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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 Relating to Commercial Insurance Filing Exemptions

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 Relating to Commercial
Insurance Filing Exemptions**

**STATEMENT OF NEED
AND REASONABLENESS**

I. INTRODUCTION AND STATEMENT OF AUTHORITY.

Chapter 70A of the Minnesota Statutes provides statutory authority for regulatory requirements concerning filing of policy forms and rate schedules for most lines of property and casualty insurance. Minnesota Statutes § 70A.02, subdivision 3 permits the Commissioner of Commerce to:

exempt from any or all of the provisions of this chapter, if and to the extent that the Commissioner finds their application unnecessary to achieve the purposes of this chapter;

- (1) Any specified person, by order, or class of persons by rule;
and
- (2) any specified risk by order, or any line or kind of insurance or subdivision thereof or class of risks or combination of classes by rule.

These rules are promulgated to exempt policy forms and schedules of rates used solely for business insureds from the filing and approval requirements of chapter 70A.

Minnesota Statutes § 70A.06, subdivision 2 requires insurers to file policy forms with the Commissioner for approval. Subdivision 1 of that section requires rates to be filed, although the Commissioner's approval is not required. These requirements carry out the purposes of Minnesota Statutes Chapter 70A as described in § 70A.01, subdivision 2:

- (a) To protect policyholders and the public against adverse effects of excessive, inadequate or unfairly discriminatory rates;
- (b) To encourage, as the most effective way to produce rates that conform to the standards of paragraph (a), independent action by and reasonable price competition among insurers;

- (c) To provide formal regulatory controls for use if independent action and price competition fail;
- (d) To authorize cooperative action among insurers in the rate-making process, and to regulate such cooperation in order to prevent practices that tend to bring about monopoly or to lessen or destroy competition;
- (e) To encourage efficient and economic practices.

In addition, policy form filing and approval is necessary in order to be certain that policy forms comply with the requirements of other Minnesota Statutes.

The limited insurance knowledge of consumers demands a formal review and approval process for non-commercial insurance policies. On the other hand, problems arising from misleading commercial policy provisions are unlikely due to the sophistication of business insureds. There are, moreover, comparatively few statutory requirements which relate to provisions of commercial line policy forms. For these reasons, there is little need for formal review of commercial line policies.

Formal review of rates is necessary for personal lines of insurance because of a potential for excessive or unfairly discriminatory rates. Greater competition for commercial lines business precludes the need for this review for commercial lines insurance rates. This competition is evidenced by flexibility built into many commercial rate schedules to allow subjective variation of rates by means of various credits or, in some cases, rates which are individually set for each risk. As shown above the filing and approval requirements of Minnesota Statutes § 70A.06, subdivisions 1 and 2 are not necessary to assure that commercial lines customers do buy policies which are not misleading or do not comply with statutory provisions. These requirements are also not necessary to prevent excessive or discriminatory rates. Thus, it can be seen that the statute requires adherence to requirements which result in unnecessary effort and expense for insurers and the Department of Commerce. The proposed rules remove as much of that burden as possible while maintaining the regulatory surveillance and controls which the Legislature intended and is required by Minnesota Statutes § 70A.01, subdivision 2.

Historical Background

In February 1982, Commissioner of Insurance Michael D. Markman had adopted rules that are essentially identical to the rules being proposed today. From February 1982 until January 1986, insurance companies were exempt from the requirements of Minnesota Statutes § 70A.06 of filing policy forms and schedules of rates used solely for commercial insureds.

The basis of the exemption essentially was that there was little need for the procedural burden of reviewing commercial insurance policy forms and rates, since such

filings were not necessary to prevent excessive or discriminatory rates. In addition, it was determined that problems arising from misleading commercial policy provisions were unlikely due to the sophistication of the business insureds.

In the spring of 1985, Commissioner of Commerce Michael Hatch became alarmed that policy forms and rates for commercial lines of insurance were not being filed. Commissioner Hatch became concerned about this exemption when he received an inquiry regarding a pollution exclusion on a commercial policy. When he became aware that the commercial filings were not available at the department of commerce, and that the department needed to request a copy of the policy from the insurer, Commissioner Hatch decided that the 1982 rules needed to be repealed.

