INSURANCE: STATE REGULATORY LEGISLATION BARS REGULATION BY FTC

Federal Trade Commission v. The American Hospital & Life Insurance Co., 357 U.S. 560 (1958)

As a result of hearings before the Federal Trade Commission, the respondent insurance companies had been ordered to cease and desist from distributing allegedly misleading advertising materials.[1] Both companies appealed from these orders in the appropriate appellate courts[2] and it was held in both cases that under the terms of the McCarran-Ferguson Act[3] the FTC lacked jurisdiction since the states involved had their own regulatory legislation. The FTC obtained certiorari[4] in both cases and they were combined before the Supreme Court where the decisions of the courts of appeals were affirmed.[5]

The advertising materials complained of were shipped in bulk by the companies to their agents who distributed them locally.[6] The Supreme Court pointed out that the case did not raise the question of the constitutional infirmity of the states to regulate across state lines.[7] Thus, the court regarded the only "distribution" involved to be the local distribution by the agents, and construed the order of the FTC as being directed against distribution within a state; if the state had regulatory legislation, the order of the FTC would be invalid because of lack of jurisdiction.[8]

Since the decision in the instant case turned upon an interpretation of the McCarran-Ferguson Act, some study of the background of this legislation is necessary.

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[1] The American Hospital and Life Insurance Co., 21 Fed. Reg. 2979 (1956); National Casualty Co., 21 Fed. Reg. 3924 (1956).

[2] National Casualty Co. v. FTC, 245 F.2d 883 (6th Cir. 1957), *cert. granted,* 355 U.S. 867 (1957); American Hospital and Life Insurance Co., 243 F.2d 719 (5th Cir. 1957); *cert. granted,* 355 U.S. 867 (1957).

[3] 15 U.S.C. §§ 1011-15 (1952).

[4] *Supra* note 2.

[5] FTC v. The American Hospital & Life Insurance Co., 357 U.S. 560 (1958).

[6] While some of the advertising complained of was distributed through the mails directly to potential customers, most of the material was shipped in bulk to agents who distributed it locally. The Supreme Court, however, confined its consideration to the latter material, dismissing the former as an "insubstantial amount".

[7] "Whatever may have been the intent of Congress with respect to interstate insurance practices which the states cannot for constitutional reasons regulate effectively, that intent is irrelevant in the cases before us." 357 U.S. at 564.

[8] "These orders seek to proscribe activities within the boundaries of states that have their own statutes prohibiting unfair and deceptive insurance practices as well as within states that do not." *Id.* at 562; "An examination of that statute [McCarran-Ferguson Act] and its legislative history establishes that the act withdrew from the Federal Trade Commission the authority to regulate respondents' advertising practices in those states which are regulating these practices under their own laws." *Id.* at 563.

The rule that insurance was not commerce had been followed in an unbroken line of cases since first announced by the Supreme Court in *Paul v. Virginia*[9] in 1868. Therefore, it came as a considerable surprise to those interested in the "business of insurance" when the court held, in the *South-Eastern Underwriters* case, that insurance was commerce; when conducted across state lines it was interstate commerce and, as such, subject to federal antitrust laws.[10] The court distinguished its earlier holdings by pointing out that previous litigation had never tested the power of *Congress* under the commerce clause, but rather tested the validity of state action.[11] Protest by insurance executives and state insurance officials followed swiftly in the wake of the decision.[12] Congressional reaction came in the McCarran-Ferguson Act which became law on March 9, 1945. While the legislative history of the act[13] reveals that some members of Congress wished to nullify the *South-Eastern* decision and exclude all federal regulation of insurance, even a cursory reading of the act reveals that Congress did not place the business of insurance beyond its reach.[14]

Insurance executives were placed in a genuine quandary by the *South-Eastern* decision. State tax laws and state regulations, in view of the holding that insurance was commerce, might well be declared to be unconstitutional burdens on interstate commerce. State revenues, of which taxes on insurance companies were an important component, were in danger. Accordingly, one of the main purposes of the act was to give legal sanction to these state laws, and prevent the collapse of existing insurance regulation.[15]

In essence, the McCarran-Ferguson Act was a call to action to the states. The act provided:

1. For a stated period federal regulatory legislation would

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[9] "Issuing a policy of insurance is not a transaction of commerce." Paul v. Virginia, 75 U.S. (8 Wall.) 168, 183 (1868). "The business of insurance is not commerce. The contract of insurance is not an instrumentality of commerce." Hooper v. California, 155 U.S. 648, 655 (1895).

