

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

OHIO CASUALTY INSURANCE CO. : CIVIL ACTION  
: :  
v. : :  
: :  
THE SOUTHLAND CORPORATION, :  
AMERICAN MOTORISTS INSURANCE :  
and DALLER, GREENBERG & :  
DIETRICH, L.L.P. : NO. 98-CV-6187

**MEMORANDUM AND ORDER**

**J. M. KELLY, J.**

**APRIL 21, 1999**

Presently before the Court is Defendant Edward A. Greenberg and Daller, Greenberg & Dietrich, L.L.P.'s ("Greenberg") Motion to Dismiss; Defendant American Motorists Insurance Company's ("AMICO") Motion to Dismiss or, in the Alternative, for Summary Judgment; Defendant The Southland Corporation's ("Southland") Motion to Stay Pending Arbitration; and Plaintiff Ohio Casualty Insurance Corporation's ("Ohio Casualty") responses thereto. For the reasons that follow, Greenberg's and AMICO's motions to dismiss are denied. Southland's motion is granted.

**I. FACTUAL BACKGROUND**

Southland entered into a franchise agreement with Philip Mattie in January 1987. Among this agreement's various provisions are two relevant to Southland's motion, one that addresses arbitration and another that concerns choice of law. The arbitration provision states:

Any controversy relating to this Agreement which the parties cannot mutually resolve (including tort as well as contract claims, claims based upon any federal, state, or local statute, law, order, ordinance, or regulations, and claims arising from any relationship

prior to, at the time of entering, during the term, or upon or after expiration or termination of this Agreement) shall be settled by individual arbitration in accordance with the rules of the American Arbitration Association . . . .

(Store Franchise Agreement (“Agreement”) ¶ 31.) That provision also specifically prohibits the arbitrator from awarding punitive damages. Id. The choice-of-law provision provides in relevant part:

This Agreement shall be governed by and construed according to the laws of the state where the Store is located. If, however, any provision, or portion hereof in any way contravenes the laws of any state or jurisdiction where this Agreement is to be performed, such provision, or portion thereof, shall be deemed to be modified to the extent necessary to conform to such laws, and still be consistent with the parties’ intent as evidenced herein, or if such modification is impossible, to be deleted herefrom.

Id. ¶ 32.

Southland and Mattie were sued in February 1996 by Gerald and Donna Schaffer, who alleged Mr. Schaffer was injured after he tripped over plastic newspaper bands in Mattie’s store. Southland’s insurance company, AMICO, retained the same counsel, Defendant Greenberg of the firm Daller, Greenberg & Dietrich, L.L.P., for Southland’s and Mattie’s defense. The case eventually proceeded to trial, where the jury found the defendants liable to the Schaffers for \$2.3 million dollars. The trial court then dismissed the case against Southland, but Mattie was not so fortunate, and was left solely responsible for the judgment. The Schaffers settled their case against Mattie for \$1.45 million, with Southland contributing \$500,000.00 pursuant to an indemnity agreement with Mattie and Mattie’s excess insurance carrier, Plaintiff Ohio Casualty, contributing the balance. Plaintiff has brought this action as Mr. Mattie’s subrogee.

Greenberg moves to dismiss Plaintiff’s claim against him and his firm on the theory that Plaintiff, as Mattie’s subrogee, lacks the privity necessary to maintain a legal malpractice claim.

Plaintiff likens its rights to those of an assignee, which Pennsylvania courts allow to bring legal malpractice actions. AMICO moves to dismiss Plaintiff's claim because it claims Mattie was not insured, and therefore it owed him no duty that Plaintiff can assume in this subrogation action. Plaintiff counters that its claims against AMICO do not rest on Mattie being AMICO's insured, but that in any event Mattie was an insured under AMICO's policy.

Southland moves to stay this suit pending arbitration in reliance on the Agreement's arbitration provision. Plaintiff claims arbitration is inappropriate for essentially two reasons. First, Plaintiff notes that it has brought a claim under Pennsylvania's bad faith statute, 42 Pa. Cons. Stat. Ann. § 8371, and argues because the Agreement precedes the enactment of this statute, the parties could not have intended to submit this claim to arbitration. Second, Plaintiff asserts the Agreement's choice-of-law provision reflects an intention by the parties to have state law applied wherever it conflicts with arbitration, and because arbitration conflicts with certain elements of the bad faith statute, the Court should decline to send the case to arbitration.

