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A DOZEN YEARS AFTER *BIRTH CENTER*, THE THIRD PARTY BAD FAITH CLAIM CONTINUES TO EXPAND

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INTRODUCTION

Over a half century ago, Pennsylvania recognized the right of an insured to sue a liability insurer for its bad faith refusal to settle a lawsuit against the insured within the policy limits, thus exposing the insured to a verdict in excess of the limits. For much of that period, the fact pattern in such "third party bad faith" actions—so called because the underlying lawsuit against the insured is initiated by a third party—was fairly typical: (1) plaintiff's demand for settlement within policy limits; (2) the failure of the liability insurer to settle on behalf of the defendant insured; and (3) a subsequent trial and excess verdict against the insured. Damages awarded in such cases were likewise typical: the amount of the excess verdict. With the 1990 enactment of Pennsylvania's bad faith statute, 42 Pa.C.S.A. §8371, and more particularly with the Pennsylvania Supreme Court decision in *Birth Center v. St. Paul Companies, Inc*., 787 A.2d 376 (Pa. 2001), the third party bad faith claim has, whether rightly or wrongly, been the subject of expansion by the courts.

THE COMMON LAW ORIGIN OF THIRD PARTY BAD FAITH IN PENNSYLVANIA

The third party bad faith cause of action was first judicially recognized by the Pennsylvania Supreme Court in *Cowden v. Aetna Casualty Insurance Company*, 134 A.2d 223 (Pa. 1957). In that case, Pennsylvania joined the majority of other jurisdictions in recognizing that a liability insurer's conduct in handling

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WHAT CAUSES OF ACTION CAN PENNSYLVANIA PLAINTIFFS PURSUE AGAINST MANUFACTURERS OF GENERIC PHARMACEUTICALS IN THE WAKE OF *MUTUAL PHARMACEUTICAL, INC. V. BARTLETT* AND *PLIVA, INC. V. MENSING*?

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On June 24, 2013, the United States Supreme Court handed manufacturers of generic pharmaceuticals another victory in *Mutual Pharmaceutical Co., Inc. v. Bartlett*, ___ U.S. ___, ___ S.Ct. ____, 2013 WL 3155230 (Jun. 24, 2013). The Court held that "state-law design defect claims . . . that place a duty on a manufacturer to render a drug safer by either altering its composition or altering its labeling are in conflict with federal laws that prohibit manufacturers [of generic prescription drugs] from unilaterally altering drug composition or labeling." *Id*. at *11. This decision follows the Court's decision in *PLIVA, Inc. v. Mensing*, 564 U.S. ___, 131 S.Ct. 2567, 180 L.Ed.2d 580 (2011) which held that state tort claims directed to the adequacy of a generic prescription drug's warnings are preempted.

Even prior to the preemption of such claims, Pennsylvania was more circumscribed in causes of action it made available against manufacturers of prescription drugs. This article examines the *Mutual Pharmaceutical* and *PLIVA* decisions, as well as significant

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the defense of a third party claim could give rise to a bad faith claim against the insurer. The court held that the insurer was obligated under the contract to act in good faith in the defense of the underlying claim, stating:

It is established by the greatly preponderant weight of authority in this country that an insurer against public liability for personal injury may be liable for the entire amount of a judgment secured by a third party against the insured, regardless of any limitation in the policy, if the insurer's handling of the claim, including a failure to accept a proffered settlement, was done in such a manner as to evidence bad faith on the part of the insurer in the discharge of its contractual duty. (*Id*. at 227.)

In *Cowden* and later cases, the courts recognized that the transfer of rights—investigation, defense, and settlement of claims—from the policyholder to the insurer transferred a corollary obligation to act in good faith. An insurer's failure to act in good faith exposed it to extra-contractual damages. The damage award recoverable for a liability insurer's bad faith failure to settle a claim or suit against its insured was typically "the entire amount of a judgment secured by a third party against the insured, regardless of any limitation in the policy … ." *Id.*

BIRTH CENTER'S ALLOWANCE FOR CONSEQUENTIAL DAMAGES IN ADDITION TO PAYMENT OF POLICY LIMITS AND EXCESS VERDICT AMOUNT

The bad faith statute, enacted in 1990, provided that "[i]n an action arising under an insurance policy, if the court finds that the insurer has acted in bad faith toward the insured," the court is empowered to award punitive damages, attorneys' fees, interest, and court costs against the insurer. *See* 42 Pa.C.S.A. §8371. This statute had an immediate impact on first party claims, i.e., policies where the insured brings his or her claim directly with the insurer (such as homeowners' property coverage or auto comprehensive/collision coverage) because, before 1990, Pennsylvania had not recognized the first party bad faith claim. *See D'Ambrosio v. Pennsylvania National Mutual Casualty Insurance Company*, 431 A.2d 966 (Pa. 1981). The bad faith statute's impact upon the traditional common law third party claim was to come later, and was, at least initially, more subtle.

The bellwether decision came in 2001 with the Supreme Court's opinion in *Birth Center v. St. Paul Companies, Inc*. St. Paul insured Birth Center under a medical professional liability policy with a $1 million policy limit. St. Paul refused to settle a medical malpractice suit against Birth Center. The case proceeded to trial, resulting in a verdict (after the inclusion of delay damages and interest) against Birth Center of $4,317,743. St. Paul agreed to indemnify Birth Center for the entire verdict and the parties settled the case for $5,000,000.

Birth Center thereafter filed a §8371 and common law bad faith actions. In the bad faith trial, a jury found that (1) St. Paul acted in bad faith when it refused to settle the suit against Birth Center and (2) the insurer's bad faith conduct was a substantial factor in causing Birth Center to incur compensatory damages (loss of business and reputation) in the amount of $700,000. In affirming the bad faith verdict, the Supreme Court held, "Where an insurer refuses to settle a claim that could have been resolved within policy limits without 'a *bona fide* belief . . . that it has a good possibility of winning,' it breaches its contractual duty to act in good faith and its fiduciary duty to its insured. *Birth Center*, 787 A.2d at 379 (citing *Cowden*, 134 A.2d at 229).

Significantly, the Supreme Court held that the payment by St. Paul of the excess verdict did not insulate it from bad faith liability, stating:

> The fact that the insurer's intransigent failure to engage in settlement negotiations forced it to pay damages far in excess of the policy limits … does not insulate the insurer from liability for its insured's compensatory damages where the insured can prove that the insurer's bad faith conduct caused damages. (*Id.*)

> The Court allowed the insured, Birth Center, to recover its lost profits and compensatory damages under a contractual bad faith theory as well as under §8371. While stating that "the insured's liability for an excess verdict is a type of compensatory damage for which this Court has allowed recovery," *id.* at 389, the Court added, "[W]hen an insurer breaches its insurance contract by a bad faith refusal to settle a case, it is appropriate to require it to pay other damages that it knew or should have known the insured would incur because of the bad faith conduct." *Id.* at 389. According to the court, apart from §8371 damages, "the insurer is liable for the known and/or foreseeable compensatory damages of its insured that reasonably flow from the insurer's bad faith conduct." *Id.*

Although the Supreme Court majority in *Birth Center* suggested that its decision did not represent a departure from existing law for breach of contract, for all practical purposes the law regarding bad faith damages took a dramatic turn with that decision. The Supreme Court allowed the imposition of consequential damages over and above the amount of the excess verdict. No reported cases had ever upheld such a claim before. Following *Birth Center*'s rationale, subsequent courts have rendered large consequential damages awards in the context of an insurer's denial of coverage under a liability policy. *See, e.g., Upright Material Handling, Inc. v. Ohio Cas. Grp*., 74 Pa. D.&C.4th 305 (Lackawanna 2005), *aff'd sub nom., Bombar v. West Am. Ins. Co*., 932 A.2d 78 (Pa. Super 2007); *Pa. Nat. Mut. Cas. Ins. Co. v. Johnson*, 82 Pa.D.&C. 4th 23 (Del. 2007).

APPLICATION OF RELAXED NEGLIGENCE STANDARD IN THIRD PARTY BAD FAITH FAILURE TO SETTLE CASES

In acknowledgment that it was creating a new cause of action with significant extra-contractual repercussions, the *Cowden* court required that "bad faith must be proven by clear and convincing evidence and not merely insinuated." *Cowden*, 134 A.2d at 229. Further, *Cowden* expressly acknowledged that negligence or bad judgment by the insurer did not equate to bad faith, holding that "bad faith and bad faith alone was the requisite to render the [insurer] liable," and "of course, bad judgment, if alleged, would not have been actionable." *Id*.

The recognition that mere negligence does not establish bad faith, and that bad faith must be proven by clear and convincing evidence, has long underpinned the jurisprudence regarding insurer bad faith, and, indeed, these principles have been incorporated into decisions applying the bad faith statute. *See e.g., Terletsky v. Prudential Property & Cas. Ins. Co*., 649 A.2d 680, 688 (Pa. Super. 1994), appeal denied, 659 A.2d 560 (Pa. 1995); *Condio v. Erie Insurance Exch*., 899 A. 2d. 1136, 1142 (Pa. Super. 2006).

Incongruously, therefore, one of the more remarkable developments in the last decade has been the emergence of case law suggesting that the standard to prove the third party common law bad faith claim is that of negligence. In *Schubert v. American Independent Ins. Co*., 2003 U.S. Dist. LEXIS 10769 (E.D. Pa. June 24, 2003), the late Judge Newcomer held that negligence was the standard to be applied in such cases, stating:

> [A]n insurer must act with due care when handling an insured's litigation. Included within this duty is the obligation to act reasonably when deciding whether or not to accept a settlement offer. Reasonableness has traditionally been the standard governing an insurer's decision whether to settle. . . . An insurer has been deemed to act reasonably when its decision whether or not to settle is "honest, intelligent, and objective." (*Id*. at *6-7.)

This analysis was echoed more recently in Judge McLaughlin's opinion in *DeWalt v. Ohio Cas. Ins. Co*., 513 F. Supp. 2d 287 (E.D. Pa. 2007). Citing Third Circuit and Pennsylvania Supreme Court cases, the court concluded that under Pennsylvania decisions (or at least *dicta* in those decisions), "negligence or unreasonableness in investigating a claim or refusing an offer of settlement can constitute bad faith." *Id*. at 297. Although applying this relaxed standard, the *DeWalt* court ultimately concluded that the insurer there did not act in bad faith in refusing to pay its policy limits to one claimant when there had been two other claimants also suing the insured.

ALLOWANCE OF THIRD PARTY BAD FAITH CLAIM EVEN WHEN INSURER SETTLES THIRD PARTY SUIT BEFORE TRIAL WITHIN POLICY LIMITS

The classic third party bad faith claim involved the failure of an insurer to settle a suit within the liability policy limits, followed by trial and a resulting excess verdict against the insured. In exchange for an agreement not to execute upon the excess verdict, the insured would assign his or her rights to the successful plaintiff in the underlying case, who, as assignee of the insured, would prosecute the bad faith action. *See, e,g., Gray v. Nationwide Mut. Ins. Co*., 223 A.2d 8 (Pa. 1966) (holding that common law bad faith claims were assignable).

With the conceptual expansion of the third party bad faith claim after *Birth Center*, it was only a matter of time until a court would be asked to determine whether a §8371 or common law third party bad faith claim might be allowed to proceed even where the insurer agreed to settle a suit against its insured before trial—in other words, where there was *no trial*, and thus *no excess verdict*.

Judge Schiller of the Eastern District first answered this question in the negative in *Daniel P. Fuss Builders-Contractors, Inc. v. Assurance Company of America*, 2006 U.S. Dist. LEXIS 56742 (E.D. Pa., Aug.11, 2006). There, the court concluded that where the third party litigation was ultimately settled within policy limits and without the entry of an excess verdict, there could be no bad faith claim, even where it was alleged that the insurer acted unreasonably and in bad faith in delaying the settlement of the litigation. According to the court, it did not "uncover a single federal or state court in Pennsylvania that has recognized a cause of action for an insurer's delay of payment in the context of a third party claim brought under § 8371 or a contractual bad faith claim." *Id*. at *12. The court stated that it was unwilling to "create a cause of action not yet recognized by Pennsylvania law." *Id*. at *14.

Notwithstanding Judge Schiller's discretion on the issue, subsequent district court judges have answered the question differently. Judge Cohill of the Western District refused to dismiss a bad faith case where it was alleged that a liability insurer acted in bad faith in the way it handled a third party claim which was ultimately settled by the insurer in *Gideon v. Nationwide Mut. Fire Ins. Co.*, 2008 U.S. Dist. LEXIS 26729 (W.D. Pa. Mar. 20, 2008). Acknowledging that its decision differed from that in *Fuss Builders*, the court stated, with little discussion on the point, "We simply disagree with the analysis of the issue by our sister court." *Id* at *23. In *Standard Steel, LLC. v. Nautilus*

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Ins. Co., 2008 U.S. Dist. LEXIS 71487 (W.D. Pa. Sept. 17, 2008), Magistrate Judge Mitchell of the Western District weighed in on the subject. Relying upon *Gideon*, and declining to follow *Fuss Builders*, the court concluded, "[A]bsent Pennsylvania caselaw or statutory text which supports [the insurer's] position that an excess verdict is a condition precedent to a statutory bad faith claim for failure to settle a third party claim, we do not impose such a requirement here." *Id.* at *12.

