IN THE COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY
FIRST JUDICIAL DISTRICT OF PENNSYLVANIA
CIVIL TRIAL DIVISION

LA WEIGHT LOSS CENTERS, INC.,	:	December Term 2003
Plaintiff,	:	No. 1560
v.	:	
	:	
LEXINGTON INSURANCE COMPANY,	:	Commerce Program
Defendant.	:	Control Numbers 072109/072287

ORDER

AND NOW, this 1ST day of March, 2006, upon consideration of the Parties' Cross Motions for Partial Summary Judgment, all responses in opposition, Memoranda, all matters of record and in accord with the contemporaneous Memorandum Opinion to be filed of record, it hereby is **ORDERED** and **DECREED** that:

1. Defendant Lexington Insurance Company's Motion for Summary Judgment (cn 072109) to Count I (breach of contract) is **GRANTED** and Count I is **DISMISSED**.
2. Defendant Lexington Insurance Company's Motion for Summary Judgment (cn 072109) in regard to its counterclaim for restitution is **DENIED** and said counterclaim is dismissed.
3. Plaintiff LA Weight Loss' Motion for Summary Judgment (cn 072287) is **DENIED.**

BY THE COURT:

_____

C. DARNELL JONES, II J.

IN THE COURT OF COMMON PLEAS OF PHILADELPHIA COUNTY
FIRST JUDICIAL DISTRICT OF PENNSYLVANIA
CIVIL TRIAL DIVISION

LA WEIGHT LOSS CENTERS, INC.,	:	December Term 2003
Plaintiff,	:	No. 1560
v.	:	
	:	
LEXINGTON INSURANCE COMPANY,	:	Commerce Program
Defendant.	:	Control Numbers 072109/072287

MEMORANDUM OPINION

JONES, II, J.

This is an insurance coverage action filed by LA Weight Loss Centers, Inc. against Lexington Insurance Company ("Lexington") for breach of contract and bad faith arising from the denial of coverage for an underlying EEOC Class Action Litigation captioned EEOC v. LA Weight Loss Centers, Inc., Civil Action Number CV 648. Presently before the court are the parties' cross motions for summary judgment to Count I of the Complaint. Additionally, Lexington moves for summary judgment on its counterclaim for restitution of defense costs. For the reasons discussed below, Lexington's Motion for Summary Judgment is granted as to Count I and denied as to its claim for restitution and LA Weight Loss' Motion for Summary Judgment is denied.

BACKGROUND

Lexington issued a claims-made employment practices liability insurance policy to LA Weight Loss Centers, Inc. for the policy period March 20, 2001 to March 20, 2003, policy number 1052239. This was the first policy written by Lexington for LA Weight Loss Centers, Inc.

The Lexington policy obligates Lexington to indemnify LA Weight Loss and to pay all forms of monetary damages, settlements, attorney fees and defense costs arising out of claims alleging discrimination and wrongful termination that are made during the policy period.

Prior Charges of Discrimination

1. Kathy Koch

On or about June 22, 1998, Kathy Koch, a former employee of LA Weight Loss, filed a charge of discrimination against LA Weight Loss with the Commission of Human Relations and the office of the EEOC in Maryland, alleging that she was terminated in retaliation for her complaints about LA Weight Loss's hiring practices and their personal treatment of her. (Dfts. Mt. for SJ Exhibit "9"). On November 3, 1998 the EEOC sent LA Weight Loss notice of the Koch charge and resultant investigation (Dfts. Mt. for SJ Exhibit "10"). The Charge involved allegations relating to Koch's personal treatment and the alleged retaliation against her by LA Weight Loss. (Dfts. Mt. for SJ Exhibit "9"). On January 6, 1999 LA Weight Loss responded to the Koch charge by filing a position paper with the EEOC detailing Koch's poor job performance. On September 14, 2000, the EEOC issued a Determination on the Koch charge, stating that "there was reasonable cause to believe that, since at least 1997, LA Weight Loss has throughout its entire Company discriminated against males as a class on the basis of gender with respect to its selection and hiring in all positions throughout the Company." (Dfts. Mt. for SJ Exhibit "15"). The Determination included a written notice to LA Weight Loss of results of the EEOC's investigation into the Koch charge, with an invitation by the EEOC for LA Weight Loss to participate in the "process of conciliation." *Id.*

