

**PRELIMINARY REPORT OF THE ATTORNEYS GENERAL  
OF CALIFORNIA, MINNESOTA, MISSOURI, AND OKLAHOMA ON THE  
PROPOSED INTERSTATE INSURANCE PRODUCT REGULATION COMPACT:  
A CRITIQUE**

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The **Preliminary Report** is accurate in describing the proposed Interstate Insurance Product Regulation Compact as “a new plan for organizing government regulation” [p. 1] of the business of insurance, but is inaccurate in declaring “[a]n interstate compact is an unusual form of government...” [p. 6]. The compact does not establish a government and interstate compacts are a common means employed by states to cooperate with sister states on a variety of public matters including regulation. Furthermore, the report contains overgeneralizations, suggests sweeping tentative conclusions, and offers scenarios describable only as theoretically possible unless one concludes the proposed compact commission would act in reckless disregard of consumer interests. Nevertheless, the **Preliminary Report** raises questions that need to be considered by the drafters of the Compact.

**THE COMPACT COMMISSION: A PUBLIC OR A PRIVATE CORPORATION?**

The author(s) of the **Report** maintain the proposed compact would establish “a Private Corporation to Replace State or Federal Regulators of the Market Place for the Purpose of Consumer Protection” [p. 8]. The **Report** also contends “[t]he proposed compact offers a completely different model for government consumer protection regulation—a quasi-privatization” [p. 9], and would “vest in a private commission the authority of state government to protect consumers in the marketplace...” [p. 12] This conclusion completely ignores the

following declaration in section 2 of Article III of the compact: “The Commission is a body corporate comprising each Compacting State.”

Interstate compact commissions are public bodies. The 1990 Delaware-New Jersey Interstate Compact, for example, contains in Article IV a clear declaration of the nature of the Delaware River and Bay Authority by stipulating it “shall constitute an agency of government of the State of Delaware and the State of New Jersey for the following general purposes, and which shall be deemed to be exercising essential functions in effectuating such purposes, to wit:...”

The author(s) apparently have not read the unanimous decision of the New Hampshire Supreme Court, delivered by Chief Justice Allen, in *Ham v. Maine-New Hampshire Interstate Bridge Authority et al.* holding:

While it derives its powers and functions by a delegation of authority from the legislatures of two states, this fact does not change its character and modify it into standing as a private corporation. [92 N.H. 268 at 270, 30 A2d 1 at 3 (1943)].

The United States District Court for the Middle District of Pennsylvania in 1996 reached a similar conclusion relative to the Delaware River Port Authority (DRPA) and declared: “The DRPA is a public corporate instrumentality of the Commonwealth of Pennsylvania and the State of New Jersey” [Pievsky v. Ridge, 921 F.Supp. 1335 at 1341 (1996)].

## **UNCONSTITUTIONAL DELEGATION OF LEGISLATIVE POWERS?**

The **Report’s** author(s) suggest “The Proposed Compact May Violate State Constitutional Limits on the Delegation of Authority” [p. 15]. The **Report** accurately describes the only United States Supreme Court’s decision involving an interstate compact commission

and addressing the question of whether such a violation had occurred. The Court in *State ex rel. Dyer et al. v. Sims* [341 U.S. 22, 71 S.Ct. 557 (1951)], speaking through Justice Felix Frankfurter, reversed the decision of the Supreme Court of Appeals of West Virginia [58 S.E.2d 766 (1950)] holding the 1939 enactment of the Ohio River Valley Water Sanitation Compact [Chapter 38] invalid on the grounds the police power of West Virginia had been delegated to sister compact states and the Compact bound future State Legislatures to appropriate funds to the Compact Commission in violation of Section 4 of Article X of the West Virginia State Constitution prohibiting the contracting of debt by the State other than to meet casual deficits and other specified situations.

