust Street, Inc. [hereinafter "Peasant"] leased a restaurant, located at 1500 Locust Street, Philadelphia, from 1500 Locust Limited Partnership, for a term of fifteen years. Peasant also leased restaurant equipment from General Electric Capital Corporation, on October 11, 1994. Morton's Restaurant Group, Inc., which is Peasant's parent company, guaranteed both leases. In October 1996,

Peasant assigned the restaurant lease to Corsica, Inc., so that Corsica could run a restaurant called Napoleon on the premises. Peasant also subleased the restaurant equipment to Corsica.

After the assignment and sublease, Morton remained a guarantor on both the original leases. Corsica and Daniel Charest, Corsica's sole shareholder, entered into an indemnification agreement with Morton whereby if Corsica defaulted on either lease, Daniel Charest and Corsica agreed to indemnify Morton for any payments made under the guarantees. Corsica stopped making rental payments in July of 1997<sup>1</sup> and Morton became liable for those missed rent payments. Morton sued for indemnification by Charest and Corsica. Corsica responded that the assignment and sublease were fraudulently induced and therefore, payments under the indemnification agreement were not due. Charest filed for bankruptcy, and was discharged in September of 1998; therefore, any potential liability under this suit has been discharged with respect to him. Plaintiff has filed a motion for summary judgment against Corsica.<sup>2</sup>

At the time the restaurant lease was assigned, Corsica had been in the restaurant

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<sup>1</sup> Corsica's restaurant on the premises continued in operation until May 13, 1998.

<sup>2</sup> Plaintiff is suing for past due rent totaling \$224,807.36 plus interest. The past due rent includes: \$13,333.33 monthly rent for the restaurant premises plus \$905.60 in common area maintenance fees due on the first of each month from July 1997 to October 1997; \$14,583.33 monthly rent for the restaurant premises plus \$905.60 in common area maintenance fees due on the first of each month from November 1997 to June 1998; back rent of \$2,500; increased taxes of \$1,811.26; and \$3,048.38 monthly rent for the restaurant equipment due on the first of each month from June 1997 to June 1998.

business for 7 years. See Answer, Amended Affirmative Defenses and Amended Counterclaim to Complaint [hereinafter “Answer”] ¶ 34. Corsica was represented during the lease negotiations. See Defendants' Response to Plaintiff's First Set of Interrogatories to Defendant, 1(a) (Exh. C to Plaintiff's Motion for Summ. J.). Corsica acknowledged in its answer that the restaurant was being relocated to 1500 Locust Street due to problems at its previous location caused by construction. See Answer ¶ 34. Yet Corsica does not allege that it asked plaintiff about the possibility of construction outside the premises at 1500 Locust Street. In defendants' answers to plaintiff's interrogatories, Corsica states that Charest, Corsica's sole shareholder, told plaintiff's agent, Tom Baldwin, of previous problems with construction. See Defendants' Response to Plaintiff's First Set of Interrogatories to Defendant, 2(a), (Exh. C to Plaintiff's Motion for Summ. J.).

In its answer, Corsica claimed that plaintiff acted fraudulently by failing to tell defendant about the impending construction at the new restaurant site. See Answer ¶ 44. Further, Corsica claims that due to this fraud, plaintiff is estopped from enforcing the indemnification agreement. See Answer ¶ 45. Corsica claims that due to the fraud, it is entitled to an offset equal to lost gross receipts if plaintiff is awarded anything on its claim. See Answer ¶ 46.

Corsica also counterclaimed that plaintiff was liable to it for damages caused to the business as a result of plaintiff's fraud. See Answer ¶¶ 48-49. As a result of Corsica's failure to comply with an order to compel production, this court precluded Corsica from

introducing any evidence in support of its counterclaim filed in this action as a sanction.<sup>3</sup>

See Order, 8-20-98.

As of July 16, 1998, Reed Smith Shaw & McClay, counsel for both Charest and Corsica, withdrew its appearance. No new counsel has since entered an appearance for Corsica, and the defendant has not filed any response to the motion for summary judgment.

## II. **STANDARD FOR SUMMARY JUDGMENT**

Either party to a lawsuit may file a motion for summary judgment and it will be granted “if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to judgment as a matter of law.” Fed. R. Civ. P. 56(c). Where the nonmovant bears the burden of persuasion at trial, the moving party may meet its burden “by 'showing'-- that is, pointing out to the district court-- that there is an absence of evidence to support the nonmoving party's case.” Celotex Corp. v. Catrett, 477 U.S. 317, 325 (1986). Thus, summary judgment will be entered “against a party who fails to make a showing sufficient to establish an element essential to that party's case, and on which that party will bear the burden of proof at trial.” Id. at 322.