[10] "No commercial enterprise of any kind which conducts its activities across state lines has been held to be wholly beyond the regulatory power of Congress under the Commerce Clause. We cannot make an exception of the business of insurance." U.S. v. South-Eastern Underwriters Association, 322 U.S. 533, 553 (1944).

[11] "But past decisions of this Court emphasize that legal formulae devised to uphold state power cannot uncritically be accepted as trustworthy guides to determine *Congressional power* under the Commerce Clause." *Id.* at 545.

[12] In fact, several bills were introduced in Congress prior to the decision in *South-Eastern* which would have made the question in the case moot by specifically exempting insurance from the operation of the Sherman and Clayton Acts. See S. 1362, H.R. 3270, H.R. 3269, 78th Cong., 2d Sess. (1944).

[13] See, *e.g.*, 91 CONG. Rec. 1085-1094 (1945).

[14] See, *e.g.*, 15 U.S.C. § 1013(a) (1952).

[15] SEN. REP. No. 20, 79th Cong., 1st Sess. (1945).

not apply to the business of insurance.[16]

2. At the end of the period it would again apply except to the areas in which there was state regulatory legislation.[17]
3. To the extent that the business of insurance went unregulated by the state, the Federal Trade Commission Act would apply.[18]

Therefore, it became necessary for the states to enact legislation which covered the fields of the federal legislation. It was *not* necessary that state statutes embody the same criteria as the federal laws. As Senator Ferguson's remarks made clear,[19] the state law would control even if in conflict with federal legislation. Thus, in the reverse of the usual preemption concept, the states were given Congressional authority to preempt certain areas of interstate commerce regulation.

In their attempt to justify their jurisdiction to regulate in the instant cases, the FTC, relying on the reservation of power to them contained in the act,[20] maintained that *regulate* meant more than *legislate;* and that if a state was not *regulating administratively* the mere presence of regulatory legislation on its statute books did not prevent the FTC from regulating. The court said this argument was not persuasive in these cases.[21]

The second main branch of the FTC argument was based on the idea that individual states cannot regulate completely because of their limited territorial jurisdiction. This argument, as noted previously[22] was dismissed by the Court as irrelevant.

The question then, of a state's ability to regulate an unlicensed out-of-state insurer, is still an open one. The "constitutional infirmity" of the states to reach beyond their own jurisdiction would seem to make at least this one area subject to the control of the FTC under the terms of the proviso in Section 1012(b). Nevertheless, even here the states are taking measures to assert their own control.

One of the means used is the "Unauthorized Insurance Service of Process Act" which is now law in forty-two states and two territories.[23]

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[16] 15 U.S.C. § 1013(a) (1952).

[17] 15 U.S.C. § 1012(b) (1952).

[18] 15 U.S.C. § 1012(b) (1952).

[19] "Under the language which is now in the bill as it appears in the conference report, if a state passes an act regulating insurance or taxing insurance, and that regulation is contrary to the Sherman Act or the Clayton Act [or Federal Trade Commission Act], then the State law would be the law." 91 CONG. REC. 1481 (1945) (remarks of Senator Ferguson).

[20] 15 U.S.C. § 1012(b) (1952).

[21] "However, assuming there is some difference in the McCarran-Ferguson Act between 'legislation' and 'regulation', nothing in the language of that act or its legislative history supports the distinctions drawn by petitioner." 357 U.S. at 364.

[22] *Supra* note 7.

[23] NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS, 1958 Proc. Vol. II 328.

This act, which operates much like the non-resident motorists statutes, provides that insurance activity within a state by an unlicensed insurer authorizes a designated state official to accept service of process for the insurer. While this law enables state courts to assert jurisdiction in a properly brought litigation, it does not provide for any administrative jurisdiction by the state insurance department.

