

AMERICAN LAW AND INSURANCE REGULATION---INTRODUCTION (530-1)

EO 1. **THE DIFFERENCE BETWEEN THE CIVIL AND COMMON LAW FORMS OF LEGAL SYSTEMS: THE CIVIL LAW LEGAL SYSTEM** is based on scholarly interpretations of comprehensive written laws. It is the basis of the law in some European and Latin American countries and in parts of the US that were under French or Spanish rule.

The law of Louisiana still uses many aspects of the Napoleonic Code.

THE COMMON LAW LEGAL SYSTEM is the basis of **THE US LEGAL SYSTEM** which is composed of both **statutes** (legislated law) and **common law** (judicial decisions).

Common law is based on **the doctrine of stare decisis** (Latin “to stand by the decision”) which requires current judicial decisions to be based on past judicial decisions, known as **precedents**.

Courts use the synthesis process to review and apply the law to new fact situations.

Threshold cases present new legal questions and fact patterns.

Courts, by interpreting and applying laws, effectively enact new laws.

Such case law stands until changed by constitution, statute, or new judicial precedent.

Landmark decisions, such as Brown vs. Board of Education and Roe vs. Wade *significantly* change the law.

COMMON LAW, therefore, is simply judicial case law.

Alternately, **common law** is the unwritten codification of society’s rules of conduct as rendered by judicial decisions. The origins of common law date back to the Norman conquest of England in 1066.

Its stability is maintained by applying the doctrine of stare decisis.

Its growth derives from the uniqueness and evolving character of the individual cases brought to courts.

CLASSIFICATION OF AMERICAN LAW:

Criminal law--deals with actions injuring the state or society.

Criminal wrongs are prosecuted by the state prosecutor. **Statutes specify if a crime is**

1. a **felony** (a major crime),
2. a **misdemeanor** (a minor crime), *or*
3. a **summary offense** (a crime punishable by a fine, such as speeding or parking illegally).

Civil law--deals with actions injuring a citizen or other member of society (a corporation, partnership, governmental entity). The **plaintiff** (aggrieved party) brings suit against the **defendant** (alleged wrongdoer).

Some acts involve both criminal and civil liability by both violating the dignity of the community (**crime**) *and* invading the rights of an individual (**tort**).

Such acts are tried twice, in different courts, under different rules of evidence, with different burdens of proof, and with different penalties.

Examples: theft (liable for the value of the property), negligent manslaughter (liable for the human life value), and arson. OJ was acquitted in a criminal trial for murder (requiring proof beyond a reasonable doubt) yet was civilly liable (requiring a preponderance--51%--of the evidence) to his victims’ estates.

Arsonists may also escape criminal penalties, yet *not* be paid insurance benefits for fire or murder.

Law may be classified by subject matter: administrative law, agency, commercial paper, constitutional law, contracts, corporate law, criminal law, rules of evidence, family law, partnerships, property law, torts, and wills. Actions may be brought **at law** to recover money damages or **in equity** for other remedies, such as injunctions or specific performances, when money damages would be inadequate.

Substantive law defines people’s rights and liabilities. It’s what we think of as ‘the law’.

Procedural law specifies how attorneys file legal papers and how judges apply the substantive law.

Criminal and civil cases have different procedural rules (criminal procedures and civil procedures).

EOs 2 + 3. **THE SOURCES OF AMERICAN LAW**--The federal government and the 50 states form the framework for our nation's 51 legal systems. **Each of those 51 systems has five sources of law:**

1. federal and state constitutions,
2. legislative bodies,
3. judicial courts,
4. executive branches, *and*
5. administrative agencies.

CONSTITUTIONAL GROUND RULES: Constitutions establish their governments' forms (**procedural law**) and powers (**substantive law**) but limit those powers by guaranteeing individual rights.

The US Constitution is the self-proclaimed "supreme Law of the Land".

A state's constitution is the supreme law of that state, superseded *only* by the US Constitution.

The Due Process Clause, the Fifth Amendment, prevents the federal government from depriving anyone of life, liberty, or property "without due process of law".