In May 2013, Judge Mariani of the Middle District sided with the judges of the Western District in *Bodnar v. Nationwide Mut. Ins. Co*., 2013 U.S. Dist. LEXIS 70144 (M.D. Pa. May 16, 2013). Stephen Bodnar was a masonry contractor insured under a $1 million commercial liability policy with Nationwide. Bodnar was sued by the Estate of James Berry in connection with a fatal accident involving Berry. Nationwide agreed to defend Bodnar subject to a reservation of rights. Coverage questions included whether Berry had been an employee of Bodnar's business at the time of the accident. Nationwide instituted a declaratory judgment action, which was dismissed.

Ultimately, Bodnar entered into an agreement with the Estate, which provided that Nationwide would pay the Estate $1,000,000 plus interest, and the Estate would hold Bodnar harmless from any further liability in connection with the fatality involving Berry. Bodnar then sued Nationwide for common law and statutory bad faith, based upon the insurer's alleged unjustified delay in resolving the Estate's litigation against Bodnar. The complaint alleged that the company acted in bad faith in its "callous, unjustified and unreasonable refusal to settle the action," and that even though Bodnar had allegedly "continuously told the Defendant that Berry was not his employee," the insurer "continued to drag out the litigation" between Bodnar and the Estate. *Id*. at *9-10.

Nationwide moved for summary judgment on the bad faith counts. The insurer argued that in the absence of the possibility of an excess verdict, there could be no viable common law or statutory bad faith claim against it. Because it paid its policy limits plus interest to the Estate on behalf of Bodnar in accordance with the settlement agreement, it said, there could be no further recovery against the insurer. Citing *Fuss Builders*, the company pointed out that there were no appellate court decisions recognizing a viable third party bad faith claim based solely on delay.

In a detailed and citation-filled opinion, Judge Mariani rejected the insurer's arguments. Although "express[ing] no opinion as to the merits of Plaintiffs' claims, any attempt at the determination of which must be deferred, at least until the conclusion of discovery," the court denied summary judgment. *Id*. at *43. The court ruled that the insurer "may not avoid further inquiry into its conduct in connection with its handling of the claims," explaining as follows:

> That is not to say that an insurer's delay in the settlement of a claim, standing alone, presents a cause of action for breach of contract or bad faith. But it is equally the case that an insurer's payment of the policy limits prior to a verdict cannot insulate an insurer from claims of breach of contract and bad faith in connection with its conduct prior to its payment. A delay in payment of a third party claim, if of inordinate and unreasonable length, effectively becomes a denial of the claim as assuredly as if the denial was swiftly and unequivocally communicated to the insured. This is particularly the case when the insurer's conduct over a substantial period of time is consistent with or suggests the absence of a good faith intent to resolve the claim for the benefit of its insured. (*Id*. at *41.)

CONCLUSION

In the dozen years since the decision in *Birth Center v. St. Paul Companies*, courts have wrought a significant expansion of the traditional third party common law bad faith action. This expansion is evident in at least three ways.

First, as demonstrated in *Birth Center*, the courts may choose to take an expansive view of the consequential damages a plaintiff is permitted to seek for alleged breach of the implied contractual duty of good faith and fair dealing. Second, as seen in the *Schubert* and *DeWalt* decisions, in reviewing the conduct of an insurer in deciding not to settle a case before trial, courts may apply a more relaxed negligence standard, rather than the bad faith standard originally articulated in *Cowden*. Third, as demonstrated most vividly in *Bodnar v. Nationwide*, in the face of allegations of delay or other misconduct, courts may be persuaded to allow a third party bad faith claim to proceed even where the insurer fully satisfies its contractual agreement to settle a suit against its insured before trial.

Query whether this expansion of the third party bad faith cause of action reflects sound public policy, a fair understanding of the real-world duties of the liability insurer, or even the correct interpretation of the cause of action as founded in *Cowden*. Certainly, this is an area requiring more input from our state appellate courts. In the meantime, however, insurance claims professionals and attorneys representing insurance companies must be mindful of the new reality exemplified by the cases cited above.

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Pennsylvania holdings to identify the theories and causes of action that are subject to dismissal as a matter of law, and concludes with a consideration of the relatively narrow range of claims that may still be brought against the manufacturer of a generic prescription drug.

A. Overview of the Approval Process for Generic Prescription Drugs

Generic drugs are treated differently from name brand drugs for preemption purposes. Compare *Wyeth v. Levine*, 555 U.S. 555 (2009) (finding no federal preemption for manufacturers of name brand prescription drugs approved under a New Drug Application) *with PLIVA, supra* (preempting state law failure to warn claims against manufacturer of generic prescription drug approved under an Abbreviated New Drug Application). The difference lies in the manner in which the drugs are approved by the Food and Drug Administration and the resulting ability of a manufacturer to change the labeling and design of the drug.

Briefly, new name brand prescription drugs are required to submit a New Drug Application ("NDA") to the Food and Drug Administration ("FDA") that requires significant clinical studies demonstrating that the drug is "safe for use" in the manner described in its labeling and package insert. See 21 U.S.C. §355(d). The process is both time consuming and expensive.

Generic drugs, on the other hand, are approved under the Hatch-Waxman Amendments to the Food, Drug and Cosmetic Act ("FDCA"). *See* "P.L. 98-417, Drug Price Competition and Patent Term Restoration Act," H.R. Rep. No. 857(I), 98th Cong., 2d Sess. (1984), reprinted in 1984 U.S.C.C.A.N. 2647. The Hatch-Waxman Amendments created an expedited FDA review process for proposed generic drugs in order to promote the production of affordable generic medicines. *See generally* 21 U.S.C. § 355(j) (2007); *see also Purepac Pharm. Co. v. Thompson*, 354 F.3d 877, 879 (D.C. Cir. 2004). To accomplish the goal of lower priced medications, the Hatch-Waxman Amendments exempt generic drug manufacturers from the requirement of conducting the extensive investigational studies and clinical trials required when a new drug is brought to market. Rather, the Hatch-Waxman Amendments permit generic drugs to be approved by an Abbreviated New Drug Application ("ANDA") showing that the generic product uses the same active ingredient as a previously approved drug, *See* 21 U.S.C. §355(j). Further, the drug must be the "bioequivalent" of the previously-approved name brand drug. A generic drug is the "bioequivalent" of an approved name brand drug if "the active ingredients of the new drug are of the same pharmacological or therapeutic class as those of the reference listed drug . . . and the new drug can be expected to have the same therapeutic effect as the listed drug[.]" 21 U.S.C. § 355(j)(2)(A)(iv). The applicable regulations further define "bioequivalence", in pertinent part, as having the absence of a significant difference in the rate and extent to which the active ingredient or active moiety in pharmaceutical equivalents or pharmaceutical alternatives becomes available at the site of drug action when administered at the same molar dose under similar conditions[.]" 21 CFR § 320.1(e)

In addition, the Hatch-Waxman Amendments require that a generic drug's labeling and warnings be "the same" as the FDA approved name brand drug. 21 U.S.C.§ 355(j)(2)(A)(v). Each application for a proposed generic drug (or "ANDA") must include proof "that the labeling proposed for the [generic] drug is the same as the labeling approved for the [brand-name] drug . . . except for changes required . . . because the [generic] drug and the [brand-name] drug are produced or distributed by different manufacturers." *Id*. § 355(j)(2)(A)(v) (emphasis added). The only acceptable deviations from the approved name brand drug's labeling are for "differences in expiration date, formulation, bioavailability, or pharmacokinetics, labeling revisions made to comply with current FDA labeling guidelines or other guidance[.]". 21 C.F.R. §314.94(a)(8)(iv). These federal requirements of sameness restrict the ability of manufacturers of generic prescription drugs from modifying their products under most circumstances. These restrictions form the basis for why state tort claims concerning generic drugs are preempted.

B. *PLIVA, Inc. v. Mensing* Holds That State Tort Claims Concerning the Adequacy of a Generic Drug's Warnings Are Preempted.

In *PLIVA, Inc. v. Mensing*, 564 U.S. ___, 131 S.Ct. 2567, 180 L.Ed.2d 580 (2011), the United States Supreme Court held that state tort lawsuits challenging the adequacy of the warnings associated with generic prescription drugs are preempted by federal law.

PLIVA concerned the viability of personal injury lawsuits filed by persons who claimed they were injured by a generic version of the prescription drug metoclopramine. *Id*. at 2573. Evidence accumulated that use of metoclopramine could cause tardive diskiniesia, a neurological disorder. *Id*. The generic manufacturers argued that federal law preempted state law tort claims because federal statutes and FDA regulations require them to use the same safety and efficacy labeling as the name brand drug. *Id*. Therefore, the manufacturers argued, they could not comply with a federal requirement to make their labeling and warnings the same as the name brand drug, and comply with any state tort law duty that would require them to use a different label and warnings. *Id*. When the Courts of Appeals for the Fifth and Eighth Circuits rejected the manufacturers' arguments, the claims were consolidated for appeal to the Supreme Court.

The Supreme Court reversed the Fifth and Eighth Circuits, finding that federal law and FDA regulations preempted the state tort claims. *Id*. The Supreme Court noted that "[p]re-emption analysis requires us to compare federal and state law. We therefore begin by identifying the state tort duties and federal labeling requirements applicable to the Manufacturers." *Id*. Under state law, a drug manufacturer that is or should be aware of its product's danger has a duty to label that product in a way that renders

it reasonably safe. *Id*. The plaintiffs alleged that the manufacturers "knew or should have known of the high risk of tardive dyskinesia inherent in the long-term use of their product" and "that their labels did not adequately warn of that risk." *Id*. at 2574. Therefore, "if these allegations are true, state law required the Manufacturers to use a different, safer label." *Id*.

The Supreme Court noted that brand name manufacturers have the ability to strengthen their warnings by using different, safer labeling, but critically, generic manufacturers do not. *PLIVA,* 131 S.Ct. at 2575. Specifically, the FDA's "changes-being-effected" (CBE) process allowed the name brand manufacturers to change their labels when necessary. *Id*. at 2574. "The CBE process permits [name brand] drug manufacturers to "add or strengthen a contraindication, warning, [or] precaution," or to "add or strengthen an instruction about dosage and administration that is intended to increase the safe use of the drug product," *Id*. (citing § 314.70(c)(6)(iii)(C); 21 CFR § 314.70(c)(6)(iii)(A)(2006)).

Generic manufacturers do not have the ability to change their labeling to include additional warnings because the CBE process is not available to them. *Id*. at 2575. The FDA informed the Court that it "interprets the CBE regulation to allow changes to generic drug labels only when a generic drug manufacturer changes its label to match an updated brand-name label or to follow the FDA's instructions." *Id*. at 2574-75. The FDA advised further that a generic manufacturer cannot use CBE changes to strengthen a generic drug's warning label, because doing so would violate the statutes and regulations requiring a generic drug's label to match its brand-name counterpart's, rendering it "no longer consistent with that for [the brand-name drug].'" *Id*. (citations omitted). The Court "conclude[d] that the CBE process was not open to [the generic drug] Manufacturers for the sort of change required by state law" and that generic manufacturers are not permitted to add additional warnings to their labeling. *Id*. at 2575.

The Supreme Court also held that generic manufacturers could not issue warnings separate from the drug's labeling. The Supreme Court noted that the FDA considers separate warnings, known in the industry as "Dear Doctor" letters, to be a form of "labeling." *Id*. at 2576 (citing 21 U.S.C. § 321(m); 21 CFR § 202.1(l)(2)). "[A]ny such letters must be 'consistent with and not contrary to [the drug's] approved . . . labeling.'" *Id*. (citing 21 CFR § 201.100(d)(1)). The FDA argued, and the Supreme Court agreed, that "if generic drug manufacturers, but not the brand-name manufacturer, sent such letters, that would inaccurately imply a therapeutic difference between the brand and generic drugs and thus could be impermissibly "misleading." *Id*. (citing 21 CFR § 314.150(b)(3)). Therefore, the Court held that "federal law did not permit [generic drug m]anufacturers to issue additional warnings through Dear Doctor letters." *Id*.

Because federal law prohibits generic drug manufacturers from issuing warnings that are different from those of the name brand drug, federal law preempts any state law claims alleging that the generic manufacturer failed to warn. "The Supremacy Clause establishes that federal law 'shall be the supreme Law of the Land . . . anything in the Constitution or Laws of any State to the contrary notwithstanding.'" *Id*. (quoting U.S. Const., Art. VI, cl. 2). "Where state and federal law 'directly conflict,' state law must give way." *Id*. "[S]tate and federal law conflict where it is 'impossible for a private party to comply with both state and federal requirements.'" *Id*. (citing *Freightliner Corp. v. Myrick*, 514 U.S. 280, 287 (1995)). The Supreme Court explained, "We find impossibility here. It was not lawful under federal law for the Manufacturers to do what state law required of them." *Id*. at 2577. The Court reasoned, "If the Manufacturers had independently changed their labels to satisfy their state-law duty, they would have violated federal law." *Id.* However, federal law "demand[s] that generic drug labels be the same at all times as the corresponding brand-name drug labels. *Id.* (citing 21 CFR § 314.150(b)(10)). "Thus, it was impossible for the Manufacturers to comply with both their state-law duty to change the label and their federal law duty to keep the label the same." *Id*. at 2577-78. Therefore, insofar as generic drugs are concerned, state "failure to warn" tort claims are preempted and cannot be pursued. *Id*.

