

TECHNICAL ADVISORY

INDEPENDENT INSURANCE AGENTS OF LOUISIANA

TA 132

December 7, 1998

SUBJECT: Criminal Liability for an Associate's Record
"Dishonest or Breach of Trust" in 18 U.S.C. §1033

BACKGROUND: The following article was prepared by Ann Monaco Warren and John William Simon, members of the law firm of English & Monaco, P.C., Jefferson City and Lake Ozark, Missouri, for the *Missouri Agent* publication. The authors have granted IIAL permission to reprint the article.

Warren is the author of the chapter on insurance regulation in Missouri Bar's official manual of insurance practice. She has served as executive director of the Surplus Lines Association of Missouri and is past president of the Mid-America Claims Association of Missouri. Simon has served as chair of the Criminal Law Committee of the Missouri Bar and is a board member of the Missouri Association of Criminal Defense Lawyers.

MAIN POINTS: As part of the 1994 Crime Bill, Congress adopted an unprecedented federal statute regulating employment in the insurance industry. On behalf of the insurance regulatory bar, the authors of this article call the attention of insurance agents and other insurance professionals to the potential for exposure to criminal prosecution under this statute.

FELONY. Subsection (e) of the newly enacted 18 U.S.C. §1033 makes it a federal crime for a person to engage in the business of insurance if the person has been convicted of "any criminal felony involving dishonesty or a breach of trust" or of "an offense under this section." It also makes it a felony to "willfully permit" another person to engage in the business of insurance. The subsection allows a person with such a criminal record to be employed in the insurance industry if the person has received the written consent of "any insurance regulatory official authorized to regulate the insurer, which consent specifically refers to this subsection." This statute provides for a prison sentence of up to and including five (5) years for anyone who works in the insurance industry, or "willfully permits" another to work in it, in violation of this subsection.

Subsection (e) of section 1033 creates the potential for a lifetime of exposure to criminal liability in the business of insurance, if not actual exclusion to

criminal liability in the business of insurance, if not actual exclusion from it. It applies to anyone who has a felony conviction “involving dishonesty or breach of trust.” Although subsection (e) provides for one means of lifting this disability to serious criminal liability whenever his or her company merges or expands.

Subsection 1033’s proscription of former felons was a relatively minor part of a larger bill, H.R. 665. The bill was aimed at fraud by insurance executives.

In his capacity as Chairman of the Oversight and Investigations Subcommittee of the House Energy and Commerce Committee, Congressman John Dingle of Michigan conducted hearings over five to six years that resulted in H.R. 665. As he observed on the floor of the House:

“Failed Promises.” In February 1990, the subcommittee focused public attention on the need for Federal criminal legislation with its report, “Failed Promises.” In this report, the subcommittee examined four major insurance company failures and concluded that existing State remedies were ineffective against the fraudulent behaviors that drove these companies into solvency.

The National Association of Insurance Commissioners (NAIC) was a principal advocate for the statute. In the *Guidelines for State Insurance Regulators to the Violent Crime Control and Law Enforcement Act of 1994: 18 United States Code Sections 1033 and 1034 - December 1997* (draft of Dec. 8, 1997) (“NAIC Guidelines”), the Antifraud Special Issues Committee of the NAIC indicated that “[t]he NAIC has been proposing legislation like this to members of Congress since April 1991.” It explained that [t]he NAIC originally proposed this type of Federal insurance fraud statute because of the power of the Federal government to bring additional jurisdictional, investigatory and law enforcement resources to bear in combating insurance fraud.” Although the criminal jurisdiction the subsection invokes is federal, the subsection authorizes state regulators - such as the members of NAIC - to grant dispensations.

Substantive Crimes. Subsections (a)-(d) of section 1033 of title 18 of the United States Code create four (4) substantive crimes involving the business of insurance. These include making false statements to regulators for the purpose of affecting their decisions or false entries in books or reports with the intent to deceive anyone about a company’s financial condition, as well as embezzling and using force or threats of force in connection with insurance regulation and the business of insurance. For any of these substantive offenses, section 1033 provides for imprisonment up to and including ten years. If the conduct in question “jeopardized the safety and soundness of an insurer and was a significant cause of such insurer being placed in conservation, rehabilitation, or liquidation,” the imprisonment can extend to

fifteen years.