## **II. DISCUSSION**

### **A. Greenberg's and AMICO's Motions to Dismiss**

#### **1. The Rule 12(b)(6) Standard**

Greenberg and AMICO move to dismiss the claims against them under Federal Rule of Civil Procedure 12(b)(6), and the Court, in resolving these motions, must consider only those facts alleged in the complaint and must accept those facts as true. Hishon v. King & Spalding, 467 U.S. 69, 73 (1984). Moreover, the Court will view the complaint in the light most favorable to Plaintiff. Tunnell v. Wiley, 514 F.2d 971, 975 n.6 (3d Cir. 1975). Only if Plaintiff can prove no set of facts that would entitle it to relief will the Court grant either motion to dismiss. See

Conley v. Gibson, 355 U.S. 41, 45-46 (1957); see also Fries v. Helsper, 146 F.3d 452, 457 (7th Cir.) (“At a minimum, a complaint must contain facts sufficient to state a claim as a matter of law . . . .”), cert. denied, 119 S. Ct. 337 (1998).

## 2. Greenberg’s Motion to Dismiss

Subrogation is the equitable doctrine under which one party, the subrogee, is placed in the position of another. Johnson v. Beane, 664 A.2d 96, 100 (Pa. 1995). In that position the subrogee assumes those rights the subrogor possessed. Id. This equitable doctrine, however, has limits: the subrogation of another’s rights is not permitted when public policy or a statute stands in the way. Michael v. City of Bethlehem, 478 A.2d 164, 166 (Pa. Commw. Ct. 1984).

Courts of many states, including Pennsylvania, recently have encountered these limitations on subrogation when addressing whether parties may assign legal malpractice claims. The majority of jurisdictions have followed the reasoning stated in Goodley v. Wank & Wank, Inc., 133 Cal. Rptr. 83 (Cal Ct. App. 1976), in which the California Court of Appeal held the personal nature and confidentiality of the attorney-client relationship were public policies that counseled against allowing the assignment of legal malpractice claims, id. at 87. See, e.g., Roberts v. Holland & Hart, 857 P.2d 492, 495-96 (Col. Ct. App. 1993) (relying on Goodley as support for holding assignments of legal malpractice claims are against public policy); Picadilly, Inc. v. Raikos, 582 N.E.2d 338, 339, 341-42 (Ind. 1991) (same); Wagener v. McDonald, 509 N.W.2d 188, 191 (Minn. Ct. App. 1993) (same); White v. Auto Club Inter-Ins. Exch., 984 S.W.2d 156, 160-61 (Mo. Ct. App. 1998) (same); Can Do, Inc. Pension & Profit Sharing Plan & Successor Plans v. Manier, Herod, Hollabaugh & Smith, 922 S.W.2d 865, 868-69 (Tenn.) (same), cert. denied, 117 S. Ct. 298 (1996); Zuniga v. Groce, Locke & Hebdon, 878 S.W.2d. 313,

316-17 (Tex. App. 1994) (same), writ ref'd; MNC Credit Corp. v. Sickels, 497 S.E.2d 331, 333-34 (Va. 1998) (same). Pennsylvania, however, has not followed the lead of the court in Goodley. Rather, the Pennsylvania Supreme Court explicitly rejected the policies embraced in Goodley in favor of requiring attorneys to answer for the injuries their representation causes. Hedlund Mfg. Co. v. Weiser, Stapler & Spivak, 539 A.2d 357, 359 (Pa. 1988). The court therefore held the assignment of legal malpractice claims was permissible. Id.