Finally, the Supreme Court rejected the plaintiff's argument that a generic drug manufacturer could request that FDA permit it to issue a stronger warning. *Id*. at 2578. Even if doing so would have satisfied a federal requirement, "it would not have satisfied their state tort-law duty to provide adequate labeling." *Id*. at 2578. The Supreme Court observed, if a generic manufacturer had requested a stronger warning, the FDA *might* have negotiated with the name brand manufacturer, and *might* have decided that a stronger warning was required. *Id*. Therefore, if a generic manufacturer asked the FDA for a stronger warning, the Supreme Court speculated that it is possible that this "would have started a Mouse Trap game" that would lead to a stronger warning label. *Id.* However, the Supreme Court held that this possibility is not enough to overcome preemption because "accepting this argument would render conflict pre-emption largely meaningless because it would make most conflicts between state and federal law illusory." *Id*. at 2579. "If these conjectures suffice to prevent federal and state law from conflicting for Supremacy Clause purposes," it would not be clear when the Supremacy Clause would have any force. Therefore, the Supreme Court held that a plaintiff cannot argue an alleged violation of a duty to report to the FDA. *Id*.

The *PLIVA* decision severely limited plaintiffs' ability to pursue claims against generic drug manufacturers. All prescription drugs have beneficial effects and side effects. That is why they are only available by prescription. A learned intermediary such as a physician is required to evaluate a patient and to determine whether the benefits of the drug outweigh the potential side effects. However, the PLIVA decision left open the question of whether its rationale would also apply in design defect claims. That question was answered in *Mutual Pharmaceutical v. Bartlett*.

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C. *Mutual Pharmaceutical Co., Inc. v. Bartlett* Holds That State Law Defective Design Claims Against Generic Manufacturers Are Also Preempted.

The plaintiff in *Mutual Pharmaceutical Co., Inc. v. Bartlett*, ___ U.S. ___, ___ S.Ct. ____ 2013 WL 3155230 (Jun. 24, 2013) was prescribed sulindac, a non-steroidal anti-inflammatory drug (NSAID). *Id*. at *5. The pharmacist filled her prescription with a generic form that was manufactured by Mutual Pharmaceutical Co., Inc. *Id*. Plaintiff developed an acute case of toxic epidermal necrolysis which required her to spend months in a medically-induced coma, undergo twelve surgeries, and which resulted in disfigurement and near blindness. *Id*. Bartlett sued Mutual Pharmaceutical in New Hampshire state court on various causes of action including strict products liability. Mutual Pharmaceutical removed the case to federal court. The jury found it liable on respondent's design-defect claim and awarded her over $21 million. *Id*. The First Circuit affirmed, finding that neither the FDCA nor the FDA's regulations pre-empted respondent's design-defect claim, and distinguishing *PLIVA*, *supra*, by theorizing that generic manufacturers facing design-defect claims could comply with both federal and state law simply by choosing not to sell the drug at all. *Id*. at *6 (the "stop selling" theory).

The Supreme Court of the United States reversed, holding that Bartlett's state law design defect cause of action was preempted by federal law. Bartlett argued that her New Hampshire strict products liability cause of action imposed no state law duties on Mutual Pharmaceutical because the purpose of strict liability claims is not regulatory, but compensatory. *Id*. at *7. She further argued that even if it did, the duty did not encompass a duty to change the drug's design or its labeling. *Id*. at *8. The court rejected this argument, holding that state law did impose affirmative duties, and noting that in New Hampshire to determine whether a product is "unreasonably dangerous", the New Hampshire Supreme Court requires a "'risk-utility' approach" under which a product is defective in its design "'if the magnitude of the danger outweighs the utility of the product.'" *Id*. (quoting *Vautour v. Body Masters Sports Indus., Inc*., 784 A.2d 1178, 1182 (NH 2001). Three factors are relevant to that analysis: the product's desirability and usefulness to the public, whether the risk of the product could be reduced without a significant effect on its usefulness or manufacturing cost, and whether an efficacious warning was present to warn of unavoidable risks from foreseeable uses and hidden dangers. In the case of one molecule generic prescription drugs, increases in the drug's usefulness and decreasing the risk of harm would require the drug to be redesigned, which is impossible for two reasons. First, if the drug's molecular structure were changed, it would no longer be the same drug. It would be something different. *Id*. Second, generic pharmaceutical manufacturers are forbidden from altering the active ingredient's structure, because doing so would require the filing of a new drug application. Therefore, the Supreme Court reasoned, the only option under New Hampshire's three-part test would have been to strengthen the warning label which, as *PLIVA* made clear, generic manufacturers are forbidden from unilaterally doing. *Id*. at *9.

The Supreme Court also rejected the "stop selling" theory relied upon by the Court of Appeals for the First Circuit. *Id*. at *10. It noted that if federal preemption could be defeated simply because a manufacturer could choose to stop selling a product in a particular state, conflict preemption would be rendered "'all but meaningless.'" *PLIVA*, 131 S.Ct. at 2579. Indeed, if that were a viable theory, it would have applied in *PLIVA* as well. *Mutual Pharmaceutical*, 2013 WL 3155230 at *10. If the "stop selling" theory were viable, it "would mean not only that *PLIVA*, but also the vast majority – if not all – of the cases in which the Court has found impossibility preemption, were wrongly decided." *Id*. at *11.

Therefore, the Court held "that state-law design defect claims like New Hampshire's that place a duty on a manufacturer to render a drug safer by either altering its composition or altering its labeling are in conflict with federal laws that prohibit manufacturers [of generic prescription drugs] from unilaterally altering drug composition or labeling." *Id*. While the plaintiff's "situation is tragic and evokes deep sympathy, a straightforward application of pre-emption law requires that the judgment below be reversed." *Id*. at 12.

The Supreme Court's observation that design claims do not make sense with regard to prescription drugs is correct. Drug and Device Law provided the following example which illustrates the point: if the most commonly known molecule, H20, were "redesigned" by adding an additional oxygen molecule, it would no longer be water. It would be hydrogen peroxide. The Supreme Court's holding on preemption provides another basis to seek dismissal of design-based claims.

D. Pennsylvania Law Limits the Causes of Action That Can Be Pursued Against Prescription Drug Manufacturers.

Even before *PLIVA* and *Mutual Pharmaceutical* were decided, Pennsylvania law permitted personal injury claims concerning prescription drugs under a more limited set of circumstances than some other states.

Pennsylvania law does not permit strict products liability claims to be asserted against alleged manufacturers of prescription pharmaceuticals. See, e.g., *Hahn v. Richter*, 673 A.2d 888, 891 (Pa. 1996) (citing *Mazur v. Merck & Co., Inc*., 964 F.2d 1348, 1353-55 (3d. Cir. 1992), *cert. denied*, 506 U.S. 974 (1992)); *Aaron v. Wyeth*, 2010 WL 653985 (W.D. Pa. Feb. 19, 2010) (dismissing all non-negligence based claims, including strict products liability); *Colaccio v. Apotex, Inc*., 432 F. Supp.2d 514, (E.D. Pa. 2006); *Kester v. Zimmer Holdings, Inc*., 2010 WL 2696467 (W.D. Pa. June 16, 2010).

Similarly, Pennsylvania courts do not permit plaintiffs to pursue theories of breach of implied warranties of

merchantability and fitness for a particular purpose in prescription drug claims. *See, e.g.*, *Makripodis by Makripodis v. Merril-Dow Pharmaceuticals, Inc.*, 523 A.2d 374 (Pa. Super. 1987). "The essence of the warranty of merchantability is that the item sold is fit for the ordinary purposes for which such goods are used. *Id*. at 376 (citations omitted). Prescription drugs "are not available to the general public but may be obtained only upon the prescription of a licensed physician." *Id*. "This restriction on the availability of such drugs has been imposed because of the inherently dangerous properties of such drugs." *Id*. Because "[p]rescription drugs may pose a threat to the safety of certain identifiable segments of the public, or may be dangerous when used in conjunction with other drugs or substances, or may be harmful if taken by persons suffering from certain diseases or conditions," prescription drugs "are quite incapable of being made safe for their intended and ordinary use." *Id*. at 377. Therefore, "the very nature of prescription drugs precludes a warranty of fitness for 'ordinary purposes', as each individual for whom they are prescribed is a unique organism[.]" *Id*. *See also Kester v. Zimmer Holdings, Inc.*, 2010 WL 2696467 at *11 (W.D. Pa. June 16, 2010) ("Pennsylvania courts have held that the nature of prescription drugs and prescription medical devices precludes claims for breach of implied warranty."); *Colaccio v. Apotex, Inc.*, 432 F. Supp.2d 514, 547 (E.D. Pa. 2006); *Kline v. Pfizer, Inc.*, 2008 WL 4787577 (E.D. Pa. Oct. 31, 2008).

E. A Limited Number of Causes of Action Remain Viable Against Generic Pharmaceutical Manufacturers in Pennsylvania in the Wake of *PLIVA* and *Mutual Pharmaceutical*.

Between the preemption of claims concerning the adequacy of the warnings and the drug's design and the limitations on causes of action imposed by Pennsylvania law, plaintiffs could only bring claims against manufacturers of generic drugs under a fairly limited range of circumstances.

Negligent manufacture claims remain viable against manufacturers of generic prescription drugs. If, for example, negligence in the manufacturing process resulted in the presence of a contaminant that caused harm, such a claim would not be preempted. Similarly, if negligence in the manufacturing process resulted in a molecule different from the molecular structure of the approved reference listed drug, that too could result in liability.

A negligent failure to warn claim could be viable if the reference listed name brand drug manufacturer amends its package insert to strengthen a warning of a particular side effect and the generic manufacturer fails to update its own labeling to be consistent with the updated name brand labeling. While a generic manufacturer cannot unilaterally change its labeling to add a warning that is not present on the labeling of the reference listed drug, generics are required to update their labeling when the reference listed drug manufacturer updates its labeling. When the name brand manufacturer strengthens its warnings, FDA will accept changes being effected - special supplement submissions to make the ANDA generic drug's labeling "the same" as the revisions to the RLD's labeling. *FDA's Guidance for Industry, Revising ANDA Labeling Following Revision of the RLD Labeling, May, 2000.* If a generic manufacturer fails to do so, and a user of a generic drug develops the condition that is the subject of the strengthened warning on the name brand product, then a resulting failure to warn claim may not be preempted. *See Lyman v. Pfizer*, 2012 U.S. Dist. LEXIS 13185 (D. Vt. 2012).

It is more difficult to conceive of a negligent design claim that would fall outside the scope of federal preemption. As noted above, federal law requires that generic drugs use the same active ingredient, dosages and labeling as the approved name brand drug. The inactive ingredients do not necessarily need to be identical to those used in the name brand product. The federal requirement of "sameness" does not apply to the inactive ingredients. However, the issue of "bioequivalence" remains. The generic drug is bioequivalent to the name brand drug on which it is based if there is an "absence of a significant difference in the rate and extent to which the active ingredient . . . becomes available at the site of drug action[.]" 21 CFR § 320.1(e). Regardless of differences between the inactive ingredients used in a generic product and those used in the name brand drug, a plaintiff would have to prove that there was a "significant" difference between the rate of availability in the generic drug as compared to the name brand drug, and that difference caused the harm. In the absence of such a difference, a claim would be preempted, because of the federal obligation of producing a bioequivalent product. While a non-preempted design claim could exist in theory, such a case is unlikely to manifest itself in practice because it could only occur in a very narrow range of circumstances.

F. Conclusion

The Supreme Court's decisions in *Mutual Pharmaceutical* and *PLIVA*, as well as Pennsylvania's own limitations on claims against prescription drug manufacturers, provide a number of bases to seek dismissal as a matter of law for your generic drug manufacturing clients at an early stage.

IN TWO SIGNIFICANT DECISIONS, THE UNITED STATES SUPREME COURT ADDRESSES EMPLOYMENT LAW ISSUES REGARDING THE PLAINTIFF'S BURDEN OF PROOF IN RETALIATION CLAIMS AND EMPLOYER LIABILITY FOR SUPERVISOR CONDUCT

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The United States Supreme Court recently ruled on long anticipated civil rights decisions regarding the federal Voting Rights Act and state and federal laws concerning same sex marriage. Unfortunately, those decisions overshadowed two important employment law cases that the Court issued at the same time that many employers were anxiously waiting to hear the results of. Employers are now breathing a sigh of relief in light of the outcomes in *University of Texas Southwestern Medical Center v. Nassar*, ____ U.S. ____ , 2013 WL 3155234 (June 24, 2013), and *Vance v. Ball State University*, ____ U.S. ____, 2013 WL 3155228 (June 24, 2013). In *Nassar*, the United States Supreme Court determined that under Title VII, employee retaliation claims must be proven under the stricter "but-for" causation test and not under the less burdensome "motivating factor" standard. In *Vance*, the Supreme Court decided that under Title VII, an employer's strict liability for workplace harassment by a "supervisor" requires that the supervisor be empowered by the employer to take tangible employment actions against the employee. While these decisions appear to provide significant benefits to employers defending claims involving these issues, those employers and the attorneys who represent them in employment law cases need to be alert for potential difficulties that may arise in the future as lower courts attempt to apply theses decisions to cases before them.