One of the most central and most controversial phrases in the new statute is “felony conviction involving dishonesty or breach of trust.” As the NAIC Guidelines point out, Congress took this language from “several Federal statutes, including provisions relating to Federally insured banks, savings and loans, and credit union, the farm credit system, small business investment companies, and the rural business investment fund.” The principal statutes that include this language are twelve U.S.C. §§ 1818(g) & 1829. The Guidelines point out, as well, that in one case construing the same language in another statute, a federal court held that the federal agency could determine whether a conviction fell within the statutory language.

NAIC Guidelines. From this decision, the NAIC Guidelines draw the inference that each state insurance commissioner has the discretion to decide whether a conviction was for a felony “involving a dishonesty or breach of trust.” On the theory that the NAIC Guidelines advance, a state insurance commissioner’s decision that a given offense “involve[d] dishonesty or breach of trust” would be reviewable in the judicial courts only for “arbitrary or capricious” determinations.

A second battleground in the new statute is “any insurance regulatory official authorized to regulate the insurer.” Read as Congress passed it, this language authorizing an insurance regulator to give a convicted felon permission to work in the insurance industry says that “any” insurance regulator who has the authority to regulate “the insurer” may do so. Paragraph (2) of subsection (f) defines the “insurer” to include both an entity employing the person with the conviction and the person himself or herself.

Penal statutes must be strictly construed against the sovereign and in favor of the accused citizen. The text of the statute indicates that if a person with a felony conviction were an officer or employee of an insurance company doing business in all fifty states, the insurance commissioner of “any” state could give him or her written permission to engage in the business of insurance in all fifty states.

“Standards of Review.” Not so, say the NAIC Guidelines. A majority of the “working group” which prepared the NAIC Guidelines has proposed that NAIC members should adopt “Standards of Review” under which the regulators will decide where an insurance professional with a felony conviction must apply for “written consent,” and that if the commissioner in the jurisdiction the regulators choose turns down the application, the person would not be able to engage in the business of insurance in any jurisdiction.

What remedies are available to a person who has a felony record that a federal

prosecutor might find to fall within the statute? What remedies are available to a company that wishes to employ such a person?

Paragraph (2) of subsection (e) provides that person whom paragraph (1) bars from the business of insurance may engage in it “if such person has the written consent of any insurance regulatory official authorized to regulate the insurer, which consent specifically refers to this subsection.”

“Written Consent.” There is a broad range of opinion about who may give “written consent” under this provision. If the NAIC Working Group has its way, an insurance professional with a criminal conviction in his or her past will be forced into a forum not of his or her choosing, with the state regulator’s determination reviewable only under a highly deferential standard. Such a remedial structure could result in many qualified applicants’ being denied the right to do their jobs.

By contrast with the specific and limited relief of “written consent” from one or more regulators, a pardon removes the need for even asking what convictions the statute covers or which regulator may give consent to do business in spite of them.

Pardon. Under subsection (e), the disqualification from engaging in the business of insurance depends on the existence of the conviction. The Full Faith and Credit Clause of the United States Constitution contains no exception for pardons: a regulator in one state must give effect to another state’s executive’s pardon of an offense against the laws of the pardoning state. Once the insurance professional established that he or she had been pardoned by the state whose laws he or she had been convicted of violating, the regulator would have no cause to inquire into the application of subsection (e).

A pardon has several independent advantages over regulatory action under paragraph (2) of that subsection. Under the Federal Rules of Evidence, a pardon on grounds that an insurance person has been rehabilitated or that he or she was innocent of the offense in the first place makes the conviction inadmissible to impeach his or her credibility as a witness. In addition, a pardon removes the conviction as a disqualification under any state statute that makes the existence of a conviction a bar to engaging in the business of insurance.

IIAL Note: The Federal prosecutors in New Orleans recently asked the Louisiana Department of Insurance (LDI) to refer all license applications which indicated prior convictions for investigation. Federal prosecutors have promised a very aggressive campaign to investigate and prosecute persons who fall within the terms of 18 U.S.C. § 1033.

**NECESSARY
ACTION:**

IIAL urges its members to familiarize themselves with this valuable information and take appropriate steps to determine if any agency employees violate the terms of 18 U.S.C. § 1033, so that you can take steps to protect the agency against possible liability.