The Court predicts the Pennsylvania Supreme Court will extend the reasoning it stated in Hedlund to subrogation cases, and the Court accordingly will deny Greenberg's motion to dismiss. Greenberg insists privity still is required to maintain a legal malpractice action and that the absence of privity acts as a bar to Plaintiff's claim. While privity generally may continue to be a requirement, the court in Hedlund's reasoning, as well as that from other Pennsylvania courts, should permit a subrogee to maintain an action for legal malpractice. First, the court in Hedlund found privity is not an issue in cases involving assignment because the assignee merely stands in the shoes of the assignor, and does not pursue its own cause of action. Id. at 358 (citing Gray v. Nationwide Mut. Ins. Co., 223 A.2d 8, 9 (Pa. 1966)). A subrogee, too, stands in the shoes of the subrogor, and exercises only the rights it inherited from the subrogor. Holloran v. Larrieu, 637 A.2d 317, 322 (Pa. Super. Ct. 1994). By extension, privity is not an issue in subrogation cases. Second, the court in Hedlund removed any public policy obstacle to allowing the subrogation of legal malpractice claims when it elevated the policy of protecting clients' rights over the policy of protecting the personal and confidential nature of the attorney-client relationship. Hedlund, 539 A.2d at 359 ("We will not allow the concept of the attorney-client relationship to be used as a shield by an attorney to protect him or her from the consequences of

legal malpractice.”); see also DiMarco v. Lynch Homes -- Chester County, Inc., 583 A.2d 422, 425 n.1 (Pa. 1990) (“[W]hen those policies pale in comparison to the harm at issue, this Court has not hesitated to find that lack of privity does not bar a third party from maintaining a cause of action against a professional.”). Because subrogation is permitted in Pennsylvania when it does not violate public policy or a statute, Michael, 478 A.2d at 166, the subrogation of Mr. Mattie’s malpractice claim is appropriate here. Finally, Pennsylvania courts traditionally have allowed subrogation where they have not allowed assignment. See Demmery v. National Union Fire Ins. Co., 232 A.2d 21, 25 (Pa. Super. Ct. 1967). Because assignment of legal malpractice claims is allowed, so too should be the subrogation of those claims. The Court therefore finds the privity requirement does not bar Plaintiff’s subrogation action as a matter of law, cf. National Union Ins. Co. v. Dowd & Dowd, P.C., 2 F. Supp. 2d 1013, 1027 (N.D. Ill. 1998) (predicting Illinois law); Allstate Ins. Co. v. American Transit Ins. Co., 977 F. Supp. 197, 201 (E.D.N.Y. 1997) (predicting New York law), and Greenberg’s motion to dismiss is denied.

### **3. AMICO’s Motion to Dismiss**

AMICO bases its motion to dismiss entirely upon the complaint and the insurance policy it issued to Southland. A court, when resolving a motion to dismiss, ordinarily may consider only those documents attached to the complaint. Fed. R. Civ. P. 10(c); Ala. Inc. v. Ccair, Inc., 29 F.3d 855, 859 (3d Cir. 1994). When, however, the defendant attaches a document on which the plaintiff bases its claims to a motion to dismiss, and when neither side disputes the authenticity of that document, a court may consider that document in its analysis. Pension Benefit Guar. Corp. v. White Consol. Indus., Inc., 998 F.2d 1192, 1196 (3d Cir. 1993), cert. denied, 510 U.S. 1042 (1994). Plaintiff, for the purposes of this motion, does not challenge the authenticity of the

policy to which AMICO refers, and so the Court will examine the policy in its treatment of AMICO's motion.

AMICO argues Mattie was not an insured under the policy, and urges the Court to dismiss those claims that depend upon an insurer-insured relationship. In support of its argument that Mattie is not an insured, AMICO points to the schedule on the policy's endorsement 3, which lists as insureds: "Any company, partnership, joint venture, or other organization (and any partner or member thereof as respect [sic] his / its liability as such) in which the named insured has [a] financial interest but does not exercise active managerial control; but only to the extent of the named insured's financial interest only [sic] . . . ." (Southland Ins. Policy, Endorse. 3 at C.) AMICO claims Mattie, who ran his franchise as a sole proprietor, is a mere individual who cannot be characterized as a "company, partnership, joint venture, or other organization" and therefore is not an insured under the policy. Plaintiff accordingly cannot maintain any of its causes of action, AMICO argues, because each one requires an insurer-insured relationship either upon explicit reliance on the contract or AMICO's alleged role as a fiduciary.