It is important to note the dissenting opinion of Judge Given, joined by Judge Riley, of the Supreme Court of West Virginia:

The compact...restricts the use of the police power of the State to the authorized representatives of this State, the members of the Commission appointed by this State, and subject to removal of such Commissioners by the Governor of this State....Thus, it will be seen, that the compact vests in the Commissioners representing this State, as such Commissioners and not as individuals, the sole and absolute power to exercise and control the police power delegated. That power is not to be, and in the nature of things cannot be exercised beyond the territorial limits of this State, and only courts within the jurisdiction of this State would have original jurisdiction in proceedings to enforce such orders. This being true, there could be no unlawful use or any unconstitutional delegation of any police power of this State. No language in the compact or the act can be

construed to “grant” or perpetually “alienate” any police power [134 W.Va. 278 at 301, 303, 58 S.E.2d 766 at 778-79].

Justice Frankfurter in *Dyer et al. v. Sims* explained: “A State cannot be its own ultimate judge in a controversy with a sister State. To determine the nature and scope of obligations as between States, whether they arise through the legislative means of compact or the ‘federal common law’ governing interstate controversies...is the function and duty of the Supreme Court of the Nation” [341 U.S. 22 at 28, 71 S.Ct. 557 at 569]. The Justice also cited the opinion of Justice Louis Brandeis in *Hinderlider v. La Plata River & Cherry Creek Ditch Company* [304 U.S. 92, 58 S.Ct. 803 (1938)] reversing the decision of the Colorado Supreme Court that an interstate compact enacted by the Colorado and New Mexico State Legislature was invalid because it had an impact on the water appropriations rights guaranteed by the Colorado State Constitution. Justice Frankfurter in *Sims* opined:

We find nothing ...to indicate that West Virginia may not solve a problem such as the control of river pollution by compact and by the delegation, if such it be, necessary to effectuate such solution by compact....The Compact involves a reasonable and carefully limited delegation of power to an interstate agency. Nothing in its Constitution suggests that, in dealing with the problem dealt with by the Compact, West Virginia must wait for the answer to be dictated by this Court after harassing and unsatisfactory litigation [341 U.S. 22 at 31, 71 S.Ct. 557 at 562].

Justice Frankfurter also explained “[t]he Compact was evidently drawn with great care to meet the problem of debt limitation” and concluded “the obligation of the State under the Compact is not in conflict with Art. X, §4 of the State Constitution” [341 U.S. 22 at 32, 71 S.Ct. 557 at 562-63].

There has been only one other dispute involving the failure of a party state to meet its contractual obligation to contribute funds to an interstate compact commission. The Commonwealth of Massachusetts in 1989 failed to provide the full amount of its contractually obligated funds to the New England Board of Education, but the dispute was settled through negotiations and the Commonwealth paid the arrears and subsequently has paid annually the current amount due under the compact.<sup>1</sup>

The Attorney General of Oregon was asked by the Public Utility Commissioner whether the Commercial Vehicle Safety Alliance, a voluntary organization of western states and one Canadian province, can take any action “on its own to preclude the necessity for member States to enact their own statutes or rules” prohibiting “the unauthorized manufacture, sale, or use of commercial motor vehicle safety inspection decals issued by the Public Utility Commissioner (PUC)?” The Attorney General in 1981 concluded the Alliance lacks such authority and added “member States may delegate such authority to the Alliance” [42 Or.Op.Atty.Gen.87, 1981 WL. 152269 (Or.A.G.)].

A 1999 decision of the North Carolina Court of Appeals does not involve an interstate compact, but does address the question of the delegation of rule making power by the North Carolina General Assembly to the State Insurance Commissioner. The Court held “the

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<sup>1</sup> Consult Joseph F. Zimmerman, *Interstate Cooperation: Compacts and Administrative Agreements* (Westport, CT: Praeger Publishers, 2002), pp. 82-83.

Commissioner had authority to promulgate and enforce the anti-subrogation rule and cited the 1978 opinion of the North Carolina Supreme Court positing “the constitutional inhibition against delegating legislature authority does not preclude the legislature from transferring adjudicative and rule-making powers to administrative bodies provided such transfers are accompanied by adequate guiding standards to govern the exercise of the delegated powers.” [*In the Matter of A Declaratory Ruling by the North Carolina Commissioner of Insurance Regarding 11 N.C.A.C. 12.0319*, 134 N.C.App. 22 at 38, 517 S.E.2d 134 at 145 (1999)], and *Adams v. North Carolina Department of Natural and Economic Resources*, 295 N.C. 683 at 697, 249 S.E.2d 402 at 410 (1978)].

