BEFORE THE INSURANCE COMMISSIONER
OF THE
COMMONWEALTH OF PENNSYLVANIA

IN RE:	:	**ALLEGED VIOLATIONS**:
	:	
Personal Surplus Lines, Inc. 431 North Springfield Avenue Clifton Heights, PA 19018	:	40 P.S. § 310.11; 40 P.S. § 3311
	:	31 Pa. Code §§ 37.46, 37.47
	:	
	:	Docket No. **SC05-05-016**

ADJUDICATION AND ORDER

AND NOW, this 28th day of November, 2005, M. Diane Koken, Insurance Commissioner of the Commonwealth of Pennsylvania ("Commissioner"), makes the following Adjudication and Order.

HISTORY

This case began when the Pennsylvania Insurance Department ("Department") filed an Order to Show Cause ("OTSC") on May 19, 2005 directed to Personal Surplus Lines, Inc. ("the respondent" or "PSL"). The OTSC alleged that PSL violated the Insurance Department Act.[1] Specifically, the OTSC alleged that the respondent, PSL, a licensed insurance producer, has failed and refused to return unearned insurance premiums, held in trust for Lincoln General Insurance Company ("Lincoln General"), to either Lincoln General or to the Arizona Premium Finance Company ("Arizona Premium") upon the cancellation of various automobile insurance policies.

[1] Act of December 6, 2002, P.L. 1183, No. 147, 40 P.S. §§ 310.1-310.99a.

DATE MAILED: November 28, 2005

The OTSC advised the respondent to file an answer in accordance with applicable regulations (1 Pa. Code § 35.37), and further advised it that the answer must specifically admit or deny each of the factual allegations made in the OTSC. PSL was advised to set forth the facts and state concisely the matters of law upon which it relies. PSL further was advised of the consequences of failing to answer the OTSC. Following the filing of the OTSC, a presiding officer was appointed and the appointment order was served on the respondent by first class mail.

PSL did not answer the Department's Order to Show Cause. During a July 6, 2005 pre-hearing telephone conference counsel for both parties informed the presiding officer that a settlement was imminent but not finalized. Department counsel agreed to withdraw its Order to Show Cause when the settlement was finalized or provide a status report to the presiding officer by July 27, 2005.

On July 27, 2005, Department counsel advised the Administrative Hearings office that a mailing problem had delayed the settlement effort and he requested an extension of time to conclude the case. The presiding officer granted the extension request. Thereafter, Department counsel advised the presiding officer that a settlement had not been reached and he requested an additional pre-hearing telephone conference.

The presiding officer scheduled a telephone conference for September 7, 2005 which was rescheduled to September 21, 2005 at respondent's request. New counsel for PSL was directed to enter an appearance. Both orders were mailed to addresses of the parties which previously had been supplied to the Administrative Hearings Office. Furthermore, even though he had not formally entered an appearance for PSL, counsel also was notified of the new schedule.

On September 21, 2005, Department counsel was available and prepared to

participate in a telephone conference. Counsel for PSL had not filed an entry of appearance as ordered and was not available for the conference call. No one from PSL or its counsel had requested a continuance or otherwise indicated a reason for the failure to be available for the telephone conference. Consequently, on that date the presiding officer issued an order directing PSL to file in writing a reason why default judgment should not be entered against it. The order was served on both PSL and its counsel. The deadline for such response was October 14, 2005. PSL did not respond to the order.

In the absence of a response to the September 21, 2005 Order, this opinion and order addresses the appropriateness of entering a default judgment and imposing penalties in this case. Factual findings and legal conclusions are contained within the body of this adjudication.

DISCUSSION

This adjudication is issued without scheduling an evidentiary hearing, because PSL did not answer the order to show cause or respond to the September 21, 2005 Order. The initial order to show cause advised PSL as to the consequences of a failure to respond;[2] however, because of the language in the penalty provisions of applicable statutes, an analysis of the Commissioner's ability to impose penalties absent an evidentiary hearing is required.

There are no factual disputes in the present matter. All factual averments in the OTSC are deemed to be admitted under 1 Pa. Code § 35.37.

Under general rules of administrative procedure, a final order may be entered

[2] The OTSC warned the that failure to answer in writing would result in the factual allegations being deemed admitted and that the Commissioner could enter an order imposing penalties.

without hearing for an insufficient answer to the OTSC unless otherwise provided by statute. *See* 1 Pa. Code § 35.37 ("Mere general denials . . . will not be considered as complying with this section and may be deemed a basis for entry of a final order without hearing, unless otherwise required by statute, on the ground that the response has raised no issues requiring a hearing or further proceedings."). A respondent failing to file an answer within the time allowed shall be deemed in default. *Id.* Department regulations do not limit the Commissioner's ability to order a default judgment without a hearing, so any limitation must come, if at all, from a statute.