Plaintiff successfully rebuts AMICO's position primarily by seizing on AMICO's assumption of Mattie's defense. In reliance on Cowden v. Aetna Casualty & Surety Co., 134 A.2d 223 (Pa. 1957), Plaintiff argues that once AMICO took over Mattie's defense it obligated itself to defend Mattie in good faith, see id. at 228. While AMICO correctly points out that there was no issue in Cowden whether the plaintiff was Aetna's insured, see id. at 224, the Court still finds Plaintiff's argument persuasive, at least at this point in the litigation. Although AMICO claims it owes Mattie no duty because its relationship was with Southland, not Mattie, AMICO does not deny it assumed control of Mattie's defense. The Court will not rule that AMICO, as a

matter of law, had no obligation to carry out this defense in good faith and as Mattie's fiduciary. AMICO's motion to dismiss and motion for summary judgment are denied.

### **B. Southland's Motion to Stay the Proceedings Pending Arbitration**

A court presented with an agreement containing an arbitration provision performs a narrow function: the court must decide whether there was a valid agreement to arbitrate, and if a valid arbitration agreement exists, the court then must decide whether the dispute falls within the substantive scope of that agreement. AT&T Tech., Inc. v. Communications Workers, 475 U.S. 643, 648 (1986); Painewebber Inc. v. Hartmann, 921 F.2d 507, 511 (3d Cir. 1990). The court must leave all substantive issues for the arbitrator. AT&T, 475 U.S. at 650; Great W. Mortgage Corp. v. Peacock, 110 F.3d 222, 228 (3d Cir.), cert. denied, 118 S. Ct. 299 (1997). To accomplish its limited task, the court preliminarily will decide whether the agreement falls under the Federal Arbitration Act ("FAA"), 9 U.S.C. §§ 1-16 (1994). If the parties' written agreement contains a provision submitting disputes arising from the agreement to arbitration, and if the contract involves commerce, the FAA is applicable. See id. § 2. Further, the agreement is valid and enforceable under the FAA unless the party resisting arbitration can show it was induced to enter the contract through fraud, duress, or some other equitable or legal defense. Id.; Seus v. John Nuveen & Co., Inc., 146 F.3d 175, 183-84 (3d Cir. 1998), cert. denied, 119 S. Ct. 1028 (1999). Finally, the court will determine the scope of the arbitration agreement by reference to state law principles of contract formation. First Options of Chicago, Inc. v. Kaplan, 514 U.S. 938, 944 (1995). Accordingly, under Pennsylvania law, which is applicable here, (Agreement ¶ 32), the court will "ascertain the intent of the parties as manifested by the language of the written instrument," see Standard Venetian Blind Co. v. American Empire Ins. Co., 469 A.2d 563, 566

(Pa. 1983). Significantly, the court must resolve all doubts in favor of arbitration when interpreting an agreement covered by the FAA. Volt Info. Sciences, Inc. v. Board of Trustees, 489 U.S. 468, 475-76 (1989).

The parties' Agreement does not raise any doubts; the Court is convinced the Agreement contains an arbitration provision governed by the FAA, the provision is valid and enforceable, and this dispute falls within the scope of the arbitration provision. The Agreement involves commerce under the FAA, Allied-Bruce Terminix Cos. v. Dobson, 513 U.S. 265, 273-74 (1995) (holding the "commerce" required under the FAA must be as broadly construed as Congress's power under the Commerce Clause), and because Plaintiff has not alleged a legal or equitable defense to the Agreement, the Court finds it is valid. Further, this dispute falls within the scope of the Agreement's arbitration provision. The parties intended, as evidenced by the provision, to submit any controversy whatsoever to arbitration. To this end, the parties used expansive, all-encompassing language: "Any controversy . . . including tort as well as contract claims, claims based upon any federal, state, or local statute, law, order, ordinance, or regulation[] . . . shall be settled by individual arbitration . . . ." (Agreement ¶ 31.) The dispute at issue here plainly falls within the galactic scope of this provision. Cf. Mastrobuono, 514 U.S. at 61 n.7 (quoting Raytheon Co. v. Automated Bus. Sys., Inc., 882 F.2d 6, 10 (1st Cir. 1989)).

