IN THE COMMONWEALTH COURT OF PENNSYLVANIA

M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania, Plaintiff	:
v.	:
Reliance Insurance Company, Defendant	: No. 269 M.D. 2001

RECEIVED AND FILED COMMONWEALTH COURT OF PA (PHILA)
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In RE: *Decision of Referee Tracy in the matter of Lugenbuhl, Wheaton, Peck, Rankin and Hubbard*

ORDER

AND NOW, this 3rd day of August, 2005, the Court has given consideration to the decision issued by Referee Frank Tracy in the matter of the objections of Lugenbuhl, Wheaton, Peck, Rankin and Hubbard to a notice of determination filed by the Statutory Liquidator of Reliance Insurance Company (Reliance) regarding a monetary claim against Reliance filed by Lugenbuhl, Wheaton, Peck, Rankin and Hubbard, and assigned Proof of Claim No. 1396936. The Court adopts the Referee's Report and Recommendation submitted to the Court and attached hereto and marked as Exhibit A. Accordingly, the Objections of Lugenbuhl, Wheaton, Peck, Rankin and Hubbard are hereby DISMISSED.

The Liquidator is directed to serve a copy of this Order upon all listed on the Master Service List and to file an affidavit of service with the Court indicating that service has been effectuated.

JAMES GARDNER COLINS, President Judge

IN THE COMMONWEALTH COURT OF PENNSYLVANIA

M. DIANE KOKEN, INSURANCE COMMISSIONER OF THE COMMONWEALTH OF PENNSYLVANIA	:	
v.	:	NO. 269 M.D. 2001
RELIANCE INSURANCE COMPANY	:	
IN RE PROOF OF CLAIM NO. 1396936 - LUGENBUHL, WHEATON, PECK, RANKIN & HUBBARD	:	

REFEREE'S REPORT AND RECOMMENDATIONS

HISTORY

This matter arises from the claim of Lugenbuhl, Wheaton, Peck, Ranking & Hubbard ("Lugenbuhl") a law firm in New Orleans, Louisiana, for unpaid legal services performed for and costs advanced to Reliance Insurance Company ("Reliance") in 2001. Lugenbuhl has filed a timely Proof of Claim in the amount of $72,064.62 and the Statutory Liquidator of Reliance Insurance Company ("Liquidator") has issued its Notice of Determination assigning Lugenbuhl's claim to a Class (e) priority in accordance with 40 P.S. §221.44(e). Lugenbuhl filed timely Objections to the Notice of Determination asserting that its claim should be accorded Class (a) priority. The Liquidator filed its Response to the Objections on October 31, 2003 and this matter was assigned to me by Order of the Court dated February 20, 2004 for the purpose of hearing the Objection to the Notice of Determination, submitting

EXHIBIT A

findings of fact where appropriate and necessary, and issuing a recommended decision regarding the Objection.

FACTS

The facts of this matter have been agreed upon by the parties and are set forth in a Stipulation of Agreed Facts submitted to me and appended hereto as Exhibit "A". These facts may be summarized as follows:

Lugenbuhl is a twenty (20) lawyer firm located in New Orleans, Louisiana. Reliance retained the services of Lugenbuhl to represent its interest in law suits brought against its insured, American Iron Reduction, LLC, and against Reliance directly, for damages arising from a shipboard explosion in the Atlantic Ocean on August 25, 1999 involving American Iron. During the course of its representation, Lugenbuhl performed various legal services for Reliance including hiring of experts, taking depositions, and attending settlement conferences abroad. Matters against Reliance were concluded by settlement, and matters against American Iron were stayed due to Chapter 11 bankruptcy protection.

The matter at hand involves two (2) unpaid invoices; the first dated March 30, 2001 in the amount of $69,830.62 for legal services rendered and costs advanced by Lugenbuhl during January and February of 2001, and the second dated May 15, 2001 in the amount of $2,234 for services performed during April 2001. There

was an intervening invoice dated April 11, 2001 for services performed during March 2001 which was paid in full. The March 30, 2001 invoice was not immediately paid because Reliance desired to conduct an audit of the charges in consideration of the large amount. The audit was completed on June 7, 2001. In the meantime, Reliance was placed in rehabilitation by Order of the Commonwealth Court dated May 29, 2001. That Order, inter alia, directed Reliance not to pay attorneys' fees or costs incurred prior to the issuance of its May 29, 2001 Order. Reliance was subsequently placed in liquidation by Order of the Commonwealth Court dated October 3, 2001.

It is not disputed that the legal services and costs advanced in this matter occurred prior to May 29, 2001, nor is the amount of the invoices or reasonableness of Lugenbuhl's charges for its services in dispute.

