

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

LOVELY G. CRANDALL, <u>et al.</u> ,	:	CIVIL ACTION
	:	
Plaintiffs,	:	No. 97-CV-957
	:	
v.	:	
	:	
ROBERT C. ALDERFER, JAMES W. APPEL,	:	
JOHN E. BARRY, LUTHER CAMPBELL, JR., M.	:	
SCOTT CLEMMENS, STANLEY E. HONIG, DAVID	:	
E. HOSLER, WILLIAM S. HUBER, NOAH W.	:	
KREIDER, JR., DONALD LECHNER, RICHARD	:	
B. NEILEY, JR., ROBERT L. SPANNIGER,	:	
G. ARTHUR WEAVER, ROBERT L. WECHTER,	:	
OLD GUARD MUTUAL INSURANCE COMPANY, OLD	:	
GUARD MUTUAL FIRE INSURANCE COMPANY, :	:	
GOSCHENHOPPEN-HOME MUTUAL INSURANCE	:	
COMPANY, & OLD GUARD GROUP, INC.,	:	
	:	
Defendants.	:	

MEMORANDUM

Green, S.J.

March 5 , 1999

Presently before this court is Defendants' Motion for Summary Judgment on the "State Action" Issue, Plaintiff's Reply in Opposition thereto and the parties' supplemental responses. Defendants' motion requests that Counts III and IV of the Complaint be dismissed pursuant to Fed.R.Civ.Pro. 56 (b). For the reasons set forth below, Defendants' motion will be granted.

Factual and Procedural Background

Defendants are the Old Guard Mutual Insurance Company, Old Guard Mutual Fire Insurance Company, Goshenhoppen-Home Mutual Insurance Company, Old Guard Group, Inc., (the "Insurance Companies") and several of the Insurance Companies' directors, in their individual capacities. Plaintiffs are both policyholders and, pursuant to a conversion plan adopted after the enactment of the Insurance Company Mutual-to-Stock Conversion Act (the

“New Conversion Act”), 40 P.S. § 911-A et seq., shareholders of the defendant Insurance Companies. The New Conversion Act, enacted in February 1996, repealed the original Mutual-to-Stock Conversion Act of 1920, 40 P.S. § 1010.1 et seq. The repealed statute provided a method for valuing an owner’s interest upon conversion from mutual to stock form and for the distribution of surplus to the policyholders. Id. § 1010.2. The New Conversion Act does not require such a valuation nor does it provide for or require any method of surplus distribution. 40 P.S. § 914-A (a)(2)(I)(B).

In March 1996, the Insurance Companies preliminarily met with their counsel and representatives of the Pennsylvania Insurance Department (the “Department”) to discuss an outline of their proposed conversion plan and the approval process. (Hr’g Tr., 13-15). This was the only meeting the Insurance Companies held with the Department. Id. In August 1996, pursuant to the New Conversion Act, the Insurance Companies filed a joint plan (the “Plan”) with the Department to convert the Insurance Companies from mutual to stock corporations. There is no evidence of any communication between defendants and the Department in the interim. After the expiration of the 60 day review period, the Department requested an extension of time to further review the Plan. Such an extension was agreed to by the Insurance Companies. The Insurance Commissioner approved the Plan in December 1996, expressly conditioned upon approval of the Plan by not less than two-thirds of voting policyholders. Id. After receiving the Department’s approval, the Insurance Companies subsequently forwarded notice of the Plan and notice of a meeting to vote on the Plan to policyholders. At a special meeting held in February 1997, the Plan was approved by more than two-thirds of the policyholders who had either voted in person or returned proxies in accordance with §§ 913-A(a) and 913-A(g) of the New Conversion Act.