In order for a Commonwealth agency adjudication to be valid, a party must have a "reasonable notice of a hearing and an opportunity to be heard." 2 Pa.C.S. § 504 (Administrative Agency Law). Similarly, the statute specifically applicable to the present matter[3] provides for a hearing procedure prior to certain penalties being imposed by the Commissioner. *See* 40 P.S. § 310.91.[4] However, given that the respondent in this case has not answered the Department's order to show cause, nor responded to the Presiding Officer's specific order to show cause why default judgment should not be entered, and given current case law, these hearing procedures are inapplicable.

While no court has directly addressed the power of a Commissioner to enter a default judgment without hearing in a case under the Insurance Department Act, the case law supports such power. For example, in *United Healthcare Benefits Trust v. Insurance Commissioner*, 620 A.2d 81 (Pa. Cmwlth. 1993), the Court affirmed the Commissioner's

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[3] Insurance Department Act, Act of May 17, 1921, P.L. 789 as *amended* by the Act of December 6, 2002, P.L. 1183, No. 147 (40 P.S. §§ 310.1-310.99a).

[4] The Insurance Department Act section mandates written notice of the nature of the alleged violations and requires that a hearing be fixed at least ten (10) days thereafter, and further provides that:

> After the hearing or upon failure of the person to appear at the hearing, if a violation of this act is found, the Insurance Commissioner may, in addition to any penalty which may be imposed by a court, impose any combination of the following deemed appropriate: . . .

40 P.S. § 310.91(d).

grant of summary judgment for civil penalties despite the language contained in 2 Pa.C.S. § 504 and 40 P.S. § 47.[5] Also, the Court specifically has upheld a decision in which the Commissioner granted default judgment for an Unfair Insurance Practices Act (UIPA) violation. *Zimmerman v. Foster*, 618 A.2d 1105 (Pa. Cmwlth. 1992).

In a case involving another agency, the Commonwealth Court upheld summary judgment imposing discipline issued by a commission despite the fact that the respondent had requested a hearing. *Kinniry v. Professional Standards and Practices Commission*, 678 A.2d 1230 (Pa. Cmwlth. 1996). In *Kinniry*, the applicable statute (24 P.S. §§ 2070.5(11), 2070.13) provided for a hearing procedure before discipline was imposed. However, the respondent's attorney merely requested a hearing without answering the specific factual averments in the charges against the respondent (which charges were treated as an order to show cause). The Court upheld the summary judgment since deemed admission of the factual averments presented no factual issues to be resolved at hearing.

The Commissioner consistently has applied the reasoning of *United Healthcare* and similar cases when a respondent does not answer the order to show cause and a motion for default judgment. *See In re Kozubal*, P93-08-13 (1997); *In re Phelps*, P95-09-007 (1997); *In re Taylor*, SC96-11-034 (1997); *In re Crimboli*, SC99-04-015 (1999); *In re Young*, SC98-08-027 (2000); *In re Jennings*, SC99-10-001 (2001); *In re Warner*, SC01-08-001 (2002). The Commissioner adopts this reasoning in the present case: the important aspects of 2 Pa.C.S. § 504 are notice and the *opportunity* to be heard. Default judgment is appropriate, despite language in applicable statutes which seems to require a hearing, when a respondent fails to take advantage of an opportunity to be heard. When a respondent in an enforcement action is served with an order to show cause detailing the nature of the charges against it as well as the consequences of failing to respond, yet fails

[5] The operative language was functionally equivalent to that in 40 P.S. § 310.91.

to answer the allegations or to participate in other proceedings pending hearing, the Commissioner adopts the Commonwealth Court's reasoning that the respondent had an opportunity to be heard but has rejected the opportunity.

Additionally, no factual matters need to be addressed at a hearing. Since the factual allegations of the OTSC are deemed admitted, the determination in this case by the Commissioner is a legal rather than a factual one. A hearing is not necessary for this type of determination. *See Mellinger v. Department of Community Affairs*, 533 A.2d 1119 (Pa. Cmwlth. 1987); *United Healthcare, supra.* The Commissioner adjudicates the present case based upon the undisputed, admitted facts as alleged in the OTSC.

