

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

WMI INVESTORS, INC.

v.

WASTEMASTERS, INC. et al.

CIVIL ACTION

NO. 98-3187

M E M O R A N D U M

Broderick, J.

April 8, 1999

Plaintiff WMI Investors, Inc. ("WMI" or "Plaintiff") originally filed this action in the Court of Common Pleas of Philadelphia County against WasteMasters, Inc. ("WasteMasters"), Continental Technologies Corporation of Georgia, Inc. ("Continental"), and the individual defendants A. Leon Blaser ("Blaser"), Richard D. Masters ("Masters"), Robert P. Crabb ("Crabb"), Julius Basham, II ("Basham"), Paul G. Williamson ("Williamson"), Robert Fahey ("Fahey"), and R. Dale Sterritt, Jr. ("Sterritt"), all of whom were directors of WasteMasters or Continental at the time the instant action arose (collectively "Defendants"). Defendant Masters is now deceased. Defendants removed this action to the United States District Court for the Eastern District of Pennsylvania on June 19, 1998 pursuant to 28 U.S.C. §§ 1441-1452. Thereafter, Plaintiff filed an amended complaint, entitled "First Amended Complaint" which contains the following counts: breach of contract, common law fraud, conspiracy to defraud, theft by deception, negligent misrepresentation, tortious interference with a contractual

relationship, "vicarious liability," "negligent supervision," "pierce corporate veil," "J,S,I." Plaintiff claims that it had a contract with WasteMasters for Plaintiff to provide WasteMasters with a line of credit up to \$1,000,000 in exchange for a warrant to purchase 49% of WasteMasters common stock at a fixed price and 100,000 shares of preferred stock. Am. Compl. at ¶¶ 12-16. Plaintiff alleges that this contract was breached and, rather than selling the stock to Plaintiff, WasteMasters sold a majority interest in the company to Continental. Plaintiff seeks damages, under both tort and contract theories, in the amount of \$72,760,263 for the appreciation Plaintiff would have realized on the stock purchase described in the contract plus interest, costs and attorney's fees.

Defendants, prior to filing an answer, filed a motion to dismiss all counts of Plaintiff's amended complaint except Count I, alleging breach of contract, for failure to state a claim upon which relief can be granted pursuant to Fed. R. Civ. P. 12(b)(6). After Plaintiff responded to that motion, but before the Court issued a ruling, counsel for all Defendants filed a motion to withdraw. This Court held a hearing on December 18, 1998 on the motion of Defendants' counsel to withdraw to give the defendants an opportunity to show cause why the motion should not be granted. Defendants did not respond to the motion of their counsel to withdraw or attend the hearing. Therefore, this Court, by Order dated December 18, 1998, granted the motion to

withdraw filed by defense counsel. By the same Order, this Court directed all Defendants to have an attorney enter an appearance in this matter on or before January 18, 1999 or, in the case of the individual Defendants, to notify the Court by that date of their intention to proceed in this matter pro se. None of the defendants responded to this Court's Order and no attorney entered an appearance on any Defendants' behalf by the date specified.

Thereafter, by Order dated January 29, 1999, this Court granted in part and denied in part Defendants' motion to dismiss several counts of Plaintiff's amended complaint. The Court dismissed Counts IX, VII, and XI of Plaintiff's amended complaint but permitted Plaintiff to proceed on all other counts. By this same Order, the Court directed Defendants to file an answer to the remaining counts of Plaintiff's amended complaint on or before February 12, 1999. Defendants did not respond to this Order and no answer was filed by any Defendant. Therefore, Plaintiff sought entry of default and default judgment against all Defendants, except Robert P. Crabb. A default was entered by the Clerk of Court against all Defendants except Robert P. Crabb on February 25, 1999. Default judgment was not entered.

After the default was entered, this Court Ordered that a hearing be held for the purpose of assessing damages on March 19, 1999. The Court directed Plaintiff to serve a copy of this March

3, 1999 Order on all Defendants. On March 15, 1999 an attorney entered his appearance on behalf of all Defendants in this matter. The following day, Defendants, through counsel, filed a motion to continue the damages hearing and a separate motion to set aside entry of the default pursuant to Federal Rule of Civil Procedure 55(c). The Court granted Defendants' motion to continue the damages hearing pending resolution of the motion to set aside entry of default by Order dated March 16, 1999. Defendants' motion to set aside entry of default and Plaintiff's response thereto are currently before the Court. For the reasons stated below, Defendants' motion to set aside entry of default will be granted and Defendants' shall be permitted to file an answer to the remaining counts of Plaintiff's amended complaint on or before April 12, 1999.

The Federal Rules of Civil Procedure provide: "For good cause shown the court may set aside entry of default and, if a judgment by default has been entered, may likewise set it aside in accordance with Rule 60(b)." Fed. R. Civ. P. 55(c). No default judgment has been entered in this case. The decision whether or not to set aside the entry of a default is in the discretion of the trial court. See, e.g., United States v. \$55,518.05 in U.S. Currency, 728 F.2d 192, 194 (3d Cir. 1984); Mike Rosen & Assoc., P.C. v. Omega Builders, 940 F. Supp. 115, 117 (E.D.Pa. 1996). However, defaults are disfavored so "in a

close case doubts should be resolved in favor of setting aside the default and reaching a decision on the merits." Gross v. Stereo Component Sys., Inc., 700 F.2d 120, 122 (3d Cir. 1983). In ruling on a motion to set aside a default, the Court must consider the following three factors: "(1) whether the plaintiff will be prejudiced; (2) whether the defendant has a meritorious defense; (3) whether the default was the result of the defendant's culpable conduct." United States v. \$55,518.05 in U.S. Currency, 728 F.2d 192, 195 (3d Cir. 1984). The Court will address each of these factors in turn.