DISCUSSION

The only issue before me is determining the appropriate level of priority to be assigned the claim of Lugenbuhl for legal services and costs advanced. In that regard, the Liquidator asserts that Class (e) level of priority assigned to general creditors under the stature obtains. Lugenbuhl argues, however, that Class (a) level of priority which applies to costs and

expenses of administration is the appropriate level. In that regard, the relevant portion of the Statute provide:

> "The order of distribution of claims from the insurer's estate shall be in accordance with the order in which each class of claims is herein set forth. Every claim in each class shall be paid in full or adequate funds retained for such payment before the members of the next class receive any payment. No subclasses shall be established within any class.
>
> "(a) The costs and expenses of administration, including but not limited to the following: the actual and necessary costs of preserving or recovering the assets of the insurer; compensation for all services rendered in the liquidation; any necessary filing fees; the fees and mileage payable to witnesses; reasonable attorney's fees; the expenses of a guaranty association in handling claims. (Emphasis supplied)
>
> . . . .
>
> (e) Claims under nonassessable policies for unearned premium or other premium refunds and claims of general creditors. (Emphasis supplied)
>
> . . . ."

Lugenbuhl makes two (2) arguments that its claim qualifies for Class (a) priority. First it asserts that its services were in the nature of costs of preserving assets of the insurer because its legal representation of Reliance produced a very favorable settlement to Reliance effecting a considerable saving over its potential loss. There may be some technical merit to the concept that Lugenbuhl preserved Reliance assets by

obtaining a favorable settlement of legal claims against Reliance. However, under this statute costs of preserving assets are merely a subset of the general category of costs and expenses of administration. Further, administration can only mean administration of the insurer's assets while in statutory liquidation. Consequently, any legal fees incurred in preserving such assets to which 40 P.S. §221.44(a) applies must be incurred during and pursuant to the administration of the insurer's assets while in the hands of the Liquidator in the course of the liquidation proceedings. There is no dispute that the legal fees and costs advanced which are the subject of this claim were all incurred prior to the liquidation and in the ordinary course of Reliance's pre-liquidation business. Accordingly, these legal fees and costs advanced do not qualify for Class (a) priority under the statute as they are not costs or expenses of administration. Rather, Lugenbuhl stands in the position of a general creditor with respect to these legal fees and costs advanced and same are properly accorded a Class (e) priority.

The Court of Appeals of North Carolina was presented with a similar situation in State of North Carolina v. Interstate Casualty Insurance Company, 20 N.C. App. 743, 464 S.E. at 2d 73 (N.C. App. 1995). There the Court held that a claim for pre-rehabilitation services to the insolvent insurer could not be considered an expense of administration of the insurer's estate

because the insurer's estate was not in existence when the services were performed. The same result obtains here.

Next, Lugenbuhl makes the argument that because 40 P.S. §221.45(a) empowers the Liquidator to "comport, compromise or any other manner negotiate the amount for which claims will be recommended to the Court" the Liquidator has discretion to accord these particular legal fees Class (a) priority. Lugenbuhl goes on to assert that the Liquidator should exercise its discretion to recommend to the Court this claim as a Class (a) priority on principles of unjustly enrichment and equitable estoppel.

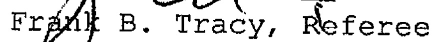
Lugenbuhl's reliance on 40 P.S. §221.45(a) is misplaced. From a reading of the plain language of the statute, it is clear that any discretion the Liquidator may have with respect to a claim goes to the amount of the claim, and not its priority status. Since the amount of Lugenbuhl's claim for legal services and reimbursement for costs is not in question, there is no basis for exercise of discretion under 40 P.S. §221.45(a) with respect to the claim. Moreover, Lugenbuhl presents no theories or authorities to show why a right to recovery for fees and costs advanced based on the principles of unjust enrichment or equitable estoppel provides an independent basis for assignment of its claim to any priority level other than that of a claim of a general creditor under 40 P.S. §221.44(e).

In consideration of the above analysis, it is clear that Lugenbuhl's claim for legal services and cost advanced is properly classified as a Class (e) priority level under 40 P.S. §221.44(e). This is consistent with the Commonwealth Court's Order and Memorandum Opinion issued by Judge Colins dated April 21, 2005 in the matter of Loeb & Loeb, LLP. There the claimant argued that its claim for legal services performed prior to liquidation should be accorded Class (b) priority afforded to "claims under policy for losses wherever incurred, including third party claims." Loeb asserted that because the legal service arose in the defense of an insured, it ought to be accorded this higher status. The Court rejected that notion noting that the legal fees incurred were not the responsibility of the insured and thus not a loss to the insured under the policy. Accordingly, the Court dismissed Loeb's objection and assigned its claim to a Class (e) priority level. Here, Lugenbuhl has presented no basis for assigning its claim for pre-liquidation legal services to Class (a) priority level, just as the claimant of Loeb was unable to substantiate classification of its pre-liquidation services to Class (b) priority level. Consequently, as in Loeb, Lugenbuhl's claim is properly assigned a Class (e) priority as a claim of a general creditor.

RECOMMENDATIONS

Based on the foregoing, it is recommended that the Objection of Lugenbuhl to the Notice of Determination assigning Class (e) priority level to the claim for legal services of Lugenbuhl should be dismissed and that the claim be assigned Class (e) priority under 40 P.S. §221.44(e).

Respectfully submitted,



Frank B. Tracy, Referee

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