In *University of Texas Southwestern Medical Center v. Nassar*, the United States Supreme Court in a 5-4 decision split along ideological lines, the Court dealt with the issue of what constituted the proper burden of proof with respect to Title VII retaliation claims. Nassar, a Muslim physician of Middle Eastern descent, claimed that he was discriminated against because of his religion and ethnic heritage. In particular, Nassar asserted that he was subjected to scrutiny of his billing practices by Dr. Levine, his ultimate superior, even though she had previously assisted him in obtaining a promotion. Nassar claimed that this hostile work environment resulted in his constructive discharge from the University. He also alleged retaliation when he was denied the opportunity to continue working on the hospital staff apart from his University position because of his complaints of Levine's bias and harassment.

At trial, the jury found for Nassar on both claims. While the jury awarded back pay in excess of $400,000 and compensatory damages of $3 million, the trial court reduced the award of compensatory damages to $300,000. Although the Fifth Circuit Court of Appeals vacated the constructive discharge claim, that Court affirmed the verdict of the jury on the retaliation claim, holding that a retaliation claim only required a showing that retaliation was a motivating factor for the adverse employment action, not the "but-for" cause. The Supreme Court granted a petition for writ of certiorari to resolve the issue of the proper standard of proof to be used for such retaliation claims.

In *Nassar*, the Supreme Court, in an opinion written by Justice Kennedy, concluded that "[t]he text, structure, and history of Title VII demonstrate that a plaintiff making a retaliation claim under §2000e-3(a) must establish that his or her protected activity was a but-for cause of the alleged adverse action by the employer."

Under Title VII, an employee's status-based discrimination claim under §2000e-2(m), as amended in 1991, only requires that an employee show that discrimination was one of the employer's motives for the employment action to prove such a claim. Congress revised Title VII at that time, following the Supreme Court's decision in *Price Waterhouse v. Hopkins*, 490 U.S. 228 (1989), which established the burden-shifting framework used in many employment discrimination claims and the but-for standard of proof for adverse employment actions. The Court in *Nassar* described the burden of proof established in *Price Waterhouse* as whether the employer "could prove that it would have taken the same employment action in the absence of all discriminatory animus," which required a but-for cause of the employment decision. The 1991 amendment adopted in response to that decision provided that "an adverse employment practice is established when the complaining party demonstrates that race, color, religion, sex or national origin was a motivating factor for any employment practice, even though other factors also motivated the practice."

Significantly, the 1991 amendment did not refer to retaliation claims in any manner. Title VII's antiretaliation provision, §2000e-3(a) appears in an entirely different section of the law, stating that "[i]t shall be an unlawful employment practice for an employer to discriminate against any of his employees … because he has opposed any practice made an unlawful employment practice by this subchapter, or because he has made a charge, testified, assisted, or participated in any manner in an investigation, proceeding, or hearing under this subchapter." In that regard, the burden of proof is just like under the Age Discrimination in Employment Act (ADEA), which prohibits adverse employment actions "because of" age criteria. In *Gross v. FBL Financial Services, Inc.*, 557 U.S. 167 (2009), the Supreme Court concluded that the "because of . . . age" language in the ADEA required a but-for burden of proof relating to age discrimination claims. Accordingly, the Court concluded that

Title VII does not specifically adopt a motivating factor standard for retaliation claims in employment cases.

In addition, the Court asserted that since Congress specifically amended a different portion of Title VII in 1991 to apply to all types of unlawful employment actions, including retaliation claims, it must have intentionally omitted retaliation claims from the change in the burden of proof standard. For that reason, the Court wanted to give effect to that apparent Congressional intent. In addition, the Court indicated that just one year prior to the Title VII amendments, Congress had enacted the Americans with Disabilities Act in 1990, which included antiretaliation as part of its overall plan. For that reason, "the ADA shows that when Congress elected to address retaliation as part of a detailed statutory scheme, it did so in clear textual terms."

Finally, in light of the detailed and comprehensive structure of Title VII, the Court was unwilling to read into it any intent other than what the statute specifically set forth. Judicial interpretations of other discrimination laws that do not have such a precise statutory scheme are given broader latitude.

Significantly, the Court pointed to several pragmatic factors affecting employment litigation in refusing to adopt the lesser standard of proof. First, the number of retaliation claims submitted to the EEOC has almost doubled in the past fifteen years. Second, a reduced standard of proof would also encourage the filing of frivolous claims. The Court suggested that any employee who anticipates any type of legal employment action will be taken against him or her would be tempted to make a frivolous and unfounded claim of discrimination simply to "forestall that lawful action." Indeed, many employers and their counsel can point to anecdotal situations in which employees have made unfounded charges of discrimination to prevent undesired changes in employment circumstances. Finally, the Court referred to the difficulty that a lesser standard would impose on lower courts "to dismiss dubious claims at the summary judgment stage." That would increase the financial and reputational costs that an employer who did not retaliate would experience. Of course, the employer will have already incurred significant cost through administrative proceedings and discovery costs by the time that dispositive motions are filed.

Finally, this decision represents a significant blow to the authority of the EEOC. The Supreme Court specifically rejected the EEOC's interpretation of Title VII as contained in its guidance manual. The Court indicated that the EEOC's interpretation of the burden of proof was unpersuasive in that the manual failed "to address the specific provisions of this statutory scheme, coupled with the generic nature of its discussion of the causation standards for status-based discrimination and retaliation claims." Employers can potentially cite to the language from this portion of the decision in contending that other EEOC interpretations contrary to employer interests should not be followed.

In a strongly worded dissenting opinion, Justice Ginsburg rejected basically all of the Court's decision with respect to the text, structure, and history of Title VII. She reaches the opposite result on each point. Perhaps, her conclusion best summarizes her response to the majority's decision when she states:

> The Court holds, at odds with a solid line of decisions recognizing that retaliation is inextricably bound up with status-based discrimination, that § 2000e-2(m) excludes retaliation claims. It then reaches outside of Title VII to arrive at an interpretation of "because" that lacks sensitivity to the realities of life at work. In this endeavor, the Court is guided neither by precedent, nor by the aims of legislators who formulated and amended Title VII. Indeed, the Court appears driven by a zeal to reduce the number of retaliation claims filed against employers.

Against this background, we address the potential implications of the *Nassar* decision. First, from a practical aspect, this decision may not result in more summary judgment motions being decided in favor of employers. Indeed, the Supreme Court specifically rejected the University's request to enter judgment in its favor as a matter of law. Instead, that issue was remanded for the Fifth Circuit to review the facts of the case and apply this holding of the Court to those facts. If adoption of this stricter burden of proof would make it easier for lower courts to dismiss unfounded claims, the Supreme Court certainly did not make use of that change in the burden to grant judgment in favor of the employer. That raises the question whether other courts will similarly pass that responsibility on to juries for resolution.

A second factor to consider is whether Congress will amend Title VII as it did following the *Price Waterhouse* decision. Indeed, the dissent strongly encourages such Congressional action. Fortunately for employers, the political landscape on Capitol Hill is very different from the atmosphere that existed in 1991. In light of the difficulty in resolving other ideological issues, Congress may not take up the calling urged by Justice Ginsburg.

Moreover, in light of the Court's castigation of the EEOC's interpretation of the applicable burden of proof, we will need to wait for the EEOC's reaction and determination of how it will now administer retaliation claims. Initially, it may look to whether Congress is likely to take action to address this issue. Additionally, those EEOC investigators who have followed the lesser motivating factor standard for retaliation claims will not change overnight and are likely to follow the same analysis in the future. Furthermore, those employees filing retaliation claims are not likely to comprehend the changed burden of proof in *Nassar*. They are still likely to pursue such claims in increasing numbers.

Finally, we need to consider whether juries will in fact understand court instructions advising them of this stricter standard of proof and accurately apply it in trials, especially in cases also involving status-based discrimination claims that will still apply the lesser motivating factor standard. We already deal with inconsistencies among various federal employment statutes when making requests to the trial courts as to

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the manner in which to charge the jury. While state discrimination laws often follow judicial interpretation of similar federal statutes, we do not know whether that will necessarily occur in the context of retaliation claims. For example, the Pennsylvania Human Relations Act, 43 P.S. §955 includes retaliation claims in its enumeration of unlawful discriminatory practices. Subsection 955(d) prohibits an employer from discriminating "in any manner against any individual because such individual has opposed any practice forbidden by this act, or because such individual has made a charge, testified or assisted, in any manner, in any investigation, proceeding or hearing under this act." We need to consider whether this difference would require a different jury instruction for claims arising under the PHRA. If that occurs, juries and judges will need to deal with even more complicated permutations in retaliation claims.

Accordingly, while this decision is significant and should reduce the burden that employers face from retaliation claims, the Supreme Court has not given a pass to employers and their counsel on retaliation claims. We still need to see how this decision will be applied in practice.

On the same day that *Nassar* was decided, the Supreme Court also announced its decision in *Vance v. Ball State University*, ____ U.S. ____, 2013 WL 3155228 (June 24, 2013). In the *Vance* case, the Court attempted to establish a bright line test for determining an employer's strict liability under Title VII for workplace harassment by a supervisor. In order to impose such liability, the Court concluded the employer must have empowered the supervisor to take tangible employment actions against the employee.

Maetta Vance, an African-American woman, sued Ball State University on the basis that a fellow employee, Saundra Davis, a white woman, created a racially hostile work environment in violation of Title VII. In this case, Vance was a full-time catering assistant. Davis, the fellow employee, was a catering specialist. Among Vance's allegations of harassing conduct were complaints that Davis "gave her a hard time at work by glaring at her, slamming pots and pans around her, and intimidating her"; that she was "left alone in the kitchen with Davis, who smiled at her"; that Davis "blocked" her on an elevator and "stood there with her cart smiling"; and that Davis often gave her "weird" looks. In response to those complaints, Ball State did attempt to resolve Vance's issues. Accordingly, the district court determined that Ball State could not be held liable for negligence because it responded reasonably to the incidents of which it was aware.

Thus, the outcome of this case turned on the question of whether Ball State could be held strictly liable for the allegedly hostile work environment created by Davis. While Vance alleged in her complaint that Davis was her supervisor, the parties agreed that Davis did not have the power to hire, fire, demote, promote, transfer or discipline Vance in any manner. On that basis, the district court granted summary judgment in favor of Ball State since it determined that Ball State could not be vicariously liable for Davis' alleged actions because she could not take any tangible employment actions against Vance and was not her supervisor for purposes of Title VII. The Seventh Circuit affirmed that decision.

The Supreme Court, in another 5-4 ruling split along the same ideological lines, issued this employer-friendly decision. In claims of hostile work environment involving an employee's co-workers under Title VII, the law was clear that an employer can only be liable if it was negligent in controlling the work conditions. On the other hand, if the hostile work environment is created by a supervisor's harassment, the employer is strictly liable under **Burlington Industries, Inc. v. Ellerth,** 524 U.S. 742 (1998), and **Faragher v. Boca Raton,** 524 U.S. 775 (1998). *Ellerth* and *Faragher*, however, did not decide the issue of who is a supervisor for purposes of Title VII.

In this case, the Supreme Court held "that an employee is a 'supervisor' for purposes of vicarious liability under Title VII if he or she is empowered by the employer to take tangible employment actions against the employee."

In responding to Vance's argument that an expansive understanding of the concept of a "supervisor" is supported by both by general usage and in legal contexts, the Court found that "[i]n general usage, the term 'supervisor' lacks a sufficiently specific meaning to be helpful for present purposes" citing to both general dictionaries and to colloquial business authorities. In legal contexts, the Court also concluded that statutory definitions adopt varying duties. The Court also pointed out that the term "supervisor" is not used in Title VII, but instead was brought into this issue by the Court in *Ellerth* and *Faragher*. But in those cases, the Court "simply was not presented with the question of the degree of authority that an employee must have in order to be classified as a supervisor" and "[t]he parties did not focus on the issue in their briefs." In its review of the facts in those cases, the Supreme Court held that the framework set forth by those decisions supported a limited interpretation of who is considered a supervisor.

The Supreme Court specifically rejected the argument that an employer should have strict liability for employees who have the ability to direct co-workers' labor but do not have the authority to take employment actions. The Supreme Court declared:

> The interpretation of the concept of a supervisor that we adopt today is one that can be readily applied. In a great many cases, it will be known even before litigation is commenced whether an alleged harasser was a supervisor, and in others, the alleged harasser's status will become clear to both sides after discovery. Once this is known, the parties will be in a position to assess the strength of a case and to explore the possibility of resolving the dispute. Where this does not occur, supervisor status generally is capable of resolution at summary judgment. By contrast, under the approach advocated by Petitioner and EEOC, supervisor status would very often be murky -- as this case well illustrates.