The facts include that PSL is a Pennsylvania corporation licensed insurance producer. [OTSC ¶¶ 1, 3]. Pasquale Scaramuzza is registered with the Department of State as the president of PSL. [OTSC ¶ 2]. His Pennsylvania insurance agent's license was suspended by a February 10, 2000 Order of the Pennsylvania Insurance Commissioner and remains inactive. [OTSC ¶ 4]. Lincoln General is an insurance company authorized to do business in Pennsylvania which entered into a brokerage agreement with PSL in 1995. [OTSC ¶¶ 8, 15; OTSC Exhibit B]. Arizona Premium is an insurance premium finance company authorized to do business in Pennsylvania. [OTSC ¶ 9]. Arizona Premium entered into transactions in which it financed premiums in connection with multiple policies sold by PSL and issued by Lincoln General. [OTSC ¶ 14].

Under the brokerage agreement with Lincoln General, PSL was responsible for collecting, accounting for and paying all premiums on the insurance business it wrote for Lincoln General. [OTSC ¶ 15(a)]. Additionally, under 40 P.S. § 3311, when any insurance policies with financed premiums are cancelled, the gross unearned premiums must be returned to the finance company as soon as reasonably possible, but in no event

later than sixty (60) days after the effective date of cancellation. [OTSC ¶ 15(c)]. PSL consistently failed and refused to return unearned portions of premiums to either Lincoln General or to Arizona Premium upon cancellation of various automobile insurance policies. [OTSC ¶¶ 14, 15(d)]. As a result of PSL's actions, Lincoln General and Arizona Premium Finance Company each suffered large financial losses. [OTSC ¶¶ 15 and 15(e)].

Consequently the Department has charged PSL with the following five actions: 1) violating the insurance laws or regulations of this Commonwealth (40 P.S. § 310.11(2)); 2) improperly withholding, misappropriating or converting money or property received during the course of doing business (40 P.S. § 310.11(4)); 3) using fraudulent, coercive or dishonest practices or demonstrating incompetence, untrustworthiness or financial irresponsibility in the conduct of doing business in this Commonwealth or elsewhere (40 P.S. § 310.11(7)); 4) committing fraud, forgery, dishonest acts or an act involving a breach of fiduciary duty (40 PS.310.11(17)); and 5) demonstrating a lack of general fitness, competence or reliability sufficient to satisfy the department that the licensee is worthy of licensure (40 P.S. § 310.11(20)).

For each of these five charges, the Commissioner has authority to impose remedial action against the respondent, including suspending or revoking its license, imposing a civil penalty not to exceed $5,000.00, ordering PSL to cease and desist from the conduct and imposing additional conditions. 40 P.S. § 310.91. Prohibited acts are listed in 40 P.S. §§ 310.11. In the present case, the admitted facts support sanctions for each of the five charges against PSL.

In this case PSL failed to return gross unearned premiums to Arizona Premium. This action violated the Insurance Premium Finance Company Act ("IPFCA").[6] Section

[6] Act of December 19, 1984, P.L. 1182 No. 224, § 1, 40 P.S. 3301-3314.

3311 of the IPFCA provides that, when policies with premiums financed by an Insurance Premium Finance Company are canceled, the gross unearned premiums must be returned to the finance company as soon as possible, but in no event later than 60 days after the effective date. Section 3311 also provides that if the crediting of return premium results in an excess, the insured is entitled to a refund of that excess. In this case PSL failed to return such premium for 400 insurance policies. [OTSC Exhibit C, p. 3]. PSL's failure to return unearned premiums to Arizona Premium not only caused financial harm to the finance company, but also to any insured who otherwise may have been entitled to a refund. PSL violated the insurance law of this Commonwealth which is prohibited under 40 P.S. § 310.11(2).

PSL withheld the gross unearned premium from both Arizona Premium and Lincoln General during the years 1995 through 1997. [OTSC ¶ 12, Exhibit B ¶¶ 14, 15]. As a result, Lincoln General terminated its brokerage agreement with PSL. [*Id.*]. PSL has continued to withhold the funds through the present time. This improper withholding of money received in the course of business is a violation of 40 P.S. § 310.11(4).