First, as to the prejudice to the Plaintiff in setting aside the default, the Court has determined that no prejudice will result to Plaintiff. Factors to be considered in determining whether or not the plaintiff will be prejudiced from the setting aside of the default include the loss of available evidence, the increased potential for fraud, and plaintiff's substantial reliance. See Feliciano v. Reliant Tooling Co., Ltd., 691 F.2d 653, 657 (3d Cir. 1982). Defendants sought to have the default set aside less than three weeks after it was entered. Therefore, it is unlikely that evidence has been lost and Plaintiff has made no such allegation. Nor has Plaintiff alleged that there is a greater likelihood of fraud caused by Defendants delay in responding. The Court does not believe that Plaintiff has relied on the default to its detriment because no default judgment had

yet been entered. At most, Plaintiff's detriment was the time spent in preparing for the hearing which was scheduled to be held on damages and the time spent in responding to Defendants' motion to set aside entry of the default. This is not sufficient to constitute prejudice to Plaintiff in setting aside the default. Nor is the fact that Plaintiff will now have to litigate this action on the merits rather than proceeding by default. See Duncan v. Speech, 162 F.R.D. 43, 45 (E.D.Pa. 1995).

Second, as to the existence of a meritorious defense, the Court finds that Defendants, through affidavits attached to their motion to set aside the entry of default, have demonstrated that they have a meritorious defense to Plaintiff's claims. "The showing of a meritorious defense is accomplished when 'allegations of defendant's answer, if established on trial, would constitute a complete defense to the action.'" United States v. \$55,518.05 in U.S. Currency, 728 F.2d 192, 195 (3d Cir. 1984) (quoting Tozer v. Charles A. Krause Milling Co., 189 F.2d 242, 244 (3d Cir. 1951)). The defendants in their motion and in their proposed answer assert several defenses which, if proved, would be defenses to Plaintiff's claims. Among these, Defendants assert that no valid contract ever existed among the parties. Defendants also deny all Plaintiff's claims of tortious conduct by any of the defendants. Although this is not the time for the Court to determine the relative merits of the parties' claims,

the Court has determined that Defendants have sufficiently responded to Plaintiff's claims to demonstrate that they have a meritorious, non-frivolous defense.

Third, as to whether or not the default was the result of culpable conduct by the defendants, the Court has found, based upon the affidavits submitted by Defendants, that, although Defendants' course of conduct in this litigation has been dilatory up to this point, the defendants lack of response does not appear to have been the result of bad faith. The Court notes that the individual Defendants in this action are officers and/or directors of the corporate Defendants. The Court accepts the assertions contained in affidavits filed by Defendants that these individual Defendants relied on the corporate Defendants to defend this action and had no knowledge that such a defense was not being pursued. As to the corporate Defendants, the affidavits filed by Defendants, which are not contradicted by any evidence from Plaintiff, establish that Defendants in good faith believed as of December, 1998 that a settlement of this action had been reached with Plaintiff which would be finalized as soon the language of the settlement agreement was resolved. The affidavits, again without contradiction, also establish that the corporate Defendants, during the period of their dilatoriness in responding to this Court's Orders, were in a period of considerable corporate turmoil which included moving offices, an

involuntary petition in bankruptcy being filed against WasteMasters by its creditors, and even litigation in another court to determine the proper directors of Continental. In light of this evidence and in the absence of contrary evidence presented by Plaintiff, the Court determines that Defendants lack of response was not undertaken in bad faith and the entry of the default was not the result of culpable conduct by Defendants.

Having found that all three of the factors weigh in favor of setting aside the default, the Court will Order the default set aside and permit Defendants to answer. Although no default was entered against Crabb, he shall be permitted to file an answer along with the other Defendants as he has joined in Defendants request to do so.

An appropriate Order follows.

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

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v.	:	
	:	
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O R D E R

AND NOW, this 8th day of April, 1999; default having been entered by the Clerk of the Court against all Defendants except Robert P. Crabb; Defendants having filed a motion to set aside the default; Defendants also seeking leave of Court to file an answer; Plaintiff having filed a response thereto; for the reasons stated in this Court's Memorandum of April 8, 1999, this Court having determined that good cause exists to set aside the default pursuant to Federal Rule of Civil Procedure 55(c);

IT IS ORDERED that Defendants' motion to set aside the default (Document No. 18) is **GRANTED**;

IT IS FURTHER ORDERED that the defaults entered against WasteMasters, Inc., Continental Technologies Corporation of Georgia, Inc., A. Leon Blaser, Richard D. Masters, Julius Basham, II, Paul G. Williamson, Robert Fahey, and R. Dale Sterritt, Jr. be set aside;

IT IS FURTHER ORDERED that Defendants shall execute and file an answer to Plaintiff's amended complaint on or before **April 12, 1999.**

RAYMOND J. BRODERICK, J.