Again, the Supreme Court specifically rejected the EEOC's definition of a supervisor, which it described as "a study in ambiguity" for a simpler, more practical approach. This determination responds to courts and commentators' request "for reasonably clear jury instructions in employment discrimination cases." The Court stressed that "[b]y simplifying the process of determining who is a supervisor (and by extension, which liability rules apply to a given set of facts), the approach that we take will help to ensure that juries return verdicts that reflect the application of the correct legal rules to the facts."

In its criticism of the EEOC Enforcement Guidance, the Court points out that "the EEOC takes the position that an employee, in order to be classified as a supervisor, must wield authority 'of sufficient magnitude so as to assist the harasser explicitly or implicitly in carrying out the harassment.'" The Supreme Court, however, correctly states that "*any* authority over the work of another employee provides at least some assistance." Furthermore, the government interprets the Guidance to mean that "the authority must exceed both an ill-defined temporal requirement (it must be more than 'occasiona[l]') and an ill-defined substantive requirement ('an employee who directs 'only a limited number of tasks or assignments' for another employee ... would not have sufficient authority to qualify as a supervisor.'" Those terms, however, have no clear meaning. As such, the Supreme Court noted that the EEOC Guidance did not satisfy the test set forth in *Skidmore v. Swift & Co.*, 323 U.S. 134 (1944), which only requires that courts give deference to administrative interpretations that have the power to persuade, which "depend[s] upon the thoroughness evident in its consideration, the validity of its reasoning, [and] its consistency with earlier and later pronouncements." In this case, the EEOC Guidance did not meet this level of persuasiveness.

In addition, the Court rejected the dissent's suggestion that this standard "would cause the plaintiffs to lose in a handful of cases involving shocking allegations of harassment" or how the legal outcome of those situations would hinge on the definition of "supervisor." Further, an employee would still have the ability to pursue such claims based on negligence of the employer. In those cases, "[e]vidence that an employer did not monitor the workplace, failed to respond to complaints, failed to provide a system for registering complaints, or effectively discouraged complaints from being filed would be relevant." Accordingly, employers could still be held responsible for their negligent conduct.

In addition, the proposed alternative approach would make matters far more complicated and difficult to procedurally administer and judicially resolve. "The complexity of the standard they favor would impede the resolution of the issue before trial. With the issue still open when trial commences, the parties would be compelled to present evidence and argument on supervisor status, the affirmative defense, and the question of negligence, and the jury would have to grapple with all those issues as well. In addition, it would often be necessary for the jury to be instructed about two very different paths of analysis, i.e., what to do if the alleged harasser was found to be a supervisor and what to do if the alleged harasser was found to be merely a co-worker."

Justice Ginsburg again wrote a dissenting opinion. For purposes of imposing strict liability on an employer, the dissent would allow such vicarious liability to be imposed for any "employees who control the day-to-day schedules and assignments of others" even if they do not have authority to take tangible employment actions. Instead, the dissent would adopt the approach to supervisory status under Title VII urged by the EEOC's Guidance which suggests that the authority to direct an employee's daily activities establishes supervisory capacity. While indicating that "[a] supervisor with authority to control subordinates' daily work is no less aided in his harassment than is a supervisor with authority to fire, demote, or transfer," the dissent misses the point that the real issue is whether the employer should be held liable for its *negligent* failure to prevent such behavior as opposed to *strict* liability for conduct that it may not even be aware is occurring. While criticizing the Court's decision for ignoring the reality of the workplace, the dissent actually fails to see the larger picture of the modern workplace. Indeed, the goal of discrimination laws should be to reduce discrimination in the workplace, not merely increase the opportunity for employees to recover increased damages. Increasing the cost of litigation undoubtedly takes away from funds that employers can expend on training to prevent such discrimination.

Unlike the *Nassar* decision, the Court's holding in *Vance* is more likely to have an immediate and demonstrable impact on employment law cases. First, *Vance* does have a clear standard that lower courts can apply in deciding motions to dismiss or for summary judgment. Thus, this decision is more likely to result in fewer cases proceeding to trial.

Second, the *Vance* holding is less likely to be overturned by Congress than the decision in *Nassar*. Congress already indicated a willingness to address the burden of proof issue when it modified Title VII following the *Price Waterhouse* decision. Since Congress failed to even define the term supervisor when it enacted Title VII, it is less likely to now address that aspect of the law.

Third, employers will be better able to analysis their potential liability for acts of their employees. While this examination may mean that employers will more clearly designate who can make tangible employment decisions, that outcome is not a bad thing. Indeed, it is likely that putting the authority to take tangible employment decisions in fewer, better trained individuals will result in less discriminatory actions being taken against employees. That will equally benefit employers and employees.

Undoubtedly, these pronouncements are not the final word on these issues. Indeed, each of these legal holdings warrants a full analysis of its implications. But for now, employers can take comfort in the Supreme Court's rulings in *Nassar* and *Vance*, which do appear to benefit them in employment litigation.

"YOU TALKIN TO ME?"
Waiver of Third Party Liability Under the WCA

By Jeffrey D. Snyder, Esquire and Kevin L. Connors, Esquire, Connors Law, LLP, Exton, PA

The Pennsylvania Supreme Court's recent decision in *Bowman v. Sunoco, Inc.*, ____ Pa. ____, 65 A.3d 901 (Pa., 2013) validates an agreement that an employee had entered into at the time of hiring. Under the agreement, the employee agreed that he/she would not bring a third-party claim or action against the employer's customers, in the event of a work injury that might otherwise have triggered consideration of third-party liability. Hey, we are talkin' to you!

Bowman involved a private security guard employed by Allied Barton Security Services, who had signed a workers' compensation disclaimer, under which she had waived her right to sue Allied's clients for damages related to any injuries that would otherwise be covered under the Pennsylvania Workers' Compensation Act.

The disclaimer stated:

> "I understand that state workers' compensation statutes cover work-related injuries that may be sustained by me. If I am injured on the job, I understand that I am required to notify my manager immediately. The manager will inform me of my state's workers' compensation law as it pertains to seeking medical treatment. This is to assure that reasonable medical treatment for an injury will be paid for by Allied workers' compensation insurance.
>
> As a result, and in consideration of Allied Security offering me employment, I hereby waive and forever release any and all rights that I may have to:
>
> - Make a claim, or
> - Commence a lawsuit, or
> - Recover damages for losses
>
> from or against any customer (and the employees of any customer) of Allied Security to which I may be assigned, arising from or related to injuries which are covered under the workers' compensation statues."

Falling on either snow or ice while providing security at a Sunoco refinery, the employee filed a workers' compensation benefits claim, and then received workers' compensation benefits pursuant to the Pennsylvania Workers' Compensation Act.

She then filed a negligence lawsuit against Sunoco, under which she alleged that Sunoco had been negligent in failing to maintain and inspect its premises, resulting in the employee sustaining her work-related injuries.

In the course of discovery in the personal injury lawsuit, the employee's disclaimer was produced. Sunoco argued that the employee's negligence claim had to be barred by the employee's voluntary disclaimer and waiver.

The employee argued that the disclaimer was void, claiming that it was contrary to public policy. Specifically, the employee argued that the disclaimer violated the public policy considerations embedded in Section 204(a) of the Workers' Compensation Act. Her argument was that the disclaimer improperly waived a cause of action that had not yet accrued.

Section 204(a) of the WCA sets forth:

> "No agreement, composition, or release of damages made before the date of any injury shall be valid or shall bar the claim for damages resulting therefrom; and any such agreement is declared to be against the public policy of this Commonwealth."

At the trial court level, the disclaimer was not found to have violated the public policies articulated in Section 204(a), with the trial court granting Sunoco's motion for judgment on the pleadings.

The employee appealed the trial court judgment to the Superior Court, with the Superior Court also agreeing that the disclaimer was not violative of public policy. The employee had waived only her right to sue third-party customers for injury covered by workers' compensation laws. The waiver/disclaimer was not an attempt to deprive her of rights under the Workers' Compensation Act; nor was it intended to shield the employer from liability, or to deprive the employee of compensation for any work-related harm or injuries.

The Supreme Court granted allocator to determine:

> "Did the Superior Court, in a decision of first impression of state-wide substantial significance, disregard the public policy of the Commonwealth of Pennsylvania and the plain meaning of the Pennsylvania Workers' Compensation Act when it decided that a third-party release in the form of a 'Workers' Comp Disclaimer', signed in consideration for employment or receipt of compensation benefits, which further required the waiver and eternal release of any and all rights to make a claim, commence a lawsuit, or recover damages or losses not void against public policy when the language of the disclaimer openly conflicts with the language of Section 204(a) of the Pennsylvania Workers' Compensation Act, which expressly renders such agreements as void against public policy?"

Before the Supreme Court, the employee argued that the disclaimer that she had signed violated the first sentence of Section 204(a) of the Pennsylvania Workers' Compensation Act. That sentence reads:

> "No agreement, composition, release of damages made before the date of any injury shall be valid or shall bar a claim for damages resulting therefrom; and any such agreements declared to be against public policy of this Commonwealth."

Arguing that the sentence was plain and unambiguous, the employee asked the Supreme Court to invalidate the disclaimer. A second basis for invalidation was asserted by the employee. She contended that the disclaimer clearly contravenes the

subrogation clause of Section 319 of the Pennsylvania Workers' Compensation Act, claiming that it was absurd for an employer to forego an opportunity to recoup expenses spent on an injured worker, effectively arguing that the negation of subrogation resulted in economic harm to her employer, Allied.

Sunoco responded by arguing that Section 204(a) only applied to an employer's attempts to limit its own liability for workers' compensation benefits and claims. It had no application to releases that might involve third parties, ones not governed by the well-muscled reach of the Pennsylvania Workers' Compensation Act.

Further arguing that the employee had never argued that the disclaimer was a contract of adhesion, or that it resulted from mistake, duress, fraud, or that it was either ambiguous or unsupported by consideration, Sunoco sought validation of the disclaimer, as waiver of any claim by the employee against it for personal injuries.

Dissecting Section 204(a) of the Pennsylvania Workers' Compensation Act, the Supreme Court, in a majority opinion authored by Justice Eakin, held that only the first sentence of Section 204(a) deals with public policy issues. The remaining sentences primarily discuss various sources and funds that an employee might receive, that might impact on the employee's receipt and entitlement to workers' compensation benefits.

Initially, the court recognized that the first sentence in Section 204(a) was not free from ambiguity. The Supreme Court then examined the inter-relationship between Article II of the Act, in which Section 204 is but one of five sections. That article related to the Pennsylvania Workers' Compensation Act as a whole. Article II is entitled "Damages by Action and Law". As had been observed by the Supreme Court in its 1999 decision *Fonner v. Shandon, Inc.,* 555 Pa. 370, 724 A.2d 903 (Pa.,1999) fundamental premise of the Pennsylvania Workers' Compensation Act is that the relations between the employee and the employer under the Act are essentially contractual in nature. The employee embraced the right of exclusive remedy, and the employer embraced the right of statutory immunity, establishing a duality of purpose inuring to the benefit of both parties.

Interpreting legislative history, the Supreme Court determined that the legislature had originally intended that the provisions of Section 204(a) would only apply to agreements between an employer and employee that might bar an employee's right to make a claim against their employer, and not, by extension, to bar claims against third parties.

Stripping away legislative ambiguities and contractual aversion, the Supreme Court held that the disclaimer and waiver entered into by the employee did not prevent the employee from receiving full and just compensation for her work-related injuries. The effective negation of the employer's potential right of subrogation, was a business decision that only affected Allied, and that it was not a deprivation of the employee's rights.

Another argument advanced by the employee was that the disclaimer/waiver contemplated actions that could only occur in the future. The court held that the disclaimer was a condition of employment, under which the parties, both the employee and employer, contemplated that it would affect future causes of action, as the disclaimer dictated how claims for work injuries would be handled in the future.

Holding that the employee was never forced to sign the disclaimer, and that the disclaimer did not prevent her from receiving workers' compensation benefits for her work-related injuries, the Supreme Court held that the disclaimer/waiver was merely a guarantee to the employer's customers that they would not be held legally responsible or liable for injuries sustained by Allied's employees.

Justice Eakin's opinion was joined in by Justices Castille, Saylor, Todd, and McCaffery.

A concurring opinion was issued by Justice Saylor, with Justice McCaffery joining in that concurring opinion.

The concurring opinion posed a "modest reservation", in the course of invoking the concept of a "double recovery", and the public policy reasons behind subrogation. Justice Saylor confessed to some circumspection about whether an injured employee is ever able to fully recover in tort where the recovery is diminished by compromise, settlement, litigation costs, and subrogation.

Justice Baer dissented, predicating the dissent on the first sentence of Section 204(a) of the Act being "clear and unambiguous", resulting in Justice Baer concluding that the disclaimer/waiver at issue clearly was prohibited by the plain language of that sentence.