Courts have made clear a state legislature may delegate rule-making powers to state administrative agencies provided the delegation is accompanied by adequate standards. Article I, §§1-7 (particularly §§1-2) and Article II, §15 of the proposed Interstate Insurance Product Regulation Compact establish adequate standards to be employed by the Compact Commission in its rule-making process.

Article XVI, §2(d) of this Compact specifically addresses the possibility a court might find a Compact provision exceeds the authority of a State Legislature under its State Constitution to delegate powers to the Compact Commission by stipulating “the obligations, duties, powers, or jurisdiction sought to be conferred by that provision upon the Commission shall be ineffective as to that Compacting State,…”

Based upon the evidence presented above, it is reasonable to conclude the probability of a court suit alleging a state legislature unconstitutionally delegated powers to the Compact Commission is remote and Article XVI, §2(d) would be applied should the court find for the plaintiff.

## IS CONGRESSIONAL CONSENT REQUIRED?

Section 10 of Article I of the United States Constitution contains an important stipulation: “No State shall, without the consent of Congress, enter into any Agreement or Compact with another State.” In consequence, there was a general assumption for decades that all interstate compacts enacted into law by the legislatures of two or more sister States are invalid in the absence of the consent of Congress. In 1893, however, the United States Supreme Court in *Virginia v. Tennessee* ruled congressional consent was mandatory only for a compact tending to increase “the political power and influence” of the party states and to encroach “upon the full and free exercise of federal authority” [138 U.S. 503 at 520, 13 S.Ct. 728 at 735-36 (1893)].

The author(s) of the **Preliminary Report** correctly note the United States Supreme Court in *United States Steel Corporation v. Multistate Tax Commission* in 1978 held the Multistate Tax Compact was constitutional despite the lack of congressional consent. The Court specifically opined the Compact does not “authorize the member states to exercise any powers they could not exercise in its absence” [434 U.S. 452 at 473, 98 S.Ct. 799 at 812-13 (1978)].

The **Report’s** author(s) contend States will have to submit the Insurance Product Regulation Compact “for Congressional consideration or live with the uncertainty of the compact’s validity lacking express Congressional authorization” [p. 5]. There is no evidence suggesting the compacting states would “exercise any powers they could not exercise” in the absence of the Compact and the author(s) admit in note 2 on page 5 “it could be argued that McCarran [spelling error corrected] Ferguson means that Congress has implicitly approved the compact and thus that Congressional approval is unnecessary because it already has been [spelling error corrected] provided.”

The author(s) on the same page misinterprets Zimmerman’s comment relative to the submittal of compacts to Congress for approval “even when such approval may not have been necessary” [p. 5]. Zimmerman wrote the 1921 Port of New York Authority Compact was submitted to Congress for approval “because bond counsels suggested congressional consent would make the authority’s bonds more appealing to investors who otherwise might be hesitant to purchase bonds issued by an unusual organization—an interstate public authority.”<sup>2</sup> There was no suggestion that the Compact needed Congressional consent in order to become constitutionally viable.

## **THE LEGAL STATUS OF INTERSTATE COMPACTS**

The author(s) of the **Preliminary Report** wrote “[a]n interstate compact is an unusual form of government that occupies “the ‘no man’s land’ between state and federal status” and cited a unsigned note in a 1998 law review [p. 6]. This statement reveals a lack of understanding of the nature of interstate compacts. No compact creates a “government,” the numerous interstate boundary compacts simply established a boundary line(s) between contiguous sister states and each such compact obviously did not create a “government” or a compact commission. Furthermore, thirty-four non-boundary compacts are administered by regular departments and agencies of the party states.