Another fact supporting Commissioner Hatch's decision to repeal the rules occurred in December 1984, when a major carrier of liquor liability insurance abruptly canceled a substantial number of policies in Minnesota due to insolvency problems in the state of New York. The commissioner determined that the fact that no filings had been made in regard to either the policies or rates since the adoption of the exemption hampered the department from anticipating that there were only a few carriers of liquor liability insurance in Minnesota at that time.

In response to the perceived crisis in availability of insurance coverage, Commissioner Hatch published a notice of intent to repeal rules without a public hearing in the State Register on May 27, 1985. A Notice of Hearing was signed by Commissioner Hatch on July 2, 1985, a copy of which appeared in the State Register on July 15, 1985. The hearing occurred on August 20, 1985 before Administrative Law Judge Peter Erickson. The repeal of the rules became effective as of January 1, 1986.

The Statement of Need and Reasonableness prepared in support of the repeal of the exemption rules ("1985 SONAR") emphasized that by requiring companies to file commercial lines forms and rates, the department would have available to it those policies and rates currently being used in the state. As a result, it was determined that the department would be able to develop a picture of the market based on those filings. The 1985 SONAR relied on problems in the liquor liability insurance area as a primary basis for the need to have accurate market data.

Unfortunately, the type of information required to be filed by commercial insurers over the past eight years has not provided the department with an accurate reflection of market price or availability of commercial lines insurance. Even though a company files its rates and forms, that act does not mean the company will write each type of risk or coverage filed. The statutes do not require that the commercial insurer write the coverage filed at the rate filed. In practice, the commercial lines company will frequently file all possible rates and forms, whether or not those rates or forms are currently being used. By making all such filings, the company can be assured that it has complied with state law, and can avoid the delays resulting from the approval process.

The department has no way to determine, from filings alone, whether the company has issued any policies in Minnesota. As to rate filings, commercial lines insurers file standard rates, which do not reflect basic underwriting factors such as rates charged to different classes of risks. There is no way to determine, based on rate filings alone, what actual cost is associated with the purchase of any commercial policy in Minnesota. The alleged problem that was intended to be addressed by the repeal of the exemption rules has not been remedied.

The reliance in the 1985 SONAR on the liquor liability insurance crisis appears to have been an overreaction. Even if the department had received form and rate filings from 1982 to 1986, the department would not have had an accurate picture of what market existed for this type of insurance. Since 1984, the department has not been aware of any other crisis in the availability of commercial lines insurance that is not handled by surplus line carriers (who are not required to file rates or forms with the department) or the assigned risk plans or the Joint Underwriting Association (JUA).

All of the predictions in the 1985 SONAR as to a capacity shortage in the insurance industry have never materialized with respect to commercial lines coverage, and are not expected to materialize in the future. It is important to note that even with the increased occurrence of hurricanes and natural disasters in various parts of the country over the past few years, companies continue to do business. The crisis to be averted with these insurers will be in the financial examination area, not with respect to the availability of coverage. Requiring companies to file standard forms and rates will not affect this situation.

The 1985 SONAR states that it is imperative that the department, which is charged with the regulation of insurance, in general should know as much as possible about what is happening in the market place in Minnesota. The department still holds this opinion, however, it has determined that receiving, reviewing and maintaining form and rate filings from commercial lines insurers serves no significant purpose in our day-to-day role as regulator. The department believes that a greater public good will be obtained by focusing available department resources on monitoring the forms and rates used for personal lines insurance. In support of this contention, information furnished by the enforcement division of the Department of Commerce indicates of the 18,911 insurance complaints and inquiries received by the department in 1992 and 1993, only 798 or 4.2% involved commercial filings. Having commercial filings on site would not facilitate efforts to resolve consumer complaints. To the extent necessary, the department believes it has sufficient access to data through annual financial filings made by all insurers, including general liability and commercial lines insurers, to monitor a company's solvency and market participation. In addition, the department believes it has adequate enforcement powers to obtain all data it deems relevant from licensed insurers pursuant to Minnesota Statutes §§ 45.027 and 70A.18 in the event that such information is necessary. Although the 1985 SONAR indicated that alternative methods to the general filing requirement are a less satisfactory method of obtaining information, the department now believes that the few instances when information obtained from the required filings may be helpful does not

outweigh the burden placed on the department (in reviewing the filings) and the commercial insurance industry in meeting the filing requirements.

