

NOV 8 1994



OFFICE OF THE COMMISSIONER

STATE OF MINNESOTA

DEPARTMENT OF COMMERCE

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November 7, 1994

Ms. Maryanne V. Hruby
Executive Director
Legislative Commission to Review Administrative Rules
55 State Office Building
100 Constitution Avenue
St. Paul, Minnesota 55155

Re: Proposed Permanent Rules Governing Self-Insurance Plan Administrators

Dear Ms. Hruby:

The Minnesota Department of Commerce intends to adopt rules. The Notice of Intent To Adopt Rules will appear in the State Register on November 7, 1994.

As required by Minnesota Statutes, sections 14.131 and 14.23, the Department has prepared a Statement of Need and Reasonableness which is now available to the public. A copy of this Statement is enclosed with this letter.

For your information, we are also enclosing a copy of the Notice of Intent to Adopt Rules and a copy of the proposed Rules in this matter.

If you have any questions about these rules, please contact me at 296-6593.

Sincerely,

JAMES E. ULLAND
Commissioner of Commerce

By:

A handwritten signature in cursive script that reads "Donna M. Watz".

Donna M. Watz
Staff Attorney

DMW/da
Enclosure

**STATE OF MINNESOTA
DEPARTMENT OF COMMERCE**

**In the Matter of the Proposed Adoption
of Rules Governing Self-Insurance Plan
Administrators**

**STATEMENT OF NEED
AND REASONABLENESS**

I. INTRODUCTION AND STATEMENT OF AUTHORITY

Minnesota Statutes section 60A.23, subdivision 8 authorizes the commissioner of commerce to license and regulate the activities of vendors of risk management services and any entity administering for compensation self-insurance or insurance plans. Clause (5) of Minnesota Statutes section 60A.23, subdivision 8 grants to the commissioner the authority to adopt rules to carry out the purposes of this subdivision 8, including the authority to adopt rules that:

- (a) establish reporting requirements for administrators of insurance or self-insurance plans;
- (b) establish standards and guidelines to assure the adequacy of financing, reinsuring, and administration of insurance or self-insurance plans;
- (c) establish bonding requirements or other provisions assuring the financial integrity of entities administering insurance or self-insurance plans; or
- (d) establish other reasonable requirements to further the purposes of this subdivision.

Rules governing self-insurance plan administrators (or third party administrators as they are sometimes called) under Minnesota Rules Part 2767 (1993) were adopted in May 1985 pursuant to this authority. The rules currently being proposed are amendments to the rules previously adopted. These amendments are proposed pursuant to the authority granted to the commissioner under Minnesota Statutes sections 60A.23, subdivision 8 and 45.023.

As set forth under Minnesota Rules Part 2767.0200, the rules are designed to assure that third party administrators are capable of providing risk management services, are financially solvent and are able to process claims in a prompt and equitable manner. The rules are also designed to allow the commissioner to authorize qualified entities to engage in the business in a manner which is fair, equitable, and consistent with all applicable Minnesota statutes. By statute, the commissioner can grant a license only when the commissioner is satisfied that the entity possesses the necessary organization, background, expertise and financial integrity to supply the services sought to be offered.

Over the past several years, department staff has become aware of the financial hardship on small third party administrators of having financial statements prepared and certified by independent certified public accountants (CPAs). Under current rules, only companies who have gross income under \$15,000 per year can have the requirement (to submit certified financial statements) waived. Based on a review of the license applications filed within the last five years, the department has determined that very few companies can take advantage of the less stringent reporting requirement because the threshold of \$15,000 is too low. The department feels that a higher threshold can be established to assist smaller businesses, and businesses who do a small amount of their national business in Minnesota, without affecting the protections afforded to Minnesota residents and consumers under Minnesota Statutes section 60A.23, subdivision 8. Even with the increased threshold to \$100,000, the commissioner is satisfied that an entity providing reviewed financial statements (in lieu of certified financial statements) will be in a position to show the necessary financial integrity to supply the services sought. In addition, by raising the threshold to \$100,000, the commissioner believes that smaller companies will be allowed to engage in business in Minnesota in a more fair and equitable manner, and consistent with all applicable Minnesota statutes.

Other changes to the rules, described more fully below, are intended to clarify certain portions of the rules and underlying statutes.

II. FACTS ESTABLISHING NEED AND REASONABLENESS

All of the proposed changes described below pertain to Minnesota Rules Part 2767.0600 regarding license renewals of third party administrators.

Subpart 2. Required Information

Clause E of subpart 2 contains a number of amendments. The insertion of the language "... of the administrator or the parent guarantor, if applicable" is necessary to clarify whose financial statements must be submitted with the renewal application. If the third party administrator has a parental performance guarantee, it is essential that the parent company submit its own financial statements, since it is the parent's financial strength supporting the performance of the subsidiary third party administrator. Without this amendment, the requirement is ambiguous and confusing.

Under clause E, the word "renewal" has been added as a technical clarification. This change is necessary to be sure that applicants differentiate between requirements for initial license applications and applications for renewal licenses.

Under clause E, the word "company" has been changed to "administrator". This is a technical change for clarification purposes. It clarifies that it is the gross income of the third party administrator, not its parent company or other related company, that will be used as a basis for determining whether a waiver of the financial statement requirement

can be sought. This amendment is necessary because of the addition of the reference to parent guarantor earlier in clause E.

The insertion of "from sources within the state of Minnesota" is a technical clarification. The language identifies what revenue is being considered in the determination of the level of financial statement presentation that is required. It is reasonable and necessary to include such language in the rule to clearly set forth for applicants what standards are being used by the department.