Practical Tips:

Does the *Bowman* decision place employers who do not secure the *Bowman*-type disclaimer/waivers at a competitive disadvantage to employers who do not secure such a disclaimer or waiver?

Will these types of disclaimers raise questions as to the adequacy of consideration, a question that might arise, if someone already employed is asked to execute such a disclaimer/waiver, in the wake of *Bowman*?

Is it possible to argue that continued retention of employment is, in fact, adequate consideration for a *Bowman*-type disclaimer/waiver?

What if an employee refuses to sign the disclaimer/waiver?

What if an employee is terminated for refusing to sign the disclaimer/waiver?

And where do we begin to analyze the definition of either a "customer or client" under the disclaimer/waiver?

Given what is at stake by application of the *Bowman* rule, additional litigation is clearly forecast in the future with this novel issue.

NEGLIGENT SUPERVISION CLAIMS DO NOT CONSTITUTE AN OCCURRENCE AND DO NOT TRIGGER COVERAGE OR A DUTY TO DEFEND UNDER A CGL POLICY: *CALFAYAN CONSTR. ASSOCS. INC. V. ERIE INS. EXCH.,* NO. 00256, 2013 WL 1364003 (PA. CT. COM. PL. 2013)

By Wesley R. Payne, Esquire and Melanie M. Romero, White and Williams LLP, Philadelphia, PA

I. Introduction

In Pennsylvania, commercial general liability (CGL) insurers are relieved of the burden of defending and indemnifying contractually based construction defect claims cloaked in negligence allegations. In the past, complaints alleging claims of "faulty workmanship" or "construction defect" against an insured contractor or subcontractor often required the insurer to at least defend, if not outright indemnify, the claim even though the law and most CGL policies exclude coverage for claims by a customer against a contractor for breach of a contract or warranties. *See, Freestone v. New England Log Home, Inc.,* 819 A.2d 550, 553 (Pa. Super. 2003). However, not until its ruling in *Kvaerner v. Commercial Union Ins. Co.*, 589 Pa. 317, (2006), did the Pennsylvania Supreme Court make clear that coverage is not triggered by a faulty workmanship claim because such contractually based claims are not "occurrences" that qualify as "bodily injury" or "property damage" under the terms and conditions of a typical CGL policy. *Id*, 335-36 (2006). Thus, damage to the property as a result of poor workmanship does not constitute an occurrence and does not trigger coverage or a duty to defend under the policy.

II. Development of the Law

Over the past several years, the Pennsylvania state and federal courts have established the frame work for evaluating such claims. In *Millers Capital Ins. Co. v. Gambone Bros. Dev.*, 941 A.2d 706, 713 (Pa. Super. Ct. 2007), the Pennsylvania Superior Court considered whether foreseeable damage to property other than the contracted property resulting from the contractor's negligence would constitute an occurrence. The Superior Court determined, in line with *Kvaerner*, that the term "occurrence" in the CGL policy contemplated a degree of fortuity that does not accompany faulty workmanship. The *Gambone* court went on to find that natural and foreseeable acts, such as rainfall, which tend to exacerbate the damage caused initially by faulty workmanship, cannot be considered sufficiently fortuitous to constitute an "occurrence." *Id*. Therefore, the direct and foreseeable consequential damage caused by the faulty workmanship to property does not constitute an occurrence or trigger coverage under Pennsylvania law.

In *Transportation Ins. Co. v. C.F. Bordo*, 2009 U.S. Dist. LEXIS 27266 (M.D. Pa., March 30, 2009), the U.S. District Court for the Middle District of Pennsylvania considered a suit against a contractor brought by a homeowner who hired the company to repair the exterior of his home. The contractor attempted to re-characterize plaintiff's breach of implied warranty claims as tortious, rather than contractual in nature. Upon reviewing the matter the court rejected the argument and recognized that a CGL policy affords "coverage ... for tort liability for physical damages to others and not for contractual liability." *Id*. Citing *Kvaerner*, it held that for conduct to be accidental, it must be unexpected and proceeded to reinforce the concept that an "occurrence…implies a degree of fortuity that is not present in a claim for faulty workmanship." *Id.* Moreover, the court found that "the definition of 'accident' required establishing an 'occurrence' under the policies cannot be satisfied by claims based upon faulty workmanship. Therefore, pursuant to the 'gist of the action' doctrine, the contractually based claim could not be recast as a tort claim for the purposes of establishing an occurrence, triggering coverage under a CGL policy.

Later that same year the U.S. District Court, Eastern District of Pennsylvania in *Meridian Mut. Ins. Co. v. James Gilligan Builders*, 2009 WL 1704474, (E.D. Pa. June 18, 2009) examined a similar issue where a savvy plaintiff, in an attempt to circumvent *Kvaerner* and *Gambone*, pled the underlying case as a negligence matter and the contractor sought coverage for the purported negligence claim. Again, the insurer, pursuant to the gist of the action doctrine, argued that the allegations of the complaint did not meet that definition of negligence and were actually contractual claims. The court agreed and held that the gist of the action sounded in contract. After deeming the action as one for breach of contract, the court turned to whether an occurrence existed. The court found the faulty workmanship claims to be very similar to those in *Kvaerner* and *Gambone*, and that the insurer does not have a duty to defend the faulty workmanship claim. Thus, even when the underlying complaint attempts to argue negligence, as opposed to a breach of the contract, the courts have found that the action is a contract action, without an "occurrence" to trigger coverage under a CGL policy. *See, also, Erie Ins. Exchange v. Abbott Furnace*, 972 A. 2d 1232, 1238 (Pa. Super. Ct. 2009) (The gist of the action doctrine precluded coverage under the CGL policy when the allegation arose from the terms of the contract and not from the larger social policies embodied by the law of torts).

Next, the Third Circuit addressed the issue of an occurrence based upon consequential damages stemming from a contract in *Nationwide Mut. Ins. Co. v. CPB International*, 562 F. 3d 591, 598 (3d Cir. 2009). In this matter, CPB contended that, because the underlying

action alleged consequential damages, it fell within the coverage of the policy. The court rejected this argument and stated: "The precise holding of *Kvaerner* is limited to claims that "aver[ ] only property damage from poor workmanship to the work product itself." The foundation of that holding is that claims for faulty workmanship "simply do not present the degree of fortuity contemplated by the ordinary definition of 'accident' or its common judicial construction in this context." *Id*. Therefore, the contractual nature of the claim excluded coverage.

Finally, relying upon *Kvaerner*, *Gambone* and *CPB International*, the Third Circuit addressed the issue of coverage for construction defect claims in *Specialty Surfaces Intern., Inc. v. Continental Cas. Co.*, ____ F.3d ____, 2010 WL 2267197 (3d. Cir., 2010). The court confirmed that an insurer has no duty under Pennsylvania law to defend or indemnify a contractor under a CGL policy for claims based on faulty workmanship and resulting foreseeable damages – even where the damage extended beyond the insured's own work product. The court stated as follows:

> Continental was not required to defend Sprinturf because the allegations in the amended complaint do not support a determination that any damage was caused by an "occurrence." Any damages to Empire's own work product based on Empire's alleged negligence are claims of damage based on faulty workmanship. Because they are not caused by an accident, under *Kvaerner*, they are not a covered "occurrence" under the insurance policy. *See* 908 A.2d at 889-90.
>
> Sprinturf [Specialty Surfaces], however, argues that the damage to the subgrade, which was prepared by Trent Construction, was accidental, and thus constitutes a covered occurrence. This argument is foreclosed by the Superior Court's decision in *Gambone*, in which the court rejected a similar argument made by the insured. There, the insured alleged that there was "ancillary and accidental damage" caused by water leaks that resulted from faulty workmanship. 941 A.2d at 713. The insured argued that the water damage to the non-defective work constituted an occurrence under the policy. Relying on *Kvaerner*, the Superior Court rejected the argument that the damage caused by water leaks resulting from faulty workmanship was an occurrence. The court observed that the *Kvaerner* court's emphasis on the 'degree of fortuity' "suggested that natural and foreseeable acts, such as rainfall, which tend to exacerbate the damage, effect, or consequences caused *ab initio* by faulty workmanship also cannot be considered sufficiently fortuitous to constitute an 'occurrence' or 'accident' . . . ." *Id.* Thus, damages that are a reasonably foreseeable result of the faulty workmanship are also not covered under a commercial general liability policy. *Id.* at 713- 14; *see also CBP International*, 562 F.3d at 596-97.

Specialty Surfaces Intern., Inc., *supra*. Accordingly, the issue that poor workmanship did not constitute an occurrence appeared to be addressed and uniformly resolved at every potential level.

However, the issue of whether negligent supervision claims which are pled as torts may trigger an occurrence or at least a duty to defend under a CGL policy remained an open question until recently when the Philadelphia Court of Common Pleas addressed the issue in *Calfayan Constr. Assocs. Inc. v. Erie Ins. Exch.*, No. 00256, 2013 WL 1364003 (Pa. Ct. Com. Pl. 2013) decision. Again, many insurers, in an abundance of caution and to prevent a potentially viable bad faith claim, would at least defend these claims under a reservation of rights. But the Philadelphia Court of Common Pleas Commerce has answered the question and added certainty to the law in this area.

III. *Calfayan Constr. Assocs. Inc. v. Erie Ins. Exch.*, No. 00256, 2013 WL 1364003 (Pa. Ct. Com. Pl. 2013).

A. Facts and Procedural History of Calfayan

In *Calfayan*, Ms. Raymond and Mr. Garafolo entered into a construction agreement (herein the "underlying lawsuit") with Calfayan Construction Associates, Inc. In their complaint, Ms. Raymond and Mr. Garafolo alleged that Calfayan was liable for negligent construction and breach of contract. Calfayan was insured under a Fivestar Contractor's policy from its insurer, Erie, which included CGL coverage. When Calfayan presented the claim to its insurer, Erie denied coverage and stated that the claims of the underlying lawsuit did not fall within Calfayan's policy because "they do not allege that an occurrence caused property damage during the policy period."

Because Erie denied Calfayan coverage, Calfayan asserted a three-count complaint against Erie for breach of contract, bad faith, and an action for declaratory judgment, seeking at a minimum, the defense of the underlying negligent supervision claim. In response, Erie filed preliminary objections to Calfayan's complaint. The court sustained Erie's preliminary objections and denied all three of Calfayan's claims because there was no alleged "occurrence" that would require Erie to defend and provide coverage.

B. Discussion

In analyzing Calfayan's claims, the court began by reviewing the terms of Erie's policy. Under Erie's policy, coverage is triggered if an "occurrence" caused any "bodily injury" or "property damage". According to Erie's policy, an "occurrence" is defined as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." The court, however, emphasized that "property damage" does not include any loss, cost, or expense *to correct* any defective . . . work performed by [insured] or by any contractors or subcontractors." *Id*. at 3 (emphasis in original).

Arguing for coverage, Calfayan made two claims: 1) faulty workmanship is an "occurrence" that triggered coverage and 2) negligent supervision of subcontractors constituted "property damage." The court rejected Calfayan's first claim and adopted the *Kvaerner* court's treatment of claims that equated

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faulty workmanship as an "occurrence." As in *Kvaerner*, the court reasoned here that "property damage" caused by poor workmanship does not trigger an insurer's duty to defend because faulty workmanship is not an "occurrence" under Erie's policy. Most notably, the court also rejected Calfayan's second claim and held that negligent supervision of Calfayan's subcontractors did not constitute "property damage." Calfayan's duty to supervise the subcontractors arose from the contract. Erie's policy explicitly states that coverage is precluded for "corrective work by Calfayan or subcontractors working on Calfayan's behalf."

Because the court held that coverage was precluded for Calfayan, the court did not need to address Calfayan's bad faith claim. In short, if there is no basis for coverage there can be no basis for a bad faith denial of coverage.

IV. Conclusion

The immediate and narrow reading of *Calfayan* is that negligent supervision claims which are pled as a tort, like other poor workmanship claims, do not constitute an occurrence and do not trigger a duty to defend or indemnify the contractor. Claims that stem from the consumer's complaints of incomplete work, unsatisfactory work, damage caused by the contractors use of a defective products, or negligent supervision of subcontractors are actually extensions of the contractual liability. They are excluded contract claims. Characterizing the claims as torts will not morph the claim into a covered liability because Pennsylvania courts have demonstrated a firm stance and consistent pattern in essentially ruling that insureds and insureds' subcontractors should mainly be held accountable in contract for the quality of their work product. Therefore, insurers can evaluate these types of claims, including negligent supervision claims, assured that viable bad faith claims are not lurking in the future for denying such claims, whether pleaded in contract or tort.

A slightly more expansive view of the cases as a whole may indicate that a contractor's and/or policyholder's inadequate contractual performance cannot rise to the level of an occurrence, the threshold for coverage under the typical CGL policy. Furthermore, re-characterizing the claims as tort claims, pursuant to the gist of the action doctrine, is insufficient to breach the threshold of an occurrence. Accordingly, when advising clients with respect to coverage, counsel should be cognizant of the fact that the basis of the claim, and not merely the nature of the claim as pled, may determine if there is an "occurrence," triggering a duty to defend or coverage under a CGL policy.