2. Nina C. Catagnus

On January 10, 2000, Nina C. Catagnus ("Catagnus") filed an age discrimination and retaliation charge against LA Weight Loss Centers with the EEOC, Philadelphia District Office. (Exhibit "23"- Dfts Mt. for SJ.). Catagnus' charge alleged that she was transferred to a less desirable area and was then terminated based upon her age and in retaliation for challenging LA Weight Loss Center's discriminatory policies towards hiring men and older people. The charge alleged that Catagnus "went against Ms. Petrizio's discriminatory orders to never hire a male," and that after she hired Todd McCann, she was transferred to work at a less desirable location, where the number of persons for whom she was responsible was reduced. On January 10, 2001, the EEOC issued a determination in the Catagnus charge. (Exhibit "24"). The EEOC determined that "the body of evidence shows that Respondent (LA Weight Loss) has a policy of discriminating against male applicants to exclude them from being hired, trained or promoted." *Id*.

3. Todd McCann

On or about March 30, 2000, Todd McCann, a former employee of LA Weight Loss, filed a charge of discrimination against LA Weight Loss with the Pennsylvania Human Relations Committee and the EEOC. (Dfts. Mt. for SJ Exhibit "25"). The charge alleged that McCann was required to perform undesirable tasks and did not receive training and promotions due to his gender. *Id*. The charge further alleged that LA Weight Loss discriminated against men and that he was constructively discharged from the company. *Id.* On March 27, 2001, the EEOC issued a Determination on the McCann Charge that the record evidence substantiated McCann's allegations of gender

discrimination against McCann and "males in general". (Dfts. Mt. for SJ Exhibit "26"). The McCann determination also stated that LA Weight Loss had a "discriminatory hiring policy regarding males." Id. The Determination comprised a written notice to LA Weight Loss of the results of the EEOC's investigation with an invitation to participate in the process of conciliation. *Id.*

On or about October 31, 2001, LA Weight Loss settled all disputes with McCann; Mc Cann executed a complete and general release in favor of LA Weight Loss for all claims arising out of or relating to the claims made in the McCann charge.

The Underlying Class Action

On February 28, 2002, the EEOC filed a class action against LA Weight Loss alleging unlawful employment practices against males as a class by failing to hire them on the basis of their sex. (Dfts. Mt. for SJ Exhibit "28").[1] On December 5, 2002, Lexington reported to LA Weight Loss that while it continued to "investigate" the coverage issues, Lexington would undertake its representation under reservation of rights. (Dfts. Mt. for SJ Exhibit "31"). The reservation of rights letter also purportedly attempted to reserve Lexington's right to seek allocation or reimbursement of defense and indemnity costs between potentially covered and non-covered claims. *Id.*

On October 14, 2003, Lexington sent a declination letter to LA Weight Loss Centers, explaining that it did not have a duty to continue to defend or to indemnify LA

[1] The complaint also made allegations on behalf of Koch for alleged retaliation against her for complaining about the company's hiring practices. LA Weight Loss concedes that Lexington has no obligation to defend or to indemnify LA Weight Loss in the Koch Intervenor Action or the EEOC class action litigation complaint to the extent it seeks recovery on behalf of Kathy Koch. (Plts. Memo of Law in Response to Lexington's Mt. for Summary Judgment pg. 2, fn 2). As such, the court will not address the issue of coverage as it pertains to Koch.

Weight Loss Centers in the EEOC matter because the policy's date of claim and retroactive date provisions prevented coverage. (Dfts. Mt. for SJ Exhibit "37").

On December 11, 2003, LA Weight Loss Centers filed the instant complaint alleging breach of contract (Count I) and bad faith (Count II) against Lexington on the basis that Lexington wrongfully refused to defend it against the EEOC class-action discrimination complaint. Lexington answered the complaint and asserted a counterclaim against LA Weight Loss Centers for restitution. The parties have now filed cross motions for summary judgment to Count I (breach of contract) of the complaint. Lexington has also filed a motion for summary judgment on its counterclaim seeking to recoup the amount it paid in defense costs in connection with the EEOC matter.