It is somewhat surprising there has not been more litigation involving interstate compacts, but this fact may be a reflection of the positive interstate cooperation brought about by non-boundary compacts to solve regional and national public problems. The Common Law of Interstate Compacts developed by the United States Supreme Court answers all but hypothetical questions about such concordats.

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<sup>2</sup> *Ibid.*, p. 50.

The **Preliminary Report's** expresses concern about “the rights of the compacting states or Congress to allow less than unanimous alteration or withdrawal from the compact” is insignificant [p.6]. Section 3 of Article XIII of the proposed Compact makes eminently clear each proposed Compact amendment requires the unanimous approval of the party States to be ratified and Article XIV spells out in detail the procedure to be followed by any State desiring to withdraw from the Interstate Compact. The **Preliminary Report** acknowledges States have “withdrawn from the Multistate Tax Compact and that withdrawal was an element of the compact” [p. 6, note 3]. States have withdrawn from several compacts. Florida, for example, has withdrawn from and rejoined the Atlantic States Marine Fisheries Compact on several occasions.

#### **CAN COMPACTS CREATE FEDERAL LAW OR PREEMPT STATE LAW?**

The author(s) of the **Preliminary Report** suggest a Interstate Compact lacking Congressional consent can be treated by courts as federal law and a Compact “treated as federal law” may contain provisions preempting state laws [p. 7]. It is pure speculation whether the United States Supreme Court would treat a Interstate Compact not consented to by Congress as federal law. To date, there is no evidence to support the speculation. Interstate Compacts, such as the proposed Interstate Insurance Product Regulation Compact, can preempt conflicting state laws and administrative rules and regulations as such preemption is at the heart of an Interstate Regulatory Compact designed to produce harmonious rules and regulations.

#### **EASE OF AMENDING INTERSTATE COMPACTS**

The author(s) of the **Preliminary Report** are correct in writing Interstate Compacts are difficult to amend and “Compacts are an exception to the rule that one legislature may not bind

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its successors” [p. 7]. The purpose of an Interstate Regulatory Compact is to establish a relatively permanent scheme of regulation and hence compact amendments should be infrequent.

### **SUNSHINE PROVISIONS**

The **Preliminary Report** is accurate in explaining Article VIII of the proposed Interstate Insurance Product Regulation Compact authorizes the Compact Commission “to determine procedures for public access to records” [p. 9], but contains no provision relating to open meetings of the Commission. The Compact empowers the Commission to “prescribe Bylaws to govern its conduct as may be necessary or appropriate to carry out the purposes, and exercise the powers, of the Compact...” [Art. V, §1(c)] and establish “reasonable procedures for calling and conducting meetings of the Commission, and ensuring reasonable notice of each such meeting;...” [Art. V, §1(c)(iv)].

This grant of authority to the Commission is consistent with provisions in other interstate compacts and encompasses the authority to adopt Bylaws providing for open meetings of the Commission and broad public access to records with a few specified exceptions specifically designed to protect the public’s interest, privacy of individuals, and trade secrets.

### **BORROWED STATE EMPLOYEES’ CIVIL SERVICE STATUS**

Relative to the Commission borrowing “employees of a Compacting State (Art. IV, §11), the **Preliminary Report** notes the “compact does not indicate whether the commission would be bound by the civil service status or related employment protections for ‘borrowed’ employees” [pp. 9-10].

Interstate cooperation is common on a wide range of public matters and States often have seconded their employees to sister states or interstate commissions for a specified period of time

for a variety of purposes including fighting forest fires, providing expertise to address a problem, and training. The civil service status of seconded state government employees, their compensation and benefits, and related matters are determined by interstate administrative agreements signed by the heads of the concerned state departments or agencies. There is no need to include a provision in the proposed compact relating to the civil service status of seconded employees.

### **ELEVENTH AMENDMENT IMMUNITY**

The **Preliminary Report** raises the question of the applicability of Eleventh Amendment immunity to the proposed Compact Commission (p. 12, note 10) and cites two conflicting court decisions.

