STATE OF ARKANSAS
BUREAU OF
LEGISLATIVE RESEARCH

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HANDOUT 1

MEMORANDUM

TO: **Senator Jason Rapert**

FROM: **Alexandra N. Stephens**

DATE: **November 6, 2017**

SUBJECT: **Delegation of authority -- Use of "incorporation by reference"**

I am responding to your request for information concerning the following:

(1) Whether the practice of incorporation by reference is usurping the legislative role in Arkansas by making substantive changes to state insurance statutes;

(2) Has the practice of incorporation by reference resulted in substantive changes to Arkansas insurance statutes without legislative oversight or review; and

(3) Whether an Arkansas statute that incorporates all or part of a federal statute, a statute of another state by specific reference, or model language from another entity, along with future amendments or administrative regulations, is an unconstitutional delegation of legislative power.

BRIEF ANSWERS

Arkansas follows the general rule of statutory construction that, when a statute incorporates all or part of another statute of the same jurisdiction by a specific reference to the statute, subsequent modification or repeal of the referenced statute will not affect the incorporating statute unless the legislature clearly manifests a contrary intention. However, if the reference in an incorporating statute is to law of the same jurisdiction that is generally governing a particular subject, the statute adopts not only the law in force at the time the incorporating statute takes effect, but also that body of law as it exists from time to time thereafter.

Arkansas follows the general rule that when a legislature adopts a law or part of a law in the existing form in which it has already been enacted by another legislative body, there is no delegation of authority. However, if future amendments or administrative regulations are included in the incorporation, an unconstitutional delegation of authority has occurred.

The National Association of Insurance Commissioners is a nonprofit organization under the Internal Revenue Code of 1986, 26 U.S.C. § 501(c)(3). The National Association of Insurance Commissioners states it is a regulatory support organization composed of insurance regulators from all fifty (50) states, the District of Columbia, and five (5) United States territories. Through the National Association of Insurance Commissioners, state regulators

establish standards and best practices to promote uniformity of insurance regulation in the United States.

The General Assembly has delegated authority to the Insurance Commissioner to adopt rules and regulations, including those proposed by the National Association of Insurance Commissioners. The Arkansas Code has over seventy-five (75) references to instructions and manuals that are adopted by the National Association of Insurance Commissioners and includes those that are amended by the National Association of Insurance Commissioners. The Insurance Commissioner is appointed by the Governor of Arkansas. The adoption of certain standards by an executive appointee raises the issue of whether there may be an unconstitutional delegation of authority with reference to instructions and manuals incorporated by reference from the National Association of Insurance Commissioners. However, such practices may be permissible with appropriate legislative oversight. These type of delegation issues have arisen in the past and the outcome of each case depended on the specific facts of each situation. The question of whether the current statutory scheme in Arkansas constitutes appropriate legislative oversight has not been considered by a court of law. This memo sets out the legal analysis that a court would use when examining the issue. If the General Assembly wished to amend the current statutory process for adopting NAIC publications to lessen potential delegation concerns, there are other alternatives to consider, including adopting the publications statutorily each session or imposing more stringent oversight, including appearances by the Insurance Commissioner before legislative committees when adopting new standards or the occurrence of certain triggers or prerequisites before the adoption of new publications.

DISCUSSION

The powers of the government of the state of Arkansas is divided among three departments:

(1) The legislative department, to enact the laws of the state;

(2) The executive department, to implement and administer the laws enacted; and

(3) The judicial department, to interpret the state constitution and laws enacted.

Delegation of legislative power is used in limited instances and varies between the states. It is unrealistic to expect state legislatures to review and approve every detail of policy. The questions that should be addressed are which powers may be delegated, to whom, and the scope of the delegation. It is important for a state legislature to provide specific guidance and standards to follow to ensure the will of the legislature when implementing the details of policy contained in legislation.

A common device in drafting legislation is to incorporate all or part of the provisions of another statute by a specific reference to the statute. Advantages are obvious. In addition to convenience for the drafter, statute books and codes are not encumbered by unnecessary repetition. While a considerable number of states have adopted constitutional restraints on such referencing legislation in an attempt to curb potential abuse of the device by those legislators who may take advantage, most courts do not give these constitutional restrictions rigid effect. 1A.N. Singer, *Sutherland on Statutory Construction* 805 (5th ed. 1993).

I. Incorporation of Arkansas Law

One example of such constitutional restraint is found in Article 5, § 23 of the Arkansas Constitution, which states that "No law shall be revived, amended, or the provisions thereof extended or conferred by reference to its title only; but so much thereof as is revived, amended, extended or conferred shall be reenacted and published at length." But, in *Austin v. Manning*, 217 Ark. 538 (1950), the Arkansas Supreme Court held that this section of the constitution does not prohibit cross-references to other statutes governing related matter not actually revived, amended, extended, or conferred by the particular enactment. The court concluded that if such acts were not held valid, legislation would become very cumbersome and difficult.