The Equal Protection Clause, the Fourteenth Amendment, provides that no *state* shall deny any person equal protection of the law or deprive anyone of life, liberty, or property "without due process".

The express powers of Congress are enumerated in Article 1, Section 8 of the Constitution (regulate commerce among the several States, tax, regulate bankruptcy).

The implied powers of Congress let Congress make laws necessary and proper to exercise its express powers. Powers not enumerated are reserved to the states or the people.

The Commerce Clause gives Congress the power "to regulate commerce with foreign nations and among the several States". The Commerce Clause applies to any commercial activity that affects interstate commerce.

LEGISLATIVE LAW MAKING: **Statutes** are written dictates of legislative bodies, which declare, command, or prohibit something.

Congress and most state legislatures are **bicameral** (two chambers--Senate and House).

Legislatures enact **statutes**, which interpret society's desires, set standards for behavior (substantive law), and provide for the functioning of the governmental unit (procedural law).

Any law (federal or state) that violates the US Constitution is voidable.

States adopt uniform laws to eliminate confusion from differences in laws between states.

JUDICIAL INTERPRETATION OF LAWS: **Judicial case law is set by the courts.**

Jurisdiction is a court's power to hear a particular case. **A court can have**

1. **original jurisdiction**--power to hear cases initiated in that court,
2. **appellate jurisdiction**--power to hear appeals from another court, *or*
3. **general jurisdiction**--power to hear a variety of cases.

The US has two court systems:

1. **The federal court system** consists of the Supreme Court, US Circuit Courts of Appeal, and US District Courts (federal trial courts).

Federal courts have jurisdiction over cases with federal questions of law, cases in which the US is the plaintiff or defendant, admiralty and maritime cases, cases involving disputes under grants by different states, and cases involving **diversity jurisdiction** (cases with parties from different states and more than a threshold amount of damages).

The losing party in a district court case may appeal to the appropriate circuit court.

The losing party in the circuit court may request a **writ of certiorari** from the Supreme Court.

The Supreme Court has discretion whether to hear a case.

2. **The state court systems** generally consist of supreme court (one in each state), appellate courts, trial courts of general jurisdiction, courts of limited jurisdiction (probate courts), and lowest courts (mayors' courts).

EXECUTIVE BRANCH AND ADMINISTRATIVE AGENCY LAW ENFORCEMENT: To have specialized and complex functions knowledgeably and efficiently performed, legislatures delegate much of their lawmaking authority to a multitude of administrative agencies in the executive branch. Rules and regulations established by those agencies (**administrative law**) carry the force of statutes. In addition to appointing heads of the administrative agencies and overseeing their activities, each legal system's **chief executive** (president, governor, mayor) normally approves or vetoes legislative statutes and recommends new laws.

A legislature has constitutional authority to delegate its powers to an administrative agency if

1. the scope of power delegated is defined,
2. the agency promulgates rules within the scope of the power delegated, *and/or*
3. the rules are subject to court review.

EO 4. **CONFLICT OF LAWS' PRINCIPLES** determine which state's law to apply when a case involves more than one state.

Example: A Maine resident buys insurance from a Connecticut company on property in Ohio.

1. **TORT AND CONTRACT CASES**--A case tried in *any* state (the **forum state**) is tried under *that* state's procedural law.
Tort cases are generally tried under the substantive law of the state where the injury occurred. **Contract cases** are generally tried under the substantive law of the state of greatest contact between the parties to the contract, known as **the center of gravity test**. Parties to a contract can avoid conflicts of law by including contractual language about which state's laws will apply in the event of a dispute.
2. **FEDERAL-STATE PROBLEMS**--Federal courts apply their own procedural law. They apply federal substantive law in cases with a federal law dispute. In diversity cases, they apply the substantive law of the state where the court is located, including the state's conflicts of law rule.