Motion for Summary Judgment

Defendants moved for summary judgment on Counts III and IV of the Complaint asserting that neither the Insurance Companies nor their directors are “state actors” nor acted “under color of state law” and therefore cannot be liable under 42 U.S.C. § 1983 for converting from mutual to stock form. The parties requested an extended discovery period. After the close of the extended discovery period, oral argument was held on defendants’ motion for summary judgment. Defendants expounded upon their grounds for the motion and essentially maintained that the policyholders, free of state, statutory or regulatory mandate, voted to demutualize and convert to stock form. (See, Hr’g Tr., 4-6). Their main assertion is that the Department’s approval of actions initiated by private parties does not constitute state action. Such action, defendants assert, is merely acquiescence or approval of a state regulator, not compulsion or action rising to such a level as would constitute state action. Defendants further maintain that their activities in lobbying for the passage of the New Conversion Act are protected by the First Amendment. Plaintiffs did not challenge this contention at oral argument.

In Counts III and IV of the Complaint, plaintiffs allege that the Insurance Companies, acting under color of state law, deprived plaintiffs of their interests in the surplus of the converted companies and impaired their contracts. (Compl. at ¶¶ 51-56). Specifically, plaintiffs claim that as a result of the conversions, they were stripped of their right to receive surplus distributions without compensation and also had their contractual ownership rights interfered with by the Insurance Companies. (See, Pl.’s Mem. in Opp’n. at 1, 2). The complaint further avers that: (1) the Department was an active participant in the conversion; (2) the Insurance Companies worked closely with the Department in shaping the new conversion statute and obtaining its passage; (3) the Insurance Companies worked with the Department in preparing the Plan; and, (4) the Department placed its imprimatur on the Plan after finding that it did not prejudice policyholders’ rights. (See, id. at 3, 4). Plaintiffs contend that defendants could not have achieved their goal of conversion without the active involvement of the

Department. Id. Plaintiffs conclude that because of an alleged close nexus between the defendants and the Department, defendants should be considered state actors within the meaning of § 1983. Id.

During oral argument on defendants' motion, plaintiffs' primary contention was that the Department's finding that the Plan was fair and not prejudicial to policyholders contributed to, or aggravated, plaintiffs resulting harm. (Hr'g Tr., 18). Plaintiffs assert that because the Department approved defendants' allegedly defective proxy and subsequently the Plan, plaintiffs suffered an unlawful taking of their interests in the Insurance Companies' undistributed surplus. (Hr'g Tr., 15-19, 22). Consequently, plaintiffs maintain that because the private party defendants could not have succeeded in converting the companies without the active and affirmative involvement of the Department, they must be considered state actors.

Discussion

Summary judgment is mandated "against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case." Celotex Corp. v. Catrett, 47 U.S. 317, 321, 106 S.Ct. 2548, 2552 (1986). The moving party is therefore entitled to judgment as a matter of law because the non-movant has failed to make a sufficient showing on an essential element of his claim for which he has the burden of proof. Id.

Plaintiffs allege that "defendants acted under color of state law in adopting and implementing the plan of conversion such that their conduct may fairly be attributed to the Commonwealth." (Pl.'s Mem. in Opp'n. at 3). In order to survive a motion for summary judgment, plaintiffs must demonstrate either that defendants, none of whom are state officials or agencies, may be considered state actors or that they acted under color of state law within the purview of § 1983. As a matter of substantive constitutional law, the state-action requirement reflects judicial recognition of the fact that "most rights secured by the Constitution

are protected only against infringement by governments.” Lugar v. Edmondson Oil Co., Inc., 457 U.S. 922, 936, 102 S.Ct. 2744, 2753 (1982). Although private parties may cause the deprivation of rights, they may only be subjected to liability under § 1983 when they do so under color of state law. Mark v. Borough of Hatboro, 51 F.3d 1137, 1141 (3d Cir. 1995), cert. denied, 516 U.S. 858, 116 S.Ct. 165 (1995)(citing Flagg Bros., Inc. v. Brooks, 436 U.S. 149, 156, 98 S.Ct. 1729, 1733 (1978)). Determining whether there has been state action requires an inquiry into whether there is a sufficiently close nexus between the State and the challenged action so that the challenged action may be fairly treated as that of the State itself.” Blum v. Yaretsky, 457 U.S. 991, 1004, 102 S.Ct. 2764, 2786 (1982).