A law to remedy this situation, and one which goes far to cure the "constitutional infirmity", is now in force in seventeen states and the Territory of Hawaii. This legislation permits the insurance department of a state in which an insurance company is licensed to take administrative action against one of its licensed companies if it is doing business in a state in which it is unlicensed.[24]

While the State of Ohio has not enacted this statute, it has adopted all of the "Model Acts"[25] which have been prepared by the National Association of Insurance Commissioners.[26] Like her sister states, Ohio has not yet found any formal means of regulating advertising activities in Ohio conducted from outside the state by an unlicensed insurer.[27]

[24] This legislation is of two types. One is a reciprocal statute and is operative only between states which have passed the reciprocal statute. Examples of this type are UTAH CODE ANN. § 31-7-13 (1953), VA. CODE ANN. § 38.1-433 (1950). The other type permits the superintendent of insurance to take action against any licensed company when it is brought to his attention that the company is doing business in a state in which it is unlicensed. See ORE. REV. STAT. § 736.645 (1958).

[25] The State Fair Trade Practice Act, OHIO REV. CODE §§ 3901.19-.23 (1955); The Unauthorized Insurance Service of Process Act, OHIO REV. CODE § 3901.17 (1955); The Uniform Accident and Sickness Policy Provisions Law, OHIO REV. CODE §§ 3923.01-.99 (1956).

[26] These acts were prepared by the Association in an attempt to cover the fields left open to the states by the McCarran-Ferguson Act. The declaration of purpose of the State Fair Trade Practices Act, for example, says, "The purpose of this Act is to regulate trade practices in the business of insurance in accordance with the intent of Congress as expressed in the Act of Congress of March 9, 1945". NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS, 1947 Proc. 392-400.

[27] Nevertheless, Ohio uses some very effective informal means to control this situation. Among these might be mentioned the news release and personal communication by the Ohio Superintendent of Insurance with the like official in the home state of the offending insurer. Briefly, this is the operation:

a. *news release:* When it is brought to the attention of the department that an unlicensed insurer is soliciting business within Ohio, a news release is issued to radio and television stations and to newspapers within the area affected. In the release it is pointed out that X company is not licensed in Ohio and that the protection of Ohio insurance laws is not afforded to policyholders of the company. This generally has the effect of ending the campaign.

b. *personal communication:* When it appears to the Superintendent that the news release procedure is not, or is not likely to be effective, he will communicate directly with the commissioner of insurance of the home state of the offending company. This officer will then inform the company of the complaint which he has received from the Ohio Insurance Department and request that they cease

A general advertising statute[28] does give a large measure of control over advertising other than direct mail from another state.

It will be seen therefore, that the states have made strong efforts to keep the regulation of insurance in their own hands and to exclude federal regulation from the field. Through the widespread adoption of the reciprocity statute they may very well succeed. On the other hand, so long as the FTC maintains there is an area beyond which the states cannot constitutionally reach, it can be expected that the Commission will continue to assert its own jurisdistion in that area. The position of the FTC is best stated by a portion of its brief in the instant case. Quoting extensively from the *South-Eastern* decision they said:

> To the extent therefore, that the individual states, with their limited territorial jurisdictions [were] not fully capable of governing 'insurance' transactions which, reaching across state boundaries, affect the people of more states than one, that condition necessarily continued after enactment of the McCarran-Ferguson Act. The result, in the absence of federal legislation to fill the void is a legal vacuum—a 'no man's land' which is not effectively regulated either by the states or the federal government.[29]

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the offending activity. This too, is very effective. Personal interview, Ohio Superintendent of Insurance, Nov. 7, 1958.

[28] OHIO REV. CODE § 3905.43 (1953). "No person . . . shall publish or distribute or receive and print for publication or distribution any advertising matter in which insurance business is solicited unless such advertiser has complied with the law of this state regulating the business of insurance. . . ." Only recently, under this statute, a well known national weekly magazine was persuaded to drop as an advertiser an insurance company that was unlicensed in Ohio. While the Superintendent recognized that he could do nothing about copies of magazines which were mailed directly to subscribers in Ohio, he pointed out to the magazine that he had the authority to move against all local distribution by wholesale news operators in Ohio. Personal interview, Superintendent of Insurance, Nov. 7, 1958.

[29] Brief for Federal Trade Commission, pp. 42, 43.