EO 5. **COURT LEGAL PROCEDURES:**

A. **PRETRIAL PROCEDURE**--

1. **The plaintiff files a complaint** (pleading or legal document) **that states the plaintiff's cause of action** (legal grounds to sue) and **allegations** (claims that the plaintiff asserts and expects to prove), the court's jurisdiction, *and* the remedy sought.
2. The court issues a summons to the defendant.
3. The defendant files
 - a. **an answer** (response to the complaint) and, sometimes, a **counterclaim** (his own complaint against the plaintiff) *or*
 - b. **an entry of appearance** that neither admits nor denies the allegations in the complaint, but states that he will appear in court.
4. The plaintiff files a reply.
5. The parties file **motions** (formal requests for actions by the court).
The defendant may file a **motion to dismiss**, which requests the court to dismiss the claim due to the plaintiff's failure to state a claim for which the court can grant relief.
Either party may file a **motion for judgment on the pleadings** or a **motion for summary judgment** that states there is no genuine issue of material fact and the moving party is entitled to judgment based on the law.
6. Either the plaintiff or the defendant may seek **discovery procedures** including **interrogatories** (written questions needing written answers), **depositions** (recorded oral testimonies), and motions to produce physical evidence.
7. Either may request a pretrial conference with the judge to try to settle or to **stipulate** (agree to) some of the facts.

B. **TRIAL PROCEDURE--**

1. Either party may challenge a juror for cause (possible bias) or use a **preemptory challenge** (to remove a juror without cause).
2. The attorneys make **opening statements** that preview the case.
3. The plaintiff's lawyer presents his client's case through **direct examination** (questioning his own witnesses).
4. The defendant's lawyer may cross-examine any witness and presents his client's case.
5. Each lawyer presents his closing argument.
6. The judge instructs the jury on the applicable law.

The judge may also take the case from the jury by

- a. **directing a verdict** (deciding the case),
- b. **declaring a mistrial** (ending the trial due to an error or a deadlocked jury), *or*
- c. **declaring a nonsuit** (finding that the plaintiff did not state a case).

The judge decides questions of law, such as whether the defendant had a legal duty.

The jury decides questions of fact, such as the extent of the plaintiff's damages.

7. **The jury renders its verdict--either**

- a. **a general verdict** (one conclusion based on all issues) *or*
- b. **a special verdict** (a determination of specific findings of fact).

8. **The doctrine of res judicata** makes final judgment on an issue binding on the parties in all future cases brought on the same matter.

The rule applies *only* to cases with the *same* parties and *same* issues.

Collateral estoppel means that once an issue has been decided, it is binding on the same parties in the future.

C. **APPELLATE PROCEDURE--**

1. Either party may appeal (become an **appellant**).
The party not appealing is the **appellee**.
A party may only appeal questions of law, not questions of fact.
2. Each lawyer files a **brief** (written statement of the facts, issues, and legal arguments) and makes an oral argument to the court.
3. The appellate court affirms or reverses, in writing, the lower court's decision or sends the case back for retrial if the lower court's error was **prejudicial** (substantially affected the outcome of the case).

Rules of evidence--to be admissible, evidence must be

1. **relevant**--relate to the matter at issue,
2. **material**--of significance to the matter at issue, *and*
3. **competent**--of a proper nature.

The hearsay rule excludes **hearsay evidence** (out-of-court statements of another offered to prove the truth of the matter asserted).

Several exceptions allow specific types of hearsay to be admitted.

Only expert witnesses may give opinion evidence.

EO 6. **ALTERNATIVE DISPUTE RESOLUTION TECHNIQUES (ADR):**

1. **ARBITRATION**--a binding resolution is made under the rules of the American Arbitration Association (**AAA**).
2. **MEDIATION**--a third party (often an experienced trial attorney or a retired judge) seeks to end the conflict through compromise.
3. **NEGOTIATION**--including private mini-trials and court-sponsored mock summary jury trials--to help the parties resolve their conflict.