It is a general rule of statutory construction that, if a statute incorporates all or part of another statute of the same jurisdiction by a specific and descriptive reference to the other statute, such incorporation takes the referenced statute as it exists on the date the referring statute becomes effective. The referring statute will not be affected by subsequent modification or repeal of the referenced statute unless the legislature clearly manifests a contrary intention. There is a qualification to the general rule, however, when a statute incorporates law of the same jurisdiction generally governing a particular subject and does not refer to any specific statute. Such incorporation encompasses not only the law in force on the effective date of the referring statute but the law as it exists from time to time thereafter. 73 Am. Jur. 2d *Statutes* § 29 (1974).

Arkansas follows both the general rule of statutory construction and its qualification. The Arkansas Supreme Court applied the general rule in *Bolar v. Cavaness*, 271 Ark. 69 (1980), a case involving the deadline for challenging the sufficiency of petitions for a local option election. The controlling statute was originally enacted as Act 341 of 1977 and stated that petitions must be circulated and sufficiency thereof determined in the same manner and procedure as provided in Act 4 of 1935 for initiated county measures. The 1935 act was subsequently repealed by Act 742 of 1977. The court held, however, that it had been incorporated as part of the local option procedure by specific reference and operation of the adopting statute was not affected by the later repeal of the incorporated statute.

The leading Arkansas case for the qualification to the general rule is *Howard v. State*, 223 Ark.634 (1954), where the issue was whether the defendant in a bastardy proceeding had made a timely appeal to the circuit court from the decision of the county court. The controlling statute stated that the deadline for appeal to circuit court from the county court in bastardy cases was the same as an appeal to circuit court from a justice of the peace court. The Arkansas Supreme Court held that the statute had incorporated the general law governing appeals from justice of the peace courts and not a specific law in force at the time the statute was enacted. As a result, any subsequent modifications of the appeal procedure from a justice of the peace court would also be adopted by the controlling statute.

II. Incorporation of Federal Law

Another question in drafting referential legislation may arise when an Arkansas statute incorporates all or part of the precepts of another law-making body such as Congress or another state legislature. Has an unconstitutional delegation of legislative authority occurred? The general rule is that, when a legislature adopts a law or part of a law in the existing form in which it has already been enacted by another legislative body, there is clearly no delegation. On the

other hand, if future amendments, rules or regulations are included in the incorporation, it is equally clear that a delegation of authority has occurred. Singer, *supra*, at 806-07.

Arkansas follows the general rule, as illustrated in the following cases. In *McLeod v. Commercial National Bank*, 206 Ark. 1086 (1944), the Arkansas Supreme Court held that a 1941 Arkansas act defining "gross estate" as that determinable under the "applicable" federal revenue act had only adopted provisions of the 1939 federal act that were in force in 1941. The court refused to presume, without evidence of express or implied legislative intent otherwise, that the General Assembly intended to delegate future exemptions to Congress. But, in *Cheney v. St. Louis Southwestern Railway Co.*, 239 Ark. 870 (1965), the court found a state income tax statute, enacted as part of the Arkansas Income Tax Law of 1929, unconstitutional as an illegal delegation of legislative power to the federal government in violation of Article 5, § 1, and Article 4, §§ 1 and 2 of the Arkansas Constitution. Under the statute's terms, the state tax liability of certain corporations was determined under the Interstate Commerce Act pursuant to the Interstate Commerce Commission's standard classification of accounts. The court held that this classification had changed over the years and was not the same standard that existed in 1928, hence the unlawful delegation of authority.

III. "As it existed" language

The purpose of using the "as it existed" language is to establish the reference to the federal law as of a certain date. With respect to legislation or administrative rules (or other matters) not originating with a particular legislative body that is referenced in or incorporated into a statute adopted by that particular legislative body, many people think that as the referenced or incorporated legislation and administrative rules are amended, that the amended version effectively amends or modifies the referencing or incorporating legislation as well. In Arkansas, as in most states, that is considered an unconstitutional delegation of legislative power.