PENNSYLVANIA EMPLOYMENT LAW UPDATE

By Lee C. Durivage, Esquire, Marshall Dennehey Warner Coleman & Goggin, Philadelphia, PA

The Supreme Court found that a potential collective action pursuant to the Fair Labor Standards Act became moot when the only plaintiff received an offer of judgment representing full relief for plaintiff's claim.

Symczyk v. Genesis Healthcare Corp., 2011 U.S. App. LEXIS 18114 (3d. Cir. 3/31/11)

The plaintiff initiated a collective action on behalf of herself and all similarly situated individuals, alleging that the employer violated the Fair Labor Standards Act by implementing a policy subjecting certain employees to an automatic meal break deduction without regard to whether the employee performed compensable work during their break. Prior to the plaintiff's filing a motion for conditional certification and prior to any other potential plaintiff opting-in to the collective action, the employer submitted an offer of judgment to the plaintiff's attorney for the wages requested plus attorneys' fees, costs and expenses, which would be determined by the court. After the plaintiff failed to respond to the offer of judgment, the employer filed a motion to dismiss, arguing that the plaintiff "no longer had a personal stake or legally cognizant interest in the outcome of this action," which is required for subject matter jurisdiction under Article III of the United States Constitution. The plaintiff opposed the employer's motion, arguing that the employer was attempting to strategically "pick off" the named plaintiff before the court could consider a motion to certify the collective action. The district court, however, dismissed the lawsuit, holding that the offer of judgment fully satisfied the plaintiff's claim and, therefore, mooted her lawsuit.

On appeal, the Third Circuit reversed the lower court's decision and reasoned that "[d]epriving the parties and the court of a reasonable opportunity to deliberate on the merits of collection action 'conditional certification' frustrates the objectives served" under the Fair Labor Standards Act. As a result, the court held that "[a]bsent undue delay, when an FLSA plaintiff moves for 'certification' of a collective action, the appropriate course—particularly when a defendant makes a Rule 68 offer to the plaintiff that would have the possible effect of mooting the claim for collective relief asserted under [the FLSA]—is for the district court to relate the motion back to the filing of the initial complaint." Accordingly, the Third Circuit instructed the district court on remand to consider whether the plaintiff's potential motion for conditional certification was made without undue delay and, if no delay is found, should have the motion relate back to the initial filing of the complaint. In addition, if the court certifies the collective action and at least one other similarly situated employee opts in, then the employer's offer of judgment "would no longer satisfy the claims of

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everyone in the collective action, and the proffered rationale behind dismissing the complaint on jurisdictional grounds would no longer be applicable."

The Supreme Court, however, reversed the decision and concluded that the individual plaintiff's claim became moot after the offer of judgment was presented and further noted that the plaintiff did not have any personal interest in representing putative, unnamed claimants, or any other continuing interest that would preserve her lawsuit from mootness. In so holding, the Supreme Court rejected the notion that such a settlement would insulate such claims from review, reasoning that "[w]hile settlement may have the collateral effect of foreclosing unjoined claimants from having their right vindicated in respondent's suit, such putative plaintiffs remain free to vindicate their rights in their own suits [and]…are no less able to have their claims settled or adjudicated following respondent's suits than if her suits had never been filed at all." Significantly, the Supreme Court noted that both the district court and the Third Circuit found that the individual plaintiff's claim was rendered moot and, as a result, it declined to opine on whether this finding was correct as a matter of law and, further, declined to resolve the circuit split on this issue.

An officer and director of a closely held corporation was not an "employee" for purposes of Title VII and was, therefore, precluded from bringing a religious discrimination claim against the company.

Mariotti v. Mariotti Building Products, Inc., 2013 U.S. App. LEXIS 8610 (3d. Cir. 4/29/13)

The plaintiff filed a religious discrimination lawsuit, alleging he was harassed and terminated by a company that was initially founded by his father after the plaintiff had a "spiritual awakening" fourteen years prior to his termination. Specifically, the company was founded by the plaintiff's father in 1947, and the plaintiff and his brothers joined the business in the 1960s. The plaintiff was a vice-president and secretary of the company and was also a member of its board of directors. The plaintiff alleged that he delivered the eulogy at his father's funeral and commented on his own faith. Two days following the funeral, he received written notice that the shareholders had voted to terminate his employment, effective immediately. The plaintiff was advised, however, that his "share of any draws from the corporation or other entities will continue to be distributed to [him]." Further, the plaintiff remained a member of the board of directors for another eight months, when the shareholders did not re-elect him to the board of directors.

In rejecting the plaintiff's claim of religious discrimination, the Third Circuit held that the plaintiff was not an "employee" of the corporation. In so holding, the Third Circuit relied heavily on the Supreme Court's decision in *Clackamas Gastroenterology Associates, P.C. v. Wells*, *538 U.S. 440 (2003)*, which previously outlined six factors that were relevant to determine whether a shareholder-director was an employee of a public corporation pursuant to the Americans with Disabilities Act. Specifically, the factors included (1) whether the organization can hire or fire the individual or set the rules and regulations of the individual's work; (2) whether and, if so, to what extent the organization supervises the individual's work; (3) whether the individual reports to someone higher in the organization; (4) whether and, if so, to what extent the individual is able to influence the organization; (5) whether the parties intended that the individual be an employee, as expressed in written agreements or contracts; and (6) whether the individual shares in the profits, losses and liabilities of the organization.

Moreover, the Third Circuit expressly rejected the plaintiff's arguments that *Clackamas* should not be applied in his case because (a) it was not an ADA case and (b) it did not involve a professional corporation. Specifically, the Third Circuit noted that the definition of "employee" was the same in the ADA as it was in Title VII and that the nature of the business entity is simply an attribute of the employment relationship that must be considered in applying the *Clackamas* test to determine whether an individual is an employee or an employer. In applying the test to plaintiff's situation, the Third Circuit found it notable that the plaintiff continued to receive draws from the company after his alleged termination and that he remained a member of the board of directors for several months as well. As a result, the Third Circuit expressly noted that the plaintiff "fails to allege that he is the kind of person that the common law would consider an employee" and upheld the dismissal of his religious discrimination claim.

Plaintiff's belief that he answered a pre-employment screening question truthfully failed to establish that his termination was a pretext for disability discrimination.

Reilly v. Lehigh Valley Hospital, 2013 U.S. App. LEXIS 6364 (3d. Cir. 3/29/13)

The plaintiff alleged that he was discriminated against on the basis of his disability after he received medical treatment for an alleged work-related injury. Specifically, when the plaintiff received treatment for his alleged work injury, he informed the treating physician that he had a history of narcotics use and is a recovering drug addict. Following the treatment, the clinical report was submitted to the hospital's health services department, and that department noted that the plaintiff answered "no" in his employee health information form as to whether he has "ever been recognized as or diagnosed with alcoholism or drug addiction." As a result of the plaintiff's admission, the hospital terminated his employment. During the plaintiff's deposition, he testified that he did not believe he was untruthful because, although he attends weekly alcoholics' anonymous and narcotics anonymous meetings, the only "treatment" he received was court ordered following a DUI arrest. In upholding the dismissal of the plaintiff's claims, the Third Circuit noted that the only evidence of pretext argued by the plaintiff was that "he answered truthfully with regards to whether he ever received treatment for alcoholism or drug abuse." In so holding, the Third Circuit found that the plaintiff's "belief" as to whether

he answered the question truthfully was not the determinative factor because the "question is whether the decision maker at [the hospital] could regard [plaintiff's] responses as dishonest [and] [t]he answer to that question is resoundingly, 'yes.'" In particular, the court noted that the plaintiff admitted during his deposition testimony that he is a recovering alcoholic and drug addict but he, nonetheless, answered "no" to the question on his employment form.

Plaintiff cannot sustain a constructive discharge claim based upon one discriminatory comment and incident.

Hoff v. Spring House Tavern, 2013 U.S. Dist. LEXIS 78782 (E.D. Pa. 6/5/13)

The plaintiff asserted a hostile work environment and constructive discharge claim after he resigned from his employment in February 2010. Specifically, the plaintiff alleged that when he arrived to work, he inquired as to whether he had to move his truck from the parking lot. The plaintiff alleged that his co-worker, who was directing traffic at the time, replied, "Yes, you're lucky. If I had my white-hooded sheet on, I would have taken your…truck." The plaintiff believed his co-worker was making a reference to the Ku Klux Klan and informed his co-worker that he was offended by the comment. The plaintiff then complained about the comment to one of the owners, who later informed the plaintiff that she had terminated the co-worker as a result of the comment. A few minutes later, the owner informed the plaintiff that the co-worker would not be terminated and asked the plaintiff if he wanted to leave or stay. The plaintiff informed the owner that he did not feel comfortable working there, resigned and then filed a complaint of discrimination—alleging that he was constructively discharged. The court, however, disagreed and held that the plaintiff could not establish a constructive discharge claim as a matter of law. In so holding, the court reasoned that "[f]or a single incident to serve as the basis for a claim of constructive discharge, an employment discrimination plaintiff may simply face a more difficult burden of proof in establishing the employer's liability" and that "we cannot say the incident…, which constituted a single comment in a brief conversation, was so intolerable that a reasonable person in Plaintiff's position would feel compelled to resign."

Pennsylvania Supreme Court holds that a non-compete provision contained in an employment agreement was enforceable, despite the fact that the provision was not expressly referenced in the employee's offer letter.

Pulse Techs., Inc. v. Notaro, 2013 Pa. LEXIS 1097 (Pa. 5/29/13)

The Pennsylvania Supreme Court held that a restrictive covenant contained in an employment contract was valid and precluded the employee from continuing his employment with a competitor even though the initial offer letter provided to the employee did not reference the restrictive covenant. The employer hired the employee through a search firm. Following several interviews, the employee was offered a position with the employer. The two-and-one-half page formal offer of employment letter contained a "summary" of the employee's "intended position with [Pulse]" and provided a description of the position, job responsibilities, location, base salary and effective date. The offer letter further stated that "[y]ou will also be asked to sign our employment/confidentiality agreement" and "[w]e will not be able to employ you if you fail to do so." The offer letter further noted that "[y]ou will be required to sign an Employment Agreement with definitive terms and conditions outlining the offer terms and conditions contained herein" on the first day of employment. The offer letter did not, however, make any reference to a restrictive covenant.

On the first day of employment, the employee was presented with the employment/confidentiality agreement, which contained a non-competition restrictive covenant. The employee read, understood and did not voice any objection to the non-competition provision. Several years later, the employee learned of an open position with a competitor of Pulse Technologies. The employee informed the competitor of his non-compete agreement and accepted the position with an agreement that the competitor would indemnify him for legal fees in connection with any litigation regarding his non-compete agreement. The trial court granted a preliminary injunction in favor of the employer, but the Pennsylvania Superior Court reversed, stating that "restrictive covenant [the employer] sought to impose on [the employee] after he had commenced employment is precluded by the express limitation in the formal offer letter that the employment agreement to be signed on the first day of employment would only 'outline the offer terms and conditions contained herein.'"

The Pennsylvania Supreme Court, however, reversed the Superior Court's decision and held that the non-compete provision was valid. In so holding, the Pennsylvania Supreme Court reasoned that the offer letter was part of the hiring process and was not the actual employment contract. As a result, the "offer letter was not intended as nor sufficient to comprise the employment contract" and that the language of the offer letter makes "clear references to future specific terms [that] show[s] the offer letter is not a contract, but only evidence of negotiation." Finally, as the restrictive covenant was contained in the employment agreement, it was ancillary to the employee's commencement of employment and, therefore, supported by consideration.

The Third Circuit finds that an employee failed to establish a causal connection between her request for future leave and her termination when the employer immediately offered her a salary increase and suggested that she join its medical insurance plan when she informed the employer that she may have cancer.

Davis v. Davis Auto, Inc., 2013 U.S. App. LEXIS 870 (3d. Cir. 1/11/13)

The plaintiff alleged that she was retaliated against in violation of the ADA after she advised her employer that she may have cancer and may need time off in the future for medical treatments and was laid off approximately three

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months later. In affirming the decision that the plaintiff failed to establish a causal connection between her alleged protected activity and the employer's decision to terminate her employment, the Third Circuit noted that the plaintiff "[d]iscounts the undisputed fact that, once informed of the possibility that [plaintiff] could have cancer on July 7, 2008, the [employer's] immediate response was to suggest that she join the [company's] medical insurance plan and to offer her a $3.00 hour raise." Moreover, the Third Circuit further reasoned that the employer's cost reduction efforts, including the effect that it had on the employer's personnel, were well-documented on the record and, as a result, it found that no reasonable juror "[c]ould find that the [employer's] decision to terminate [plaintiff] was motivated in whole or in part by her request for time off to tend to her ailments." In particular, the Third Circuit expressly noted that the plaintiff's "[a]ttempts to claim retaliatory motives after [the employer] tried to support her by offering her a medical insurance plan to cover any cancer treatments and an hourly raise is patently frivolous." Significantly, the Third Circuit did not address whether the plaintiff's request for future time off was a protected "[r]equest for a reasonable accommodation." In light of the ADAAA's current focus on reasonably accommodating employees' disabilities and engaging in the interactive process, employers will have to continue to take note of whether a request for "future leave" will be deemed "protected activity" by the courts, resulting in further exposure of retaliation claims from these employees.