When a court evaluates a motion for summary judgment, “the evidence of the nonmovant is to be believed.” Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 255

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<sup>3</sup> Thus, Corsica is unable to substantiate its counterclaim and the counterclaim will be dismissed.

(1986). Additionally, “all justifiable inferences are to be drawn in [the nonmovant's] favor.” Id. Although “the movant has the burden of showing that there is no genuine issue of fact, . . . [the nonmovant] is not thereby relieved of his own burden of producing evidence that would support a jury verdict.” Id. at 256. The pleadings alone are not sufficient to oppose a “properly supported motion for summary judgment . . . .” Id. Furthermore, the nonmovant must show more than “the mere existence of a scintilla of evidence” for elements on which he bears the burden of production. Id. at 252. Thus, “[w]here the record taken as a whole could not lead a rational trier of fact to find for the nonmoving party, there is no 'genuine issue for trial.’” Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 587 (1986).

Plaintiff filed the instant motion for summary judgment accompanied by the relevant leases, indemnification agreements and guarantees. Defendant acknowledged in its answer that these documents are accurate copies of the executed contracts. See Answer ¶ 39. Defendant did not respond to the motion for summary judgment and has filed no affidavits or any other type of evidence in support of its affirmative defense of fraud. Defendant would bear the burden of production at trial for its affirmative defense of fraud. See Harper v. Delaware Valley Broadcasters, Inc., 743 F. Supp. 1076, 1090-91 (D. Del. 1990) (“A party resisting summary judgment cannot expect to rely on the bare assertions or mere cataloguing of affirmative defenses. . . . The requirement of pointing to specific facts to defeat a summary judgment motion is especially strong when the

nonmoving party would bear the burden of proof at trial . . .”), aff'd, 932 F.2d 959 (3d Cir. 1991). Although there is some evidence before the court that plaintiff knew of the planned construction, there is no evidence that plaintiff actively concealed the construction plans from defendant. Rather, the best inference for defendant that can be drawn from the evidence before the court is that plaintiff failed to disclose its knowledge of the planned construction. There has been no evidence, however, that plaintiff had a duty to disclose; therefore, nondisclosure of such information would not constitute fraud. See Section IV, infra, for discussion of fraud.

### III. LIABILITY UNDER THE INDEMNIFICATION AGREEMENT

Plaintiff's subsidiary, Peasant, assigned the lease for the restaurant premises to Corsica. See Assignment and Agreement (Exh. E to Plaintiff's Motion for Summ. J.). Plaintiff's subsidiary, Peasant, also subleased the restaurant equipment to Corsica. See Sublease Agreement (Exh. F to Plaintiff's Motion for Summ. J.). Under these contracts, Corsica was responsible for paying the full rent for the premises as of December 16, 1996 and paying half of the rent due for the equipment as of October 16, 1998. See Assignment and Agreement ¶¶ 3 & 4 (Exh. E to Plaintiff's Motion for Summ. J.) & Sublease ¶ 3(a) & (b) (Exh. F to Plaintiff's Motion for Summ. J.). The term for the sublease of the equipment expires on December 31, 1998. See Sublease Agreement ¶ 2(a) (Exh. F to Plaintiff's Motion for Summ. J.). Under the assignment, Corsica assumed the full lease of the premises, which extends to August 28, 2009. See Assignment and

Agreement ¶ 12(a)(ii).

Plaintiff had guaranteed both leases, when the premises and equipment were originally leased by Peasant. See Guarantee and Suretyship Agreement (Exh. B to Plaintiff's Motion for Summ. J.) and Corporate Guaranty (Exh. D to Plaintiff's Motion for Summ. J.). Thus, plaintiff was liable under these agreements for any missed payments under either lease. See id. This guarantee was reaffirmed on November 16, 1996, in conjunction with the assignment and sublease. See Reaffirmation of Guaranty (Exh. G to Plaintiff's Motion for Summ. J.). Plaintiff and Corsica entered into an indemnification agreement whereby if plaintiff had to pay anything under the guarantees, due to a default by Corsica, plaintiff would be indemnified by Corsica. See Indemnity Agreement (Exh. H to Plaintiff's Motion for Summ. J.). The only exceptions stated in the contract were if the obligation which Corsica failed to pay arose due to an act or omission by Peasant or due to a condition existing at the premises prior to October 16, 1998. See id. ¶ 2. Corsica has not claimed that either of these exceptions occurred. Instead, Corsica claims that plaintiff fraudulently induced defendant to enter into the contract. If no fraud occurred, Corsica is liable to plaintiff under the indemnification agreement for the past due rent and the costs of the lawsuit, including attorney's fees.<sup>4</sup> See id. ¶¶ 2 & 14.