DISCUSSION

A. Lexington does not have a duty to defend LA Weight Loss in the Underlying Class Action Claim.

Pursuant to Pennsylvania law, it is the duty of the court to interpret the terms of an insurance contract. Standard Venetian Blind Co. v. Am. Empire Ins. Co., 503 Pa. 300, 469 A.2d 563, 566 (1983). Ascertaining the intent of the parties as manifested by the language of the written instrument is the goal of interpreting the contract. *Id.* "Where a provision of a policy is ambiguous, the policy provision is to be construed in favor of the insured and against the insurer, the drafter of the agreement." *Id*. However, where the language of the contract is clear and unambiguous, a court must give effect to that language. *Id.*

A provision of a contract is considered to be ambiguous "if reasonable persons considering the relevant language in the context of the entire policy could honestly differ as to its meaning." Lucker Mftg. v. Home Ins. Co., 23 F.3d 808, 814 (3d Cir. 1994).

That is, a term is ambiguous, "if and only if it is reasonably or fairly susceptible of different constructions and is capable of being understood in more senses than one and is obscure in meaning through indefiniteness of expression or has a double meaning…a contract is not rendered ambiguous by the mere fact that the parties do not agree on the proper construction." Bohler-Uddeholm Am., Inc. v. Ellwood Group, Inc., 247 F.3d 79, 93 (3d Cir. 2001).

Under Pennsylvania law, the insured has the burden of proving that its claim falls within the policy's affirmative grant of coverage. Koppers Co., Inc. v. Aetna Cas. and Sur. Co., 98 F.3d 1440, 1446 (3d Cir. 1996). However, the insurer carries the burden of proving the applicability of any exclusions or limitations on coverage, since they are affirmative defenses. *Id.* Moreover, the court is required to construe policy exclusions strictly against the insurer. First Pennsylvania Bank v. Nat'l Union Fire Ins. Co., 397 Pa. Super. 612, 580 A.2d 799, 802 (1990).

In the case at bar, it is undisputed that Lexington issued a "claims made" policy to LA Weight Loss with an effective date of March 20, 2001 to March 20, 2003. "Claims made" polices protect against claims made during the life of a policy irrespective of when the act giving rise to the claim occurred. Westport Insurance Co. v. Mirsky, 2002 U. S. Dist. LEXIS 16967, 29 (E.D. Pa. 2002)(*quoting* Pizzini v. Am. Int'l Specialty Lines Ins. Co., 210 F. Supp. 2d 658, 668 (E. D. Pa. 2002)). "Claims made" polices are different than occurrence policies, which protect an insured against occurrences during a policy period, regardless of when the resulting claims are made. *Id.*

A "claims made" insurance policy represents a distinct bargained for exchange between an insurer and insured. *Id.* An insurer receives the benefit of a clear and certain

cut-off date for coverage, whereas the insured typically pays a lower premium. *Id.* In a "claims made" policy, the reporting requirement helps define the scope of coverage under the policy and as a result, the reporting requirements are strictly construed. *Id.* Although preclusion of coverage is a harsh consequence, "claims made" policies and their reporting requirements are enforceable. *Id.*

The crux of the parties' motions before the court is whether the underlying EEOC action constitutes a claim "first made" during the effective dates of the Lexington policy.[2] This determination depends upon the definition of "claim" contained within the policy, as well as the application of the policy's language concerning when coverage is provided.

The Lexington policy defines "claim" as follows:

> Claim means a written demand or notice received by an **Insured** in which damages likely to be covered by this policy are alleged. **Claim** includes a civil action, an administrative proceeding; alternative dispute resolution proceeding, or an action brought by a person or entity acting on behalf of an **Employee(s)** of the **Insured** to which **you** must submit or to which **you** submit with **our** consent. **Claim** shall include a proceeding for injunctive or non monetary relief. **Claim** shall not include labor or grievance arbitration subject to a collective bargaining agreement. A class action lawsuit is considered one **Claim**.
> (Exhibit "1" Plts. Mt. for SJ Section VII A. p. 4.).