Contrary to Plaintiff's argument, legislation not enacted at the time of the Agreement also falls within scope of this provision. For Plaintiff to have prevailed, it must have shown something in the Agreement to allow the Court to find "with positive assurance" that the parties did not intend to arbitrate Plaintiff's bad faith claim. See United Steelworkers v. Warrior & Gulf Navig. Co., 363 U.S. 574, 582-83 (1960). Nothing in the arbitration provision restricts its

application to statutes already enacted; the provision contains no temporal qualifications.

Perhaps in recognition of this, Plaintiff claims the choice-of-law provision acts to limit the arbitration provision. Plaintiff argues the parties wanted Pennsylvania law to govern the Agreement and also agreed all provisions of the Agreement should be reconcilable with Pennsylvania law. Therefore, Plaintiff asserts, the Court should not enforce the arbitration provision because it restricts some remedies available under Pennsylvania's bad faith law, and Plaintiff believes Volt supports its position.

The holding in Volt, however, does not extend as far as Plaintiff would like, and the Court finds there is nothing in the Agreement that prevents the enforcement of the arbitration provision. First, the issue presented in Volt was not whether a choice-of-law provision could trump an arbitration provision, but which procedural rules the arbitrators should apply. Volt, 489 U.S. at 476, 479. Second, as the Court itself characterized it, its holding that California procedural rules were applicable demonstrates that just as parties may decide which issues, if any, they will agree to arbitrate, they also are free to choose the rules by which the arbitration will occur. See id. at 479. Volt, then, vigorously supports the notion that parties will be held to what they have contracted for. See Mastrobuono, 514 U.S. at 58 (reducing analysis of the interplay between the FAA and choice-of-law provisions to an analysis of the actual terms of the contract). Volt does not elevate one provision over another, and so the Court still must analyze the Agreement as a whole to determine the intent of the parties. Considering the Agreement as a whole, the Court does not believe the parties intended to scrap the arbitration provision in the manner suggested by Plaintiff. Moreover, even if Plaintiff's argument is colorable and the choice-of-law provision slightly undermines the application of the arbitration provision, which

the Court does not believe is the case here, that is not nearly enough to overcome the presumption in favor of arbitration. See id. at 62. Plaintiff has failed to convince the Court “with positive assurance” that the parties did not intend the arbitration provision would apply to this dispute, and the Court therefore will enforce the arbitration provision and stay the claims against Southland. Further, the Court will bifurcate this case to allow Plaintiff’s causes of action against Greenberg and AMICO to proceed. See Dean Witter Reynolds, Inc. v. Byrd, 470 U.S. 213, 217 (1985).

An Order follows.

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

OHIO CASUALTY INSURANCE CO. : CIVIL ACTION  
: :  
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: :  
THE SOUTHLAND CORPORATION, :  
AMERICAN MOTORISTS INSURANCE :  
and DALLER, GREENBERG & :  
DIETRICH, L.L.P. : NO. 98-CV-6187

**ORDER**

AND NOW, this 21st day of April, 1999, upon consideration of Defendant Edward A. Greenberg and Daller, Greenberg & Dietrich, L.L.P.'s ("Greenberg") Motion to Dismiss (Document No. 7); Defendant American Motorists Insurance Company's ("AMICO") Motion to Dismiss or, in the Alternative, for Summary Judgment (Document No. 9); and Defendant The Southland Corporation's ("Southland") Motion to Stay Pending Arbitration (Document No. 10); and Plaintiff Ohio Casualty Insurance Corporation's responses thereto, it is hereby **ORDERED**:

1. Defendant Edward A. Greenberg and Daller, Greenberg & Dietrich, L.L.P.'s Motion to Dismiss is **DENIED**;
2. Defendant American Motorists Insurance Company's Motion to Dismiss and, in the Alternative, for Summary Judgment are **DENIED**;
3. Defendant The Southland Corporation's Motion to Stay Pending Arbitration is **GRANTED**; and

4. This case is bifurcated to permit Plaintiff's claims against Edward A. Greenberg, Daller, Greenberg & Dietrich, L.L.P., and American Motorists Insurance Company to proceed.

BY THE COURT:

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JAMES McGIRR KELLY, J.