U.S. Steel's random drug and alcohol testing on probationary employees complies with the Americans with Disabilities Act.

Equal Employment Opportunity Commission v. United States Steel, 2013 U.S. Dist. LEXIS 22748 (W.D. Pa. 2/20/13)

The EEOC initiated a class action lawsuit, arguing that U.S. Steel's policy of conducting random drug and alcohol tests on its probationary employees violated the ADA when the employer did not have "[a]n individualized, reasonable suspicion of a safety concern." There, a probationary employee filed a charge of discrimination with the EEOC after she was terminated for failing a random alcohol screening examination. After receipt of the charge, the EEOC determined that the employer had a policy of randomly conducting drug and alcohol tests on its probationary employees. In rejecting the EEOC's claims, the court first noted that "[t]he EEOC did little actual investigation as to [the employee's] charge and whether U.S. Steel's policy could be justified by the business necessity exception." In particular, the court noted that the "EEOC… omitted to ask about the reasons for U.S. Steel's alcohol testing policy and never visited any U.S. Steel facility during the investigation." Rather, the "EEOC opted to rest on the assumption that random alcohol tests constituted a *per se* violation of the ADA."

Although the court determined that the EEOC complied with Title VII's multi-step enforcement procedures prior to filing the lawsuit, it nonetheless determined that the EEOC's claims of discrimination failed as a matter of law. Specifically, the court held that "U.S. Steel's policy of randomly testing probationary employees… is job-related and consistent with business necessity" and that the "[t]esting policy genuinely services [the] safety rationale and is no broader or more intrusive than necessary." In so holding, the court expressly noted that the "[u]ncontested facts in the record reveal that probationary employees are charged with performing dangerous and safety-sensitive duties alongside regular employees" and that in order to "[s]urvive a hazardous work environment that includes molten hot coke, toxic waste products, and massive moving machinery… employees must be alert at all times [and] [n]o level of intoxication is acceptable on the job in these circumstances." Indeed, the court noted that "[t]he possibility that employees would arrive at work intoxicated is not mere conjecture—its because it's a real problem at U.S. Steel's Gary Works plant in Indiana," which prompted the policy.

Moreover, the court noted that both U.S. Steel and the labor union representing the employees agreed to the policy, which further "[h]ighlights the consensus by all parties involved that such testing was consistent with maintaining workplace safety." In addition, in confirming that the policy's limitation to probationary employees was justified, the court found that "[c]ommon sense dictates that new hires would be comparatively less skilled at performing their jobs, are relatively unfamiliar with company rules, and would not have fully internalized the importance of workplace safety." As a result, the "[u]ntrained factory workers are inherently more dangerous to themselves as well as others because of their lack of training and familiarity with their job" and because "[t]here is no room for error when the dangers are as numerous and serious as in a coke plant," "[p]robationary employees are not 'similarly situated' with regular employees."

Court finds that a confidentiality provision in a Fair Labor Standards Act Settlement Agreement impermissibly frustrates the implementation of the FLSA.

Altenbach v. The Lube Ctr., Inc., 2013 U.S. Dist. LEXIS 1252 (M.D. Pa. 1/4/13)

The parties negotiated a resolution of a collective action pursuant to the Fair Labor Standards Act and sought the court's approval of the settlement agreement. In particular, the court noted that "[c]laims arising under the FLSA may be settled whether either the Secretary of Labor supervises an employer's payment of unpaid wages to employees or a district court enters a stipulated judgment after scrutinizing a proposed settlement for fairness." Although the court found that the settlement agreement was fair and reasonable, the court further determined that "[t]he Non-Publication provision impermissibly frustrates the implementation of the FLSA." Specifically, the court reasoned that, by including a confidentiality provision, the "[e]mployer thwarts the

informational objective of the notice requirement by silencing the employee who has vindicated a disputed FLSA right." In addition, the court found that a potential violation of the confidentiality provision—which would authorize the employer to recover damages from the plaintiff if the plaintiff discloses any information regarding the settlement to a third party—"[c]ontravenes the FLSA" because "[i]t permits [an employer] to retaliate against a plaintiff and promotes the silencing of an employee." As a result, while both parties often bargain for confidentiality in settlement agreements, courts have become increasingly hesitant to approve an agreement pursuant to the FLSA that has such a clause.

Plaintiff's ADA testing accommodation claim failed where the testing site attempted to implement accommodations but was interrupted when the plaintiff started a fire in the restroom.

Mahmood v. Nat'l Bd. of Med. Exam'rs, 2013 U.S. Dist. LEXIS 19811 (E.D. Pa. 1/14/13)

The plaintiff asserted that the defendant violated the ADA when it failed to "[r] easonably accommodate her visual impairment" at the time she sat for an examination. Specifically, the plaintiff requested several accommodations—including a larger computer monitor, magnifying software and additional time to take the examination—in August 2011, and the defendant agreed to provide the accommodations. On the day of the test, the defendant mistakenly seated the plaintiff in a private, special accommodations room but provided her with the other accommodations requested. However, during the examination, the test administrators were required to move the plaintiff to another room and, in the process of moving her computer monitor, the monitor stand broke, and the plaintiff alleged it was unusable. The test administrators attempted to fix the monitor stand. During this time, the plaintiff visited the restroom "[a]nd started a fire because she was depressed about the lack of adequate accommodations for the test and the looming seven-year deadline for passing the test." As a result, the plaintiff was arrested on charges of arson, and the defendant was unable to implement its practice of rescheduling the examination within the next few days (because she was in jail). In rejecting the plaintiff's claims, the court expressly noted that the plaintiff "[f]ail[ed] to establish that the delay she encountered… effectively resulted in a denial of her accommodations" and that "[c]ourts addressing delays in other contexts have found no ADA violation where an entity acts in good faith to provide an accommodation."

WORKERS' COMPENSATION UPDATE

By Francis X. Wickersham, Esquire, Marshall Dennehey Warner Coleman & Goggin, King of Prussia, PA

Pennsylvania Supreme Court decides to hear appeal in *Patton v. Worthington Construction*

The Pennsylvania Supreme Court has agreed to hear a general contractor's appeal in the case of *Patton v. Worthington Construction*.

The Supreme Court's decision is significant because the divided lower court in *Patton* essentially nullified Pennsylvania's long-standing statutory employer doctrine, which creates an employment relationship between a contractor and the employees of subcontractors, such that the employees are entitled to workers' compensation benefits from the contractor but, in exchange, the contractor receives the same workers' compensation immunity from tort liability that an actual employer receives. The doctrine operates primarily to immunize contractors on construction projects from tort lawsuits by the injured employees of subcontractors.

While the doctrine has been applied for more than 80 years based upon a straightforward application of a five-part test set forth by the Supreme Court in *McDonald v. Levinson Steel Co.*, 153 A. 424 (Pa. 1930), the lower court grafted an additional element onto the *McDonald* test that requires a fact-finder to determine whether the subcontractor's employee (the plaintiff) is also a common law employee or an independent contractor of the contractor.

However, this question can never be answered in a way that allows the statutory employer doctrine to apply, so it actually nullifies the doctrine. Specifically, if the fact-finder determines that the plaintiff is an actual employee of the contractor, the contractor is immunized as an actual employer and does not need statutory employer immunity. Likewise, if the plaintiff is an independent contractor, he by definition cannot be a statutory employee because the doctrine applies only to employees of subcontractors, not independent contractors. Consequently, although the lower court purported to apply the statutory employer doctrine, it actually nullified it.

Given that the Supreme Court grants only five percent of requests for appeal, its decision to review *Patton* is a major first-step toward reviving the statutory employer doctrine.

A Workers' Compensation Judge's suspension of the claimant's benefits based on evidence of her voluntary removal from the work force was appropriate even where the employer did not specifically request a suspension of benefits.

Jean Fitchett v. WCAB (School District of Philadelphia); 1713 C.D. 2011; filed 4/8/13; by Judge Simpson

The claimant worked for the employer as an instructional aide and was injured as a result of a student attack. The injury was acknowledged by a notice of compensation payable. Later, employer filed a termination petition alleging that the claimant fully recovered from her work-related injuries.

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During the litigation of that petition, the claimant testified that she began receiving pension benefits and Social Security Retirement benefits following the work injury. The claimant said that she accepted the benefits because she was impoverished by a lack of funds coming in from employment. The claimant also said she did not look for work after her injury, and when asked whether she considered herself retired, she responded, "Well, I'm collecting retirement." She also said that, if not for her injuries, she would have continued working.

The WCJ issued an interlocutory order, ordering the employer to reinstate the claimant's benefits as of the date the claimant returned an LIBC-760, which she claimed she never received. The judge further ordered that the employer was entitled to a credit for pension and Social Security Retirement benefits the claimant received against weekly compensation benefits. Ultimately, the judge granted the termination petition in part, denying the termination petition as to a left shoulder injury. However, the judge also ordered a suspension of benefits, finding that the claimant was essentially retired and had voluntarily withdrawn from the work force.

The Workers' Compensation Appeal Board (Board) affirmed the suspension of the claimant's benefits, as did the Commonwealth Court. The court held that, although the employer did not specifically request a suspension of benefits by filing such a petition, the claimant was, nevertheless, put on notice that a suspension of benefits was in play when the judge issued the interlocutory order and that it was proper to suspend benefits. According to the court, the claimant was not prejudiced when put on notice that a suspension was possible as she was given the opportunity to defend against the petition. Although the claimant testified that she planned to resume working when she was physically able to do so, the judge did not believe her. The Commonwealth Court further held that the employer was entitled to an offset, even though a notification of workers' compensation offset form was not sent to the claimant, because the offset was taken pursuant to a judge's decision, not unilaterally. Thus, the employer was not required to provide the claimant with prior notice of the offset.

A provider's fee review application cannot be barred by collateral estoppel where the hearing officer fails to conduct a hearing or address whether the insurer strictly complied with § 127.207 of the medical cost containment regulations.

Witkin v. Bureau of Workers' Compensation Fee Review Hearing Office (State Workers' Insurance Fund); 1313 C.D. 2012; filed 4/17/13; by Judge McCullough

In this case, the provider performed Therapeutic Magnetic Resonance (TMR) treatments on the claimant and billed them to the carrier at $3,298 per treatment. The carrier downcoded the procedure and paid the provider $26.24 per treatment. The provider then filed fee review applications with the Bureau disputing the amount that was paid. The Medical Fee Review Section of the Bureau held that proper reimbursement was made to the provider, who appealed by filing applications to a hearing officer. The hearing officer, without holding a hearing, dismissed the fee review applications, holding that the issue was identical to an issue that had already been fully adjudicated. The provider appealed to the Commonwealth Court.

The Commonwealth Court reversed the hearing officer's decision. The court held that the hearing officer improperly concluded that the provider's fee review application was barred by collateral estoppel because the hearing officer did not conduct a hearing or address whether the insurance carrier strictly complied with §127.207 of the regulations.

The Supreme Court holds that a claimant's receipt of pension benefits is not a presumption of retirement but is, instead, an inference that must be considered in connection with the totality of the circumstances.

City of Pittsburgh and UPMC Benefit Management Services, Inc. v. WCAB (Robinson); 18 WAP 2011; decided 3/25/13; by Chief Justice Castille

The Pennsylvania Supreme Court clarified the employer's burden of proof with respect to a petition to suspend benefits based on a claimant's retirement. In this case, the claimant started receiving a disability pension after her work injury. The employer then petitioned to suspend benefits, asserting the claimant had voluntarily removed herself from the work force and had not looked for a job in the general labor market. The claimant challenged the petition, presenting evidence that she was registered to work with the Pennsylvania Job Center but was not employed due to the unavailability of work and because the employer had eliminated a light-duty position that she had held.

The WCJ denied the petition, concluding that the claimant was forced into disability retirement when the light-duty position was eliminated. The Appeal Board affirmed, as did the Commonwealth Court. In affirming the decisions below, the court held that, in a petition based on the retirement of a claimant, the employer must show, by the totality of the circumstances, that the claimant has chosen not to return to the work force. In other words, the mere acceptance of a pension by a claimant does not equate with retirement.

The Supreme Court of Pennsylvania agreed with the Commonwealth Court and provided further clarification with respect to the employer's burden of proof in retirement cases. According to the court, where an employer challenges entitlement to continuing compensation on the grounds that the claimant has removed himself or herself from the work force by retiring, the employer has the burden of proving that the claimant has voluntarily left the work force. There is no presumption of retirement from the fact that a claimant seeks or accepts a pension. The acceptance of a pension entitles the employer to a permissive inference of retirement, and such an inference, on its own, is not sufficient evidence to establish retirement. The inference that arises from an acceptance of pension benefits must be considered in the context of the totality of the circumstances.

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