Under clause E, the substitution of "\$100,000" for "\$15,000" is an increase in the threshold of gross income used to determine what level of financial statement presentation is required to accompany the license renewal application. Under the proposed rule, those third party administrators whose gross income from sources within the state of Minnesota is less than \$100,000 will be allowed to present "reviewed financial statements" prepared by a CPA, which are less of a financial burden on the applicant than the "certified audited financial statements" required of those whose gross income is over \$100,000.

In reviewing renewal applications filed over the past five years, department analysts have concluded that very few companies can take advantage of the less stringent reporting requirements because the threshold of \$15,000 is too low. By increasing the threshold to \$100,000, the department expects that "start-up" companies, or companies doing a limited amount of business in Minnesota will benefit by reduced costs of financial statement preparation (charged by CPAs) as part of the license renewal process. The department has determined that the increase to the \$100,000 threshold level is reasonable, based on an analysis of current licensees. The department believes that at the present time, it is prudent to continue to require the higher level of financial statement review for companies that have gross income from sources within Minnesota in excess of \$100,000, because of potential risk to Minnesota clients and consumers should the administrator become insolvent. The department intends to continually monitor the effect of the proposed increased threshold, and it will recommend further adjustment or increases in the threshold if needed. The department prefers to proceed cautiously by increasing the threshold in increments rather than making a change that could harm Minnesota clients and consumers.

Clause E contains further technical corrections under subclause 1. The substitution of "reviewed financial statements" for "a review audit" is a technical change clarifying what type of statements must be submitted to obtain a waiver. The current language under the rule is ambiguous in that a "review" is one level of presentation and "audit" is another level. The amendment is needed to avoid confusion and clearly set forth standards for the applicant.

The substitution of the phrase "... those reviewed financial statements along with ..." in place of "... the review letter pursuant to the audit and ..." is necessary to avoid confusion among applicants. There have been instances when the renewal license applicant has read this provision quite literally and failed to file the actual financial

statements along with the CPA's letter (which describes the level of work the CPA performed.). In order for the department to review and evaluate the financial statements of the applicant, the department must have copies of the financial statements, not just the review letter. The proposed amendment to the rule clarifies what was originally intended when the rule was adopted.

Clause E is being amended to add a new subclause (2). This new provision allows the applicant to post a surety bond in lieu of financial statements, at the applicant's option. This alternative allows flexibility to the third party administrator to choose a less expensive way to comply with the license renewal requirements, yet still provides the commissioner with adequate security on which to collect in the event that the third party administrator becomes insolvent. This new provision assists businesses by affording them more options to meet regulatory requirements. The department believes that there is no additional risk to Minnesota clients and consumers. Since this new provision applies only to third party administrators who have gross income from sources within Minnesota of less than \$100,000, it assists small businesses by establishing less restrictive standards.

III. SMALL BUSINESS CONSIDERATIONS

Minnesota Statute section 14.115, subdivision 2. (1992) requires the department, when proposing rules which may affect small businesses, to consider the following methods for reducing the impact on small businesses:

- a. the establishment of less stringent compliance or reporting requirements for small business;
- b. the establishment of less stringent schedules or deadlines for compliance of reporting requirements for small businesses;
- c. the consolidation or simplification of compliance or reporting requirements for small businesses;
- d. the establishment of performance standards for small businesses to replace design or operational standards required in the rule; and
- e. the exemption of small businesses from any or all requirements of the rule.

The proposed rules are specifically intended to establish less stringent compliance and reporting requirements for small businesses conducting third party administrator activities in Minnesota. The rule amendments will have a positive effect on small businesses in that they will allow a greater number of small businesses to obtain a waiver of filing certified financial statements every two years. This will benefit small businesses by reducing the costs to obtain a renewal license.

In proposing the rules, the department considered each of the above-listed methods for reducing the impact of the rules on small business.

- a. The department believes that the proposed rules do establish less stringent compliance and reporting requirements for small businesses desiring to renew their licenses to do business in Minnesota. As discussed earlier in this statement of need and reasonableness the department believes that the \$100,000 gross income threshold (as a basis for requesting a waiver of certified financial statements) is necessary and prudent to protect clients and consumers in Minnesota.
- b. The department believes that the proposed rules establish less stringent schedules or deadlines for compliance of reporting requirements for small businesses by eliminating the costly and detailed tasks of working with a CPA to have its financial statements certified.
- c. The department believes that the proposed rules will simplify the compliance and reporting requirements for small businesses by eliminating the need to have certified financial statements filed for license renewal.
- d. The establishment of performance standards for small businesses to replace design or operational standards are not applicable to the proposed rules.
- e. The department believes that small businesses should not be exempt from the proposed rules, since the rules are designed specifically to ease the reporting requirements on smaller companies doing business in Minnesota.

IV. EXPENDITURE OF PUBLIC MONEY BY LOCAL PUBLIC BODIES

Minnesota Statutes, section 14.11 subdivision 1, does not apply because adoption of these rules will not result in additional spending by local public bodies in excess of \$100,000 per year for the first two years following adoption of the rules.

V. IMPACT ON AGRICULTURE LANDS

Minnesota Statutes, section 14.11 subdivision 2, does not apply because adoption of these rules will not have an impact on agricultural land.


VI. DEPARTMENTAL CHARGES

Minnesota Statutes, section 16A.1285, subdivisions 4 and 5 do not apply because the rules do not establish or adjust departmental charges.

VIII. CONCLUSION

Based on the foregoing, the department's proposed rules are both necessary and reasonable.

11-4-94
Date



James E. Ulland
Commissioner of Commerce