The leading Arkansas case is *Crowly v. Thornbrough*, 226 Ark. 768, 294 S.W.2d 62 (1956). Acts 1955, No. 115, required that the advertised specifications for every contract to which the state, or any county, city or town, or any taxing agency was a party, for construction, alteration, or repair of public buildings or works, and which contract involved employment of mechanics and laborers, had to contain a provision that the minimum wages to be paid were to be based upon the wages determined by the United States Secretary of Labor to be the prevailing wage rate for the corresponding classes of laborers and mechanics on projects of a character similar to the contract work in the particular area in which the work was to be performed. Every contract had to include a stipulation that the contractor would pay the workers the wage rates per the advertised specifications. The wage scale had be posted by the contractor in a prominent spot at the job site. Essentially, the General Assembly wanted to piggyback onto the federal prevailing wage rate law with respect to state and local taxpayer paid construction projects. The Arkansas Supreme Court struck down Acts 1955, No. 115, as being unconstitutional for several reasons, including the following:

> The Act fails to establish a standard or formula by which a wage scale may be formulated; but rather delegates to the Secretary of Labor of the United States the right to fix the minimum wage scale to be paid in a particular area of this State. The State retains no control over the Secretary of Labor of the United States, therefore the Act violates Article 4, Sections 1, 2 and Amendment 7 [Article 5, Section 1] to our State Constitution. Numerous decisions from other states have held similar legislation to be an

> unconstitutional delegation of legislative authority to an agency of the United States Government. *Hutchins v. Mayo*, 143 Fla. 707, 197 So. 495, 133 A. L. R. 394; *Smithberger v. Banning*, 129 Neb. 651, 262 N. W. 492, 100 A. L. R. 686; *State v. Gauthier*, 121 Me. 522, 118 A. 380, 26 A. L. R. 652; *Holgate Bros. Co. v. Bashore*, 331 Pa. 225, 200 A. 672, 117 A. L. R. 639. *Crowly v. Thornbrough*, 226 Ark. 768, 774, 294 S.W.2d 62, 66 (1956). (Bracketed language added)

To make it clear that the General Assembly is not delegating legislative power unconstitutionally, the Bureau of Legislative Research adheres to a policy that states that legislation should include a date certain for referenced or incorporated legislation and administrative rules. Under Section 4.5(b) of the Legislative Drafting Manual, Bureau of Legislative Research, concerning adoption of federal laws or regulations or the adoption of industry standards by reference, it states:

> If the bill adopts federal law or regulations or adopts the standards or manual of a private entity, avoid adopting future revisions of the document referenced. If future changes are included in the incorporation by reference, a delegation of authority has occurred.

If the referenced or incorporated legislation and administrative rules be amended or repealed, then the referencing or incorporating legislation should be amended with a new, later date certain. This drafting technique is usually illustrated in Title 26 Taxation. Whenever legislation is drafted that incorporates provisions of the Internal Revenue Code, the Bureau of Legislative Research sets out a specific date for that particular version of the Internal Revenue Code.

IV. Arkansas Attorney General Opinions

Arkansas Attorney General Opinion No. 95-008, the Attorney General opined that it violated the separation of powers doctrine set forth in Ark. Const. art 4, §§ 1 and 2, for the legislature to adopt by reference future editions of the Standard Building Code:

> It is generally stated, pursuant to this doctrine, that the legislature may confer discretion in the administration of the law. It may not, however, delegate the exercise of its discretion as to what the law shall be. 16 C.J.S. *Constitutional Law* § 137 (1984).

A previous opinion issued as Arkansas Attorney General Opinion No. 88-332, states that a delegation of authority to the United States Congress is invalid. Both opinions discussed *Terrell v. Loomis*, 235 S.W.2d 961 (Ark. 1951), quoting it as follows:

> Appellant argues that 93 is unconstitutional as an unlawful delegation of legislative authority to the Commissioner of Revenues. The applicable rule is stated in State v. Davis, 178 Ark. 153, 10 S.W.2d 513, as follows: 'While it is a doctrine of universal application that the functions of the Legislature must be exercised by it alone, and cannot be delegated, it is equally well settled that the Legislature may delegate to executive officers the power to determine certain facts, or the happening of a certain contingency, on which the operation of the statute is by its terms made to depend. [Citations omitted.]'

The opinion also discusses the lawful delegations that involve an executive official, such as the Insurance Commissioner, and the executive official's judgment. Under the opinion, it appears that the General Assembly could delegate authority to the executive official to decide

whether to certify that a trigger or appropriate prerequisites have been satisfied that allow for the application of a standard as established by the General Assembly.

The Arkansas Attorney General issued Opinion No. 2000-117 concerning an unconstitutional delegation of power from one (1) legislative body to another. The Attorney General opinion explained with respect to *Terrell v. Loomis*:

> These formulations illustrate that the contingency upon which the General Assembly can condition a law is some yet to be determined but existing state of facts, such as the will of the electorate, not a future exercise of discretion by some entity other than the legislature itself.

V. NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS

It is not uncommon for potential issues with delegation and incorporation by reference to arise when considering regulated industries that interact with standards and regulations drafted by national regulatory or accrediting agencies. While such statutory arrangements can create concerns, the Arkansas Supreme Court has held that such delegations are not de facto impermissible – the question would be fact-specific and require a study of the nature of the delegation and the amount of authority and oversight retained by the General Assembly. The General Assembly has adopted a statutory scheme that addresses the standards and requirements of the National Association of Insurance Commissioners.

In Arkansas, rules and regulations concerning insurance matters are addressed under § 23-61-108. This section authorizes the Insurance Commissioner to make reasonable rules and regulations that are necessary to carry out the Arkansas Insurance Code. Subsections (d) and (e) of § 23-61-108 states:

> (d)(1) The commissioner is authorized to employ the standards and requirements set forth in publications recited in the Arkansas Insurance Code, as those publications existed on January 1, 2001, and adopted and published by the National Association of Insurance Commissioners or by other authors in the regulation of insurance, including, but not limited to, the Valuation of Securities Manual, the examiners handbook, the Accounting Practices and Procedures Manual, and the Annual Statement Instructions as published by the National Association of Insurance Commissioners.
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> (2) The publications identified in subdivision (d)(1) of this section and others recited in and throughout § 23-60-101 et seq. are hereby adopted as they existed on January 1, 2001.
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> (3) The commissioner is authorized and empowered to promulgate regulations for the purposes of adopting all or part of other publications of the National Association of Insurance Commissioners or publications by other authors if the commissioner determines that such an action is in the best interest of the public.
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> (4) Upon the mailing of written notice by the commissioner to all domestic reporting entities of promulgation and publication by the National Association of Insurance Commissioners or other authors of amendments, revisions, or modifications to any publication previously adopted by the commissioner in the Arkansas Insurance Code, such published amendments, revisions, or modifications shall become effective on the date designated by the commissioner in the written notice, which date shall not be earlier than eight (8) months after the date of mailing of the notice.

> (e) The commissioner is authorized and empowered to adopt regulations for the purpose of modifying, amending, or revising any publication promulgated by the National Association of Insurance Commissioners or other authors, or any published amendments, modifications, or revisions to any such publications if the commissioner determines that such an action is in the best interest of the public. In such an event the effective date of any modification, amendment, or revision shall be the effective date of the regulation.

Under § 23-61-108(d)(3), the General Assembly has authorized the Insurance Commissioner, an appointed state official in charge of regulating the insurance industry in Arkansas, to promulgate rules for the purposes of adopting publications of the National Association of Insurance Commissioners if the commissioner determines that it is in the best interest of the public to do so. The commissioner is also required to provide written notice to domestic reporting entities if a revised or amended publication is used pursuant to § 23-61-108(d)(4). However, the notice is provided to domestic reporting entities and not provided to all reporting entities.

Although the National Association of Insurance Commissioners has established goals to have uniform standards and best practices to promote uniformity of insurance regulation, the revisions that are made to manuals and instructions may include substantive changes to Arkansas law. The General Assembly does not review every revision during a regular session but has adopted § 23-61-108. Section 23-61-108 allows the Insurance Commissioner to adopt rules and regulations, including those of the National Association of Insurance Commissioners, to implement the Arkansas Insurance Code. The Insurance Commissioner is appointed by the Governor of Arkansas. Section 23-61-108 and its delegation of authority to the Insurance Commissioner allows the commissioner to adopt and apply standards drafted by a private entity that were not in existence at the time of the legislative delegation.

Without the appropriate legislative oversight, deferral to a private entity appears to be an unconstitutional delegation of authority. While some might argue the statutory scheme under § 23-61-108 constitutes a violation of the separation of powers doctrine and an unlawful delegation, courts have illustrated it is possible to create a lawful delegation in such instances. The General Assembly has clearly addressed the issue and attempted to structure a mechanism to account for the adoption of National Association of Insurance Commissioner standards and regulations – this mechanism allows for the adoption of NAIC policies at the administrative level.

The Arkansas Supreme Court has not considered the constitutionality of § 23-61-108 and all statutes of the General Assembly are presumed constitutional until deemed otherwise. A challenge to the statute would be fact-intensive and consider the issues raised in this memorandum. However, there are options available if the General Assembly wished to adopt a mechanism that lessened delegation concerns by minimizing possible substantive changes to law and policy at the administrative level. These options would include adopting NAIC publications by law using "as it existed" language or providing for greater oversight. This could include the appearance of the Insurance Commissioner before legislative committees when adopting new policies or establishing certain triggers or prerequisites to authorize the adoption of new publications.