The **Report** correctly describes the United States Supreme Court's decision in *Hess v. Port Authority Trans-Hudson Corporation* [523 U.S. 30, 115 S.Ct. 394 (1994)] holding the subsidiary of the Port Authority of New York and New Jersey was not cloaked with Eleventh Amendment immunity from suit. However, the **Report** fails to explain the reason for the Court's decision; *i.e.*, the subsidiary is a self-financing entity and allowing it to be sued in the United States District Court does not place a burden upon the New Jersey Treasury or the New York Treasury.

The **Report** also correctly describes the decision of the United States Court of Appeals for the Fourth Circuit in *Lizzi v. Alexander* [255 F.3d 128 (4<sup>th</sup> Cir. 2001)] that the Washington Metropolitan Area Transit Authority, established by an interstate compact with congressional consent, is cloaked with Eleventh Amendment immunity and such "conferral of Eleventh Amendment immunity on WMATA 'is compatible' with the holding in *Hess*..." [*Ibid*, at 132]. The court opined: "The signatories of the compact intended to confer Eleventh Amendment

immunity on WMATA.” [*Ibid.* at 130]. The case involved Authority employees terminated for unexcused absences who argued their termination violated provisions of the *Family and Medical Leave Act of 1993* [107 St. 6, 29 U.S.C. §2601]. The court concluded the Act “does not waive the agency’s Eleventh Amendment immunity from suit. And the FMLA does not validly abrogate a state’s Eleventh Amendment immunity” [*Ibid.* at 138].

The *Alexander* court commented on the reference in the *Hess* decision to the 1986 decision of the United States Circuit Court of Appeals for the District of Columbia Circuit in *Morris v. Washington Metropolitan Transit Authority* [781 F.2d 218 (D.C. Cir. 1986)] holding “Eleventh Amendment immunity was accorded” to the Transit Authority.

The Interstate Insurance Product Regulation Compact Commission will be financed entirely by fees paid by insurance companies when they file products with the Commission. Could the United States Supreme Court’s decision in *Hess* serve as a precedent in the event the Commission is sued? In theory, the *Hess* decision might be cited as a precedent, but the recent *Alexander* decision suggests the contrary.

Furthermore, a suit against the Commission is most improbable in light of the facts its authority is limited to (1) establishing product standards and (2) receiving filings by insurance companies. It is inconceivable that the Commission, composed of knowledgeable state insurance officers, would establish product standards lacking adequate protection for purchasers of insurance products. In fact, no regulatory interstate compact commission has been sued on the ground the commission established inadequate standards.

Suits will continue to be filed by policyholders against rogue insurance agents and brokers alleging the sale involved deceptive advertising or other misrepresentation and/or fraud

with respect to products approved by the Commission as meeting its standards. State Attorneys General will continue to have authority to bring such suits against insurance agents and brokers.

### **CAN THE PROPOSED COMPACT PREEMPT FEDERAL LAW?**

Congress has enacted several statutes allowing States to preempt the decision of a United States Government officer subject to a Congressional override [*Nuclear Waste Policy Act of 1982*, 96 Stat 2217, 42 U.S.C. §10135] or to opt-out of a federal mandate [*Department of Transportation Appropriation Act of 1990*, 104 Stat. 2185, 23 U.S.C. §104].

The **Preliminary Report** is accurate in quoting Zimmerman that “courts could interpret Congressional consent to a compact to repeal conflicting state law” [p. 23], but fails to explain the drafters of the Interstate Insurance Product Regulation Compact decided not to seek Congressional consent for the Compact.

A heading of the **Report** maintains “[t]he compact could preempt future state or federal laws related to insurance products approved by the commission.” [p. 24]. The **Report**, however, fails to provide any evidence to support its conclusion and its text contains no reference to preemption of federal laws.

### **ADMINISTRATIVE ISOLATION AND INDUSTRY INFLUENCE**

The **Preliminary Report** refers to Weldon V. Barton’s 1967 book that found the Interstate Oil Compact Commission [now Interstate Oil and Gas Compact] “has never acted to any significant extent independently of the oil industry” and “the Atlantic States Marine Fisheries Commission..., as well as the Oil Commission, “have been unable (or indisposed) to acquire and wield effective power over the ...groups which they ostensibly are designed to

regulate” [p. 29]. Barton’s conclusions may have been accurate at the time of the publication of his book, but they are not accurate today.