#### IV. FRAUD UNDER PENNSYLVANIA LAW

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<sup>4</sup> Counsel for Morton has advised the court that Morton will not be pursuing its claim for attorney's fees in this lawsuit. See Letter from Edward Swichar, Esq., Blank Rome Comisky & McCauley LLP, to the Honorable William H. Yohn, Jr. (Oct. 28, 1998).

In a diversity case, a federal court will apply state law to all issues of substantive law. Erie R.R. v. Tompkins, 304 U.S. 64, 78-79 (1938). This case is governed by Pennsylvania law. Under Pennsylvania law, fraud must be proved by clear and convincing evidence. See Wittekamp v. Gulf & Western, Inc., 991 F.2d 1137, 1142 (3d Cir.) (applying Pennsylvania law), cert. denied, 510 U.S. 917 (1993). Fraud consists of the following five elements:

(1) a false representation of an existing fact or a nonprivileged failure to disclose; (2) materiality, unless the misrepresentation is intentional or involves a nonprivileged failure to disclose; (3) scienter, which may be actual knowledge or reckless indifference to the truth; (4) justifiable reliance on the misrepresentation, so that the exercise of common prudence or diligence could not have ascertained the truth; and (5) damage to him as a proximate result.

Id.

In Pennsylvania, whether a party has an affirmative duty to disclose information to another party to a transaction, which is called a “duty to speak,” depends “on the nature of the contract between the parties and the scope of one party's reliance on the other's representations.” Duquesne Light Co. v. Westinghouse Elec. Corp., 66 F.3d 604, 612 (3d Cir. 1995) (applying Pennsylvania law). If no duty to speak exists, an omission will not be actionable as fraud. See id. A duty to speak would arise if there was a fiduciary relationship between the parties. See id. A duty to speak could also arise in a non-fiduciary relationship under reliance principles due to a special relationship. See id. Where there is no fiduciary relationship, disclosure by a seller is also required when it is the only reasonable way a buyer could find out about a serious latent defect (not at issue

here). See id. In an arm's length transaction between experienced business entities, however, it is extremely unlikely that such a duty will arise. See id. The seller has a duty to disclose “[i]n those circumstances [in which] it cannot be said fairly that by failing to disclose the seller is legitimately enhancing his or her bargain.” Duquesne, 66 F.3d at 612. The seller can, however, use any legitimate advantages, such as extensive business knowledge or effective due diligence, without any liability. Id. Further, the cases in Pennsylvania imposing a duty to speak almost never deal with cases where both parties were “sophisticated business entities, entrusted with equal knowledge of the facts.” Id.

If a confidential relationship between the parties to a transaction exists and “the party in whom the confidence is reposed obtains an apparent advantage over the other, he is presumed to have obtained that advantage fraudulently.” Matter of Estate of Evasew, 584 A.2d 910, 912-13 (Pa. 1990). Thus, the existence of a confidential relationship operates to shift the burden of disproving fraud to the party who allegedly acted fraudulently. See id. A confidential relationship exists where there is a fiduciary relationship or where one party has such influence over the other that he has the power to take advantage of the other party. See id. at 913. A confidential relationship did not exist between Morton and Corsica.

Even where a legal finding of a confidential relationship is not justified, however, there may still be a heightened responsibility based on the dealings of the parties. In Scaife Co. v. Rockwell-Standard Corp., 285 A.2d 451, 455-56 (Pa. 1971), cert. denied,

407 U.S. 920 (1972), long negotiations to acquire a business division, coupled with long established strong business and personal relationships among the corporations' executives were insufficient to create a confidential relationship, but were enough “to justify a factual finding that [plaintiff] reposed a specific confidence in [defendant] which was knowingly abused by [defendant].” Thus, the Pennsylvania Supreme Court quoted approvingly the trial court's charge to the jury:

there are cases where a party must not be silent upon a material fact within his knowledge although he stands in no relation of trust and confidence. . . . If a party knows that another is relying upon his judgment and knowledge in contracting with him, although no confidential relation exists . . . and he does not state material facts within his knowledge, the contract will be avoided; for knowingly to permit another to act as though the action was confidential, and yet not state material facts, is fraudulent.

Id. (citing Zahn v. McMillin, 36 A. 188, 189-90 (1897)). The court also noted, however, that “[a] misrepresentation as to the subject of a proposed sale will not support an action for deceit if the subject be open to the buyer's observation.” Id. at 455 (quoting Emery v. Third National Bank, 162 A. 281 (1932)). Thus, one may justifiably rely on silence where there is no confidential relationship only if a specific relationship of trust has been developed with regard to a certain matter. Additionally, in Scaife, as in other fraudulent misrepresentation cases, the alleged misrepresentation related to the subject matter of the transaction, not action about to be taken by a third party on adjoining property. Just as no confidential relationship exists here, there appear to be no facts to justify a finding of

such a heightened relationship of trust; Morton and Corsica were both represented by counsel and were engaged in arm's length negotiations. Thus, there was no duty to speak and, therefore, no fraud.