In Lugar, the Supreme Court set forth a general two-pronged test to determine when private action is attributable to the state under § 1983:

[T]he first question is whether the claimed deprivation has resulted from the exercise of a right or privilege having its source in state authority. The second question is whether, *under the facts of this case*, respondents, who are private parties, may be appropriately characterized as ‘state actors.’ (emphasis added).

Id., 457 U.S. at 939, 102 S.Ct. at 2755. In Mark, 51 F.3d at 1142, the Court of Appeals delineated three Lugar sub-tests to determine whether there has been state action: (1) whether the private entity has exercised powers that are traditionally in the exclusive prerogative of the state; (2) whether the private party has acted with the help of or in concert with state officials, and (3) whether the State has so far insinuated itself into a position of interdependence with the private party that it must be recognized as a joint participant in the challenged activity.

Defendants’ decision to adopt the Plan converting the Insurance Companies from mutual to stock form was an action initiated and implemented by private entities. Although plaintiffs claim the proxy forwarded to policyholders was defective, the allegedly defective and misleading proxy was provided to the Department by the private party defendants. After both an extended discovery period and after oral argument on defendants’ motion, plaintiffs have

failed to identify any evidence to support their numerous contentions that defendants should be considered state actors. In their Complaint and at oral argument, plaintiffs averred that: (1) the Department's determination that the Plan was fair and non-prejudicial contributed to plaintiffs' harm; (2) the Department was an active participant in the conversion; (3) defendants worked closely with the Department in both shaping the new statute and obtaining its passage; and, (4) defendants must be considered state actors as they could not have successfully converted the Insurance Companies without the Department's active involvement. Plaintiffs, as the nonmoving party, may not rely upon conclusory allegations in its pleadings or in memoranda and briefs to establish a genuine issue of material fact or element of their claim. See, Pastore v. Bell Telephone Co. of PA., 24 F.3d 508, 511 (3d Cir. 1994). The non-movant, instead, must establish the existence of every element essential to his case based on the affidavits or by the depositions and admissions on file. Id.

On summary judgment plaintiffs have not produced any evidence of intentional conduct by the defendant Insurance Companies nor by the Department which would demonstrate a sufficiently close nexus so as to consider them interdependent. Plaintiffs have not provided this court with any evidence of intentional conduct by the Department which in any way contributed to plaintiffs' harm. What is essentially complained of is that under the Old Conversion Act surplus would have been distributed to the plaintiffs and that defendants used the terms of the New Conversion Act to deprive plaintiffs of their right to the surplus. Clearly, the New Conversion Act does not require distribution of surplus, but rather leaves that determination to the companies upon a more than two-thirds vote of their policyholders. Plaintiffs' main assertion is that the defendants utilized the provisions of the New Conversion Act to better their respective positions while simultaneously depriving plaintiffs of just compensation. As the court stated in Jackson v. Metropolitan Edison Co., 419 U.S. 345, 355, 95 S.Ct. 449, 455 (1974) "...exercise of the choice allowed by state law where the initiative comes from [the defendant]

and not from the State, does not make its actions in doing so 'state action.'”

Conclusion

Because plaintiffs have not produced evidence on summary judgment that defendants' actions are properly attributable to the Commonwealth and have therefore failed to satisfy their evidentiary burden, defendants' motion for summary judgment on Counts III and IV of plaintiffs' complaint will be granted. This court will retain supplemental jurisdiction over plaintiffs' remaining state law claims pursuant to 28 U.S.C. § 1367.

An appropriate order follows.

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COMPANY, & OLD GUARD GROUP, INC.,	:	
	:	
Defendants.	:	

ORDER

AND NOW, this 5th day of March, 1999, IT IS HEREBY ORDERED that Defendants' Motion for Summary Judgment of the State Action Issue (Counts III and IV of the Complaint) is Granted.

IT IS FURTHER ORDERED that this Court shall retain supplemental jurisdiction over plaintiffs' remaining state law claims.

BY THE COURT:

CLIFFORD SCOTT GREEN, S.J.