In 1976, Congress instructed the United States Attorney General to investigate whether advisory committees, established by the Interstate Oil and Gas Compact Commission, “could tend to create or maintain situations inconsistent with the antitrust laws of the United States.”<sup>3</sup> The Attorney General concluded in 1979 “it cannot be said that the industry representatives unduly influence the thrust of the position papers developed, since, as we have seen, virtually all the influential subcommittee members appear to view issues from the same general perspective.”<sup>4</sup> Congress initially limited its consent to the Compact, but expressed confidence in the Compact Commission in 1979 by removing the sunset clause from its consent.<sup>5</sup> A New York State Department of Environmental Conservation officer informed Zimmerman in 2002 that the Commission reflects the oil industry’s views on issues without advocating oil and gas development for its own sake.<sup>6</sup>

Zimmerman interviewed two officers who represent New York State on the Atlantic States Marine Fisheries Commission, which lacks regulatory authority, with one officer noting the Commission is above average in effectiveness and the other officer commenting the

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<sup>3</sup> “Extension of Interstate Compact to Conserve Energy,” 101 *Congressional Record*, May 2, 1979, p. S5192.

<sup>4</sup> *Ibid.* p. S5193.

<sup>5</sup> 86 Stat. 383 (1979).

<sup>6</sup> Zimmerman, *Interstate Cooperation*, p. 113.

Commission made the hard decisions that had to be made with the result the fisheries are improving.<sup>7</sup>

### **RECOMMENDED DELETION AND WORDING CHANGES**

1. Section 3 of Article III should be deleted. Reference in the section to “a not-for profit entity” is not necessary and can cause confusion with respect to whether the Commission is a public body or a private entity.
2. Section 2 of Article III should be reworded as follows: “The Commission is a body corporate and politic, and a instrumentality of the Compacting States.” In addition, the Commission could be described as a “Joint Public Agency.”
3. Consideration should be given to rewording Section 1(c)(iv) of Article V as follows: “iv. Providing reasonable procedures for calling and conducting meetings of the Commission, ensuring reasonable advance notice of each such meeting, and guaranteeing the right of citizens to attend each such meeting with enumerated exceptions designed to protect the public’s interest, the privacy of individuals, and commercial secrets.” **[Insert in the Compact or in the Bylaws the following:** “The Commission may meet in camera only after a majority of the entire membership votes to close a meeting *en toto* or in part. Within one day, the Commission must make public a copy of each such vote revealing the vote of each member with no proxy votes allowed”].<sup>8</sup>

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<sup>7</sup> *Ibid.*, pp. 105-06.

<sup>8</sup> Consult Joseph F. Zimmerman, *Curbing Unethical Behavior in Government* (Westport, CT: Greenwood Press, 1994), pp. pp. 123-42 and 222-23.

4. Consideration should be given to relettering subsection c(vii) of Article 5 as subsection c(viii) and adding: “c(vii): promulgating a code of ethics addressing actions that might be initiated by commission members and employees falling in the ‘gray’ area between clearly proper behavior and clearly illegal behavior.”<sup>9</sup>
5. Consideration should be given to the addition of the following subsection to Section 1 of Article 5: “d. The Commission shall publish its bylaws in a convenient form and file a copy thereof and a copy of any amendment thereto, with the appropriate agency or officer in each of the party States.”
6. Consideration should be given to adding the following sentence to the end of Article VII, §2: “The Commission in adopting a Uniform Standard shall consider fully all submitted materials and issue a concise explanation of its decision upon request.”
7. Consideration should be given to amending the wording of §1 of Article VIII as follows:  
“1. The Commission shall promulgate reasonable Rules establishing conditions and procedures promoting public inspection and copying of all of its data, information, and official records except data, information and records involving the privacy of individuals and commercial secrets.”

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<sup>9</sup> *Ibid.*, pp. 47-68 and 220.