In an effort to recoup their losses, both Lincoln General and Arizona in 2003 obtained judgments against PSL. [OTSC ¶¶ 10, 16]. Lincoln General obtained a judgment in the amount of $477,556.12. [OTSC ¶ 11; Exhibit A]. Arizona Premium obtained a judgment in the amount of $210,004.00 plus 6% interest from March 31, 2003 until paid. [OTSC Exhibit C]. PSL has not paid either judgment. [OTSC ¶¶ 11,17]. PSL's failure to remit the hundreds of thousands of dollars as ordered by the Court of Common Pleas of Montgomery County and by the United States District Court for the Eastern District of Pennsylvania demonstrates financial irresponsibility. Its continuing failure to pay violates the provisions of 40 P.S. § 310.11(7).

Furthermore, as an Insurance producer, PSL owed Lincoln General a fiduciary duty to hold the premiums received in trust for Lincoln General's benefit and to refrain from commingling premiums with its funds. The significant amounts of premium money withheld represent a pattern of behavior in 400 transactions in which PSL regularly violated its fiduciary duty. The resultant commingling of funds also constituted a breach of PSL's fiduciary duty in violation of Section 310.11(17). Taken all together, the actions taken by PSL during the years 1995 to the present demonstrate that it is not worthy of licensure. 40 P.S. § 310.11(20).

PENALTIES

The Commissioner may suspend or revoke a license for conduct violating certain provisions of the Insurance Department Act, including those provisions violated by PSL. 40 P.S. § 310.91. Each action violating a provision specified in section 310.11 subjects the actor to a maximum five thousand dollar civil penalty. 40 P.S. § 310.91(d)(2). In this case, PSL retained unearned premium on 400 policies. Evidence is not clear as to how many of the affected insureds were entitled to refunds; thus while a five thousand dollar civil penalty could be imposed for the action on each policy, the penalty has been somewhat reduced because in the absence of additional evidence concerning the activities on each policy.

A Commissioner is given broad discretion in imposing penalties. *Termini v. Department of Insurance*, 612 A.2d 1094 (Pa. Cmwlth. 1992); *Judson v. Insurance Department*, 665 A.2d at 523, 528 (Pa. Cmwlth. 1995). The underlying course of conduct in the present case is of the most serious nature, and directly connected to PSL's duties as an insurance producer. This seriousness is reflected in the penalties imposed. PSL's infliction of financial harm on others evidences a significant lack of the trustworthiness required in the profession. By definition, insurance producers have

extensive personal contact with applicants, insureds, insurance companies and other financial entities. The applicants and insureds entrust financial and PSL matters to the producer, and rely upon the producer's integrity. A producer who has inflicted financial harm upon others for at least ten years is incapable of the trust necessary in the profession. Simply put, PSL cannot be trusted with the pocketbooks and bank accounts of any of those persons and entities with whom PSL deals.

Aggravating circumstances in this case include the significant amounts of money PSL has withheld from the companies and insureds with which it did business, the length of time that PSL improperly has held the funds, and its complete disregard for court orders requiring repayment of the funds. Furthermore, PSL has disregarded the current proceedings. In contrast, PSL has presented no evidence to mitigate the seriousness of its violations.

The Department in its Order to Show Cause has requested revocation of PSL's license/certificate of qualification; a cease and desist order and civil penalties deemed appropriate under the circumstances. Considering the facts in this matter, the applicable law, the seriousness of the conduct, all aggravating circumstances as well as the complete lack of mitigating circumstances, penalties are imposed as set forth in the accompanying order.

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	:	
	:	31 Pa. Code §§ 37.46, 37.47
	:	
	:	
	:	Docket No. **SC05-05-016**

ORDER

AND NOW, based upon the foregoing findings of fact, discussion and conclusions of law, it is **ORDERED** as follows:

1. Personal Surplus Lines, Inc. shall **CEASE AND DESIST** from the prohibited conduct described in the adjudication.

2. All of the insurance licenses or certificates of qualification of Personal Surplus Lines, Inc. **ARE REVOKED.** Additionally, Personal Surplus Lines, Inc. is prohibited from applying for a certificate of qualification to act as an agent, broker or producer in this Commonwealth. Personal Surplus Lines is also prohibited from applying to renew any certificate of qualification previously held by it in this Commonwealth.

3. Personal Surplus Lines, Inc. shall **PAY A CIVIL PENALTY** to the Commonwealth of Pennsylvania within thirty (30) days of this order in the amount of Four Hundred Twenty Five Thousand Dollars ($425,000.00). Payment shall be made by certified check or money order, payable to the Commonwealth of Pennsylvania, directed to: Sharon Harbert, Administrative Assistant, Bureau of Enforcement, 1321 Strawberry

Harrisburg, Pennsylvania 17120.

3. This order is effective immediately.

M. Diane Koken
Insurance Commissioner