The policy further provides that coverage will be provided only to claims first made against any insured during the policy period. A claim is considered to be made on

[2] LA Weight Loss maintains that the court should utilize the "four corners" standard to determine Lexington's duty to defend it in the underlying EEOC complaint. Here, application of said standard is unnecessary, since it is undisputed that the factual allegations of the underlying complaint fall within Lexington's scope of coverage. Instead, the issue before the court is whether the EEOC complaint was first made during the effective date of the Lexington Policy. Since this information is not contained within the four corners of the EEOC complaint, the court must look to extrinsic evidence beyond the EEOC complaint to analyze the pending motions.

the earlier of:

1. the date any **Insured** receives a written notice of a **Claim** being made against any Insured seeking damages covered by this policy; or
2. the date **we** make a settlement on account of an **Insured Event** but in advance of written **Claim** being made.

An Insured Event is defined as follows:

> (1) **your Employee** or former **Employee**, or an applicant for employment with **you**, alleging **Discrimination** by an **Insured**, … Alleging means lodging an oral or written complaint or charge with your management or **Supervisory Employee(s)** or with **your** corporate legal or human resource departments. (*Id*. at 5.).

All claims arising out of one Insured Event are considered to be one claim under the policy and are deemed to be made at the time the first of such claim is made. If such claims are made while this policy is in effect and also while predecessor or successor policies issued by Lexington are in effect, all such claims are still considered to have been made at the time the first of such claims is made and only the policy in effect at that time shall apply to all such claims. *Id*. at 4.

Here, the court finds as a matter of law that although the underlying class action complaint was filed during the Lexington policy period, LA Weight Loss Centers received written notice of the underlying EEOC class action before Lexington's policy effective date of March 20, 2001. It is well settled that as a pre-condition to filing suit under Title VII, a plaintiff must first file charges with the EEOC within 180 days of the alleged discriminatory act. *See* Wright v. Phila. Gas Works, 2001 U.S. Dist. LEXIS 15852 (E.D. Pa. 2001); *See also* 28 U.S.C. § 2000E-5(e).[3] The purpose of endowing the

[3] Once the EEOC receives the charge, it must investigate the allegations to determine if there is reasonable cause to believe that the allegations are true. Hicks v. ABT Assoc., 572 F.2d 960, 963 (3d Cir. 1978). If reasonable cause is found, conciliation proceedings are instituted. *Id.* If no reasonable cause is

EEOC with the authority to initially investigate employment discrimination claims is to promote administrative conciliation, rather than immediate resort to the court system. Ostapowicz v. Johnsorn Bronze Co., 541 F.2d 394, 398 (3rd Cir. 1976). Accordingly, once a charge is filed with the EEOC, the scope of the ensuing civil action is defined by the scope of the EEOC investigation which can reasonably be expected to grow out of the charge of discrimination." Hicks, 572 F.2d at 966. Therefore, the allegations in a Title VII action must be limited to only those of which the administrative charge provided reasonable notice.

Here, the record reflects that LA Weight Loss received written notice of the class action allegations in the underlying complaint for which it seeks coverage as early as March 30, 2000, when Todd McCann filed a charge of discrimination with the EEOC. McCann's charge specifically alleged that LA Weight Loss discriminated against him and other men on the basis of gender. (Exhibit "25" to Dfts. Mt. for SJ.). McCann's charge provided notice to the LA Weight Loss of the administrative proceeding with the EEOC. "When any charge is filed, the purposes of voluntary compliance and conciliation are served as there is no claim of surprise in such a situation." EEOC v. Northwestern Human Servs., 2005 U.S. Dist. LEXIS 23768 (D. Pa. 2005).