The Third Circuit held that Pennsylvania has adopted the duty to speak requirement, but the Third Circuit also stated that it was unclear whether Pennsylvania had adopted the entirety of section 551 of the Restatement of Torts, which deals with liability for nondisclosure. Duquesne, 66 F.3d at 612-13. If Pennsylvania has adopted section 551, there is an additional possible basis for Corsica's claim of fraud. Under section 551(2)(e), there is liability when a statement will be misleading without additional disclosure; or, when, due to additional information, it becomes apparent that a previous statement was false; or, for nondisclosure of “facts basic to the transaction . . . .” Restatement (Second) of Torts § 551(2)(e) (1977).

Only the third situation has potential applicability here. Although it is not clear whether Pennsylvania law requires disclosure of facts basic to the transaction, even if it does, the proposed construction outside the restaurant does not fall within the Restatement's definition of what a fact basic to the transaction is. According to the Restatement, a fact is basic to the transaction when it “goes to the basis, or essence, of the transaction, and is an important part of the substance of what is bargained for . . . .” Id. cmt. j. A fact could be material and yet not be a fact basic to the transaction. See id. To illustrate this, the Restatement compares the sale of a termite infested house, where the

infestation would be a basic fact, to the sale of a house where the buyer believes that a highway will soon be built nearby thus increasing the value, and where even though the seller knows that the buyer thinks this and that it is untrue, it is not a basic fact. See id. cmt. j., illus. 3 & 4. The distinction rests on the assumption that in an arm's length transaction, both sides must do their own due diligence and that while the termite infestation is latent and may not be discoverable, external facts are equally discoverable by either party. See id. cmt. k. The proposed construction next to the restaurant is more like the proposed highway than a termite infestation, and thus is not a fact basic to the transaction. Therefore, even under section 551, no fraud occurred.

The problem alleged with the property at issue here is that construction was about to begin on the sidewalk outside the restaurant. Morton was not about to begin the construction; instead, a third party, the Delaware River Port Authority was. Viewing the evidence in the light most favorable to the defendant, I will assume that Morton knew about the impending construction. See Letter from Robert A. Box, Director of Engineering, Delaware River Port Authority, to Dino Cataldi, Napoleon's Bar and Restaurant (Aug. 26, 1997) (Exh. E to Plaintiff's Motion for Summ. J.).

Corsica has not alleged that it asked plaintiff about any impending construction. Instead, Corsica claims that it had told plaintiff that Corsica was relocating its restaurant due to a business slowdown caused by construction and that plaintiff therefore should have been aware that Corsica would want to know about any planned construction. See

Defendants' Response to Plaintiff's First Set of Interrogatories to Defendant, 2(a) (Exh. C to Plaintiff's Motion for Summ. J.). Thus, there is not an allegation that Morton made any affirmative misrepresentation regarding the construction.

Further, Corsica has not alleged that plaintiff prevented Corsica from finding out about the construction. Corsica in an answer to an interrogatory claimed that plaintiff had told its employees not to tell any potential renters about the proposed construction. See Defendants' Response to Plaintiff's First Set of Interrogatories to Defendant, 6(c), (Exh. C to Plaintiff's Motion for Summ. J.). This allegation, even if true, does not demonstrate fraud. Unless Corsica asked and was given misleading information about impending construction, failure to inform is only an omission and not actionable as fraud, absent a duty to disclose. No confidential relationship existed here, and there has been no allegation of facts sufficient to arise to a level of a Scaife special relationship of trust. Even if a Scaife special relationship of trust existed, the duty to disclose would only run to a material fact regarding which plaintiff knew that defendant was relying on plaintiff for disclosure. Corsica has not alleged that the only way it could find out about the construction was through plaintiff. Construction on city sidewalks is a fairly routine event and even if the easiest source of the information was the plaintiff, plaintiff was not under a duty to disclose.

## V. CONCLUSION

Corsica's only defense to enforcement of the indemnification agreement is that

plaintiff fraudulently induced it to enter into the transaction by falling to disclose the proposed construction. Corsica has not established that plaintiff actively concealed information about the proposed construction. Drawing all inferences in favor of defendant, the nonmoving party, the most that can be said is that plaintiff may have failed to disclose the proposed construction. Because no duty to disclose this information was present, I grant the plaintiff's motion for summary judgment. An appropriate order follows.