- EO 7. **ADMINISTRATIVE AGENCY RULE-MAKING PROCEDURE--Types of agency rules:**
1. **Legislative rules**--are created by the statutory delegation of authority and carry the force of law.
 2. **Interpretative rules**--interpret statutes and provide guidance for the agency and regulated parties. They do *not* carry the force of law and, thus, are *not* binding on individuals.
 3. **Procedural rules**--regulate internal agency procedures. Agency procedural rules are set by **The Administrative Procedure Act (APA)** (for federal agencies) *and* **The Model State Administrative Procedure Act (MSAPA)** (for state agencies).

The steps in the rule-making procedure:

1. An agency publishes notice of intent to adopt a regulation in an official publication, such as the **Federal Register** (for federal agencies) or the appropriate state publication.
2. The agency publishes the regulation's text and provides an opportunity for public comment, either in writing or at a public hearing run by a hearing examiner.
3. **After reviewing comments, the agency**
 - a. adopts the rule as proposed,
 - b. modifies and adopts the rule, *or*
 - c. nullifies the proposed rule.
4. The agency publishes the final rule.

ADMINISTRATIVE AGENCY CASE ADJUDICATION PROCEDURE--

1. **Notice**--including the time, place, nature, jurisdiction, and legal authority of the hearing; the statute or rule involved; and a short statement of the matters at issue.
2. **Hearing**--either **informal** or **formal** with a hearing examiner or administrative law judge.
3. **Adjudication**--a final order with findings of fact and conclusions of law.

LIMITATIONS ON ADMINISTRATIVE AGENCY INVESTIGATORY POWERS--Agencies may compel witness cooperation with a **subpoena ad testificandum (aka subpoena)** (command to testify) or a **subpoena duces tecum** (command to 'bring with you', ie, to produce documents).

Agency powers are limited by the

1. **Fourth Amendment protection against illegal search and seizure**--Requests must be relevant and not unreasonably broad.
2. **Fifth Amendment protection against self-incrimination**--A witness can *not* be forced to incriminate himself.

PREREQUISITES FOR JUDICIAL REVIEW OF ADMINISTRATIVE AGENCY ACTIONS--

1. **Standing to sue**--The plaintiff must be damaged by the agency action.
2. **Exhaustion of administrative remedies**--**Judicial review can occur only after**
 - a. the agency has issued a **final order** (determination that terminates the proceedings) *and*
 - b. the plaintiff has **exhausted all administrative remedies** (completed all possible administrative procedures and appeals).

Exception: Courts allow immediate appeal if the available administrative remedy is inadequate and administrative appeal would be futile.
3. **Standard for review**--**A court will set aside an agency action only if it**
 - a. was **arbitrary and capricious** (willful, unreasonable, or without rational basis), an abuse of discretion, *or* unlawful;
 - b. was unconstitutional;
 - c. exceeded its statutory authority;
 - d. resulted from illegal procedures or failure to follow procedural rules; *and/or*
 - e. was unsupported by substantial evidence in the record.

The court will *not* set aside the action unless it is *clearly* erroneous.

EO 8. **THE PRIVACY ACT** applies to agency records with information about people that is accessed by an identifying number.

The act allows an individual access to his own records (except CIA and law enforcement records) and prohibits disclosure without his permission.

THE FREEDOM OF INFORMATION ACT provides public access to agency information *except* classified security information, law enforcement investigation records, trade secrets, confidential commercial or financial information, and the records of financial institutions.

EO 9. **FEDERAL LAW** does *not* directly regulate the insurance business.

The Commerce Clause of the Constitution gives Congress the power to regulate “**commerce** (any commercial activity that even indirectly affects interstate commerce) among The States”.

The McCarran-Ferguson Act allowed the states to regulate the insurance industry and exempted it from federal antitrust laws to the extent that it is regulated by the states.

FEDERAL LAW GOVERNS INSURANCE *only when a federal law*

1. applies *only* to the business of insurance,
2. affects insurers’ activities that are *not* unique to the business of insurance, *and*
3. regulates an aspect of the business of insurance that is *not* otherwise regulated by state law.