The McCann charge of discrimination filed with the EEOC constitutes a "claim" under the Lexington policy, since it is an administrative proceeding in which damages likely to be covered by the policy or injunctive or non-monetary relief is sought. Pursuant to the terms of the policy, a claim is considered to be made on the date any

---

found, or if conciliation attempts fail, the EEOC issues to the complainant a notice of their right to bring a civil action. *Id.* In this instance, it is clear that the attempts to conciliate the charge failed and as a result, the EEOC decided to bring the claim on behalf of the charging party.

insured receives written notice of a claim being made against any insured seeking damages covered by this policy. Since the claim was first made outside the Lexington policy period, coverage for the underlying class action does not exist.[4]

Contrary to LA Weight Loss' contention, the underlying class action lawsuit was not the first written notice received by LA Weight Loss of class-wide gender discrimination claims. The class wide gender discrimination class action grew as a consequence of the ongoing EEOC administrative proceedings. Consequently, since the underlying class action lawsuit was a progression of the prior EEOC administrative charges filed prior to the Lexington policy period, Lexington does not have a duty to provide coverage, as the claim was first made before the Lexington policy period became effective. Accordingly, Lexington's motion for summary judgment to Count I is granted and LA Weight Loss' Motion for Summary Judgment is denied.

B. Lexington's Motion for Summary Judgment on its Counterclaim is Denied.

Lexington also filed a motion for summary judgment on its counterclaim for restitution of defense costs against LA Weight Loss. Lexington contends that since it has no duty to defend LA Weight Loss in the underlying class action and since it reserved its

[4] Similarly, the EEOC determination in the Koch charge of discrimination issued on September 14, 2000, also constitutes written notice of a claim of gender based discrimination. The Koch Determination provides in relevant part:

> With respect to other issues like and related to, and which have grown out of the Commission's investigation of the allegations raised in the charge, the Commission has determined that there is reasonable cause to believe that, since at least 1997, Respondent has throughout its entire company discriminated against males on the basis of gender, with respect to its selection and hiring in all positions throughout the company.
> (Exhibit "15" Dfts. Mt. for SJ.).

right to recoup defense costs in a reservation of rights letter, it is now entitled to recover those costs. The court does not agree.

According to Lexington, its reservation of rights letter allows it to do much more than to withdraw from defending LA Weight Loss or to deny coverage in the underlying class action litigation. Lexington claims that its reservation of rights letter also allows it to be reimbursed for the funds it expended defending LA Weight Loss in the underlying action.[5]

In support of its position, Lexington relies upon authority from other jurisdictions that have found that an insurer may recover defense costs from its insured where the insurer agrees to provide the insured a defense pursuant to an express reservation of rights which includes the right to recoup defense costs, the insured accepts the defense, and a court subsequently finds that the insurer did not owe the insured a defense. *See* United National Insurance Co. v. SST_Fitness Corp., 309 F.3d 914 (6th Cir. 2002) (insurer was entitled to reimbursement of defense costs where the insurer reserved the right to recover defense costs and the insured accepted payment of defense costs); Knapp v. Commonwealth Land Title Insurance Co., 932 F. Supp. 1169 (D. Minn. 1996) (where insurer reserved its right to seek reimbursement of attorney's fees and costs, insured's silence in response to the reservation of rights letter and subsequent acceptance of defense constituted an implied agreement to the reservation of rights); Resure, Inc. v. Chemical Distributors, Inc., 927 F. Supp. 190 (M.D. La. 1996) (insurer was entitled to reimbursement for all costs of defense where it timely and specifically reserved the right

[5] Lexington relies upon the following provision in the reservation of rights letter "Lexington also reserves the right to seek allocation or reimbursement of defense and indemnity costs between potentially covered and non covered allegations." (Dfts. Mt. for SJ Exhibit "31").

to seek reimbursement and insured did not object to the reservation); North Atlantic Casualty & Surety Insurance Co. v. William D., 743 F. Supp. 1361 (N.D. Cal. 1990) (where insurer sent letter to the insured reserving the right to reimbursement, and the insured accepted payment of defense fees without comment, insurer was entitled to reimbursement from insured); Colony Insurance Co. v. G&E Tires & Service, Inc., 777 So. 2d 1034 (Fla. App. 2000) (insurer was entitled to reimbursement of defense costs where it timely and expressly reserved the right to seek reimbursement, and the insured accepted the offer of a defense with a reservation of rights); Hecla Mining Co. v. New Hampshire Insurance Co., 811 P.2d 1083, 1089 (Colo. 1991) (court states that proper course for insurer that believes it owes no duty to defend "is to provide a defense to the insured under a reservation of its rights to seek reimbursement should the facts at trial prove that the incident resulting in liability was not covered by the policy").

As of the writing of this opinion, Pennsylvania state appellate courts have not spoken on the issue. However, other jurisdictions have. A review of these cases demonstrates a split in authority as to whether recoupment should be permitted. The majority of the courts allow an insurer to recoup defense costs with the issuance by an insurer of a valid reservation of rights letter. These courts base their finding upon the existence of a contract implied in fact or law or a finding that the insured was unjustly enriched when its insurer paid defense costs for claims that were not covered by the insured's policy.

On the other hand, a minority of the courts refuse to permit an insurer to recover defense costs pursuant to a reservation of rights, absent an express provision to that effect in the insurance contract between the parties. *See e.g.*, General Agents Ins. Co. of Am.,

Inc. v. Midwest Sporting Goods Co., 215 Ill. 2d 146, 159-166 (Ill. 2005)(refusing to permit an insurer from recovering defense costs pursuant to a reservation of rights absent an express provision to that effect in the insurance contract); Shoshone First Bank v. Pacific Employers Insurance Co., 2 P.3d 510, 514 (Wy. 2000)(The court rejected the insurer's claim that it had the right to allocate defense costs for uncovered claims because its reservation of rights letter had specifically reserved the right to allocate the fees, expenses and indemnity payments when the case was resolved since the insurer is not permitted to unilaterally modify and change policy coverage.); a*ccord* Texas Ass'n of Counties Government Risk Management Pool v. Matagorda County, 52 S.W.3d 128, 44 Tex. Sup. Ct. J. 215 (2000) (absent provision providing for reimbursement of settlement funds, unilateral reservation of rights letter could not create rights not contained within the insurance policy);

After taking into consideration the parties' respective memoranda, as well as the authorities cited therein, the court finds the analysis relied upon by the minority of the courts that have addressed the issue to be more persuasive and adopts said reasoning herein. A reservation of rights letter does not create a contract allowing an insurer to recoup defense costs from its insured, but rather, is a mean to assert defenses and exclusions which are already set forth in the policy. Certainly, if an insurer wishes to retain its right to seek reimbursement of defense costs in the event it later is determined that the underlying claim is not covered by the policy, the insurer is free to include such a term in its insurance contract. Absent such a provision in the policy, an insurer should not be permitted to unilaterally amend the policy by including the right to reimbursement in its reservation of rights letter.

In Terra Nova Insurance Co. v. 900 Bar, Inc., 887 F.2d 1213 (3d Cir. 1989), the United States Court of Appeals for the Third Circuit, applying Pennsylvania law, predicted that the Pennsylvania appellate courts would not permit an insurer to recover defense costs even when it defends under a reservation of rights if it is later determined there is no coverage. The court reasoned that:

> "A rule permitting such recovery would be inconsistent with the legal principles that induce an insurer's offer to defend under reservation of rights. Faced with uncertainty as to its duty to indemnify, an insurer offers a defense under reservation of rights to avoid the risks that an inept or lackadaisical defense of the underlying action may expose it to if it turns out there is a duty to indemnify. [footnote omitted]. At the same time, the insurer wishes to preserve its right to contest the duty to indemnify if the defense is unsuccessful. Thus, such an offer is made at least as much for the insurer's own benefit as for the insured's. If the insurer could recover defense costs, the insured would be required to pay for the insurer's action in protecting itself against the estoppel to deny coverage that would be implied if it undertook the defense without reservation." Terra Nova Insurance Co., 887 F.2d at 1219-20.

Thus, the court cannot say that an insured is unjustly enriched when its insurer tenders a defense in order to protect its own interests, even if it is later determined that the insurer did not owe a defense.

In the case at bar, Lexington's insurance policy at issue did not provide for reimbursement of defense costs. Consequently, Lexington's attempt to include the right to reimbursement in its reservation of rights letter must fail.

CONCLUSION

For the foregoing reasons, Lexington's partial motion for summary judgment is granted as to Count I and denied as to its counterclaim for reimbursement and LA Weight Loss' motion for summary judgment is denied.

An order consistent with this opinion will follow forthwith.

BY THE COURT,

_____

C. DARNELL JONES, II, J.

Date:

.