THREE ARGUMENTS FAVORING FEDERAL REGULATION OF INSURERS:

1. **Uniformity in regulation**--Insurers doing business in more than one state would *not* have to comply with 50 sets of rules.
2. **Efficiency**--Insurers would deal with only one federal agency, instead of up to 50 state agencies, and hence would have lower expenses.
3. **Higher quality personnel**--Higher salaries and greater prestige would attract better-qualified personnel at the federal level.

FIVE ARGUMENTS FAVORING STATE REGULATION OF INSURERS:

1. **Greater responsiveness**--to local needs and local problems.
2. **Uniformity of state laws**--already largely exists through NAIC model laws and regulations.
3. **Greater opportunities**--for innovation. States are less bureaucratic.
4. **Inertia**--The strengths and weaknesses of state regulation are known.
5. **Decentralization**--of power and stronger states rights are always good.

STATE INSURANCE REGULATION is an administrative agency function arising from state statutes that give state departments of insurance (**DOIs**) the primary regulatory authority over insurers.

The state insurance commissioner supervises the state DOI.

A state insurance commissioner’s duties include supervising insurer licensing, monitoring insurer solvency, reviewing insurer investments, approving policy forms, setting and/or approving rates, regulating marketing, operating guaranty funds, operating government-mandated programs, reviewing annual reports, investigating complaints, promulgating regulations, *and* proposing legislation.

THE NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC) has *no direct* regulatory authority.

The NAIC develops model legislation for state insurance departments.

The NAIC drafts

1. **model laws** (draft bills that state legislatures may adopt) *and*
2. **model regulations** (draft regulations that correspond to the model laws).

State adoption of model laws and regulations is optional.

STATE REGULATION OF INSURERS:

1. **Licensing**--To operate in a state, an insurer must be licensed by the state's DOI. **The insurer must submit an application package that includes** a description of management, an insurer history, a list of states in which the insurer is licensed, the types of insurance the insurer has written, an operating plan, biographical information about senior officers and directors, copies of reinsurance contracts, **and** recent financial statements.
2. **Audits**--After an insurer is licensed, it is subject to periodic financial audits and market conduct examinations.
In a zone examination, one DOI audits an insurer on behalf of all states in the zone in which the insurer holds licenses.

STATE REGULATION OF INSURANCE PRODUCERS--Agents and brokers must obtain licenses to solicit, negotiate, issue, and deliver insurance policies.

To get a license, a person must

1. be over a certain minimum age,
2. have an appointment from a licensed insurer,
3. complete the application, **and**
4. pass the examination requirement.

A managing general agent (MGA) negotiates and binds ceding reinsurance contracts for an insurer **or** manages its insurance business.

An MGA must be licensed and may be required to post a bond and maintain an errors and omissions policy. MGAs are subject to increased regulatory attention due to the role that some MGAs have played in insurer insolvencies.

Provisions in the contract between the insurer and MGA must discuss the MGA's duty to follow underwriting guidelines regarding the MGA's maximum annual premium volume, types of risks, maximum policy limits, applicable exclusions, territorial limitations, policy cancellation provisions, and maximum policy periods.

An agent or broker who places insurance through a nonadmitted insurer must have a surplus lines insurance license.

Under the NAIC model act, to qualify as a surplus lines broker, the agent must

1. pay an annual fee,
2. submit an application,
3. pass a qualifying examination,
4. file a bond,
5. maintain a full and complete record of each surplus lines contract placed, **and**
6. submit a quarterly report listing premiums written, amount of taxes paid, and return premiums.

[Ray's aside: Note that "commerce among the States" for most of our country's history meant 'commerce among the States' ... just what you'd expect ... just what the drafters of the Constitution intended since the purpose of the clause was to eliminate the trade barriers (quotas and tariffs) that existed among the States under the Articles of Confederation.

That commerce clause went hand-in-hand with the authority "To establish Post Offices and post Roads" since, to control commerce among the states, roads in one state generally did not match up to roads on the other side of a state line so the quotas and tariffs could be more easily enforced.

The expansion of the meaning of "States" to include corporations, partnerships, trusts, and individuals did not occur until FDR packed the Supreme Court.

Why not read Article I, Section 8 of our Constitution for yourself?]