The 1985 SONAR states that the expense of making filings was minimal even though the cost would be passed on the consumers. The filing fee at that time was \$10. In 1987 the fees were increased to \$50, which no longer can be considered minimal.

In reviewing the reasons set forth for repealing the exemption rules in the 1985 SONAR, the department carefully analyzed each assertion and conclusion contained therein. With eight years of form and rate filings experience, the department feels no more confident in making market availability predictions or rate predictions than it did prior to the repeal of the rules in 1985.

In response to a Notice of Solicitation of Outside Information and Opinion (published in the State Register on July 5, 1994), a number of insurance companies contacted the department in support of re-establishing a filing exemption for commercial lines insurers. These companies felt that the costs and efforts associated with these filing requirements were burdensome. It is interesting to note that not one person or entity submitted a comment in support of continued repeal of the exemption rules.

In 1993, pursuant to Executive Order 93-10, each state agency was asked to review the parts of the Minnesota rules and statutes that it enforces and determine which of the statutes and rules were outdated, unnecessary or unduly burdensome. In addition, each department was encouraged to amend statutes or rules in a manner that would reduce unnecessary regulatory burden on Minnesota businesses. The department believes that the commercial insurance filing requirements are unnecessary and unduly burdensome in comparison to the benefit the law provides to the department and to the public good. Since there are more reliable alternatives to addressing potential problems with the policies and rates of commercial lines insurers than by maintaining the current form and rate filing requirements, the department believes the promulgation of the proposed rules will carry out the directive of the governor as set forth in Executive Order 93-10.

For the reasons set forth in this statement of need and reasonableness, the department believes that the adoption of the proposed rules is in the best interests of all parties. The department believes that re-establishing the exemption rules is within the authority granted under Minnesota Statutes § 70A.02 subdivision 3 and that it will further the purposes described under Minnesota Statutes § 70A.01, subdivision 2.

II. FACTS ESTABLISHING NEED AND REASONABLENESS

The language proposed under the following sections is identical to the language of rules repealed in 1985. The only exception is the addition of subpart 4 under Part 2700.2470. This provision was added to specifically clarify that the exemption does not apply to rate service organizations.

Part 2700.2460 defines "commercial policies" of insurance. This term is used as a shorthand reference for the policy forms affected by these rules. This term does not include crop hail or medical malpractice insurance because these coverages, although used by businesses, are purchased in a manner similar to the purchase of homeowner's or individual liability insurance. Liability insurance for individual professionals is also excluded because individual professionals are not always as careful in business insurance purchases as are businesses which employ professionals. For example, a physician or accountant is likely to pay less attention to liability purchases than a clinic or accounting firm.

Part 2700.2470 exempts insurers from the filing and review requirements of Minnesota Statutes § 70A.06 for commercial lines of insurance. The exemptions are contingent upon the continued compliance of forms or rates within the provisions of the Minnesota Statutes. It is the intent of the Commissioner to presume that all exempt forms and rates comply with statutory requirements unless it is discovered via investigation of a consumer complaint or staff research that the presumption is not correct. When a form does not comply, the insurer will no longer be exempt from the filing and approval requirements. When the Commissioner finds that continued filing and approval is no longer necessary to assure continued compliance with the law, an order will be issued pursuant to Minnesota Statutes § 70A.02, subdivision 3, to provide an exemption for the insurer. The ability to remove the exemption in this manner will assure the successful operation of these rules and will fulfill the legislative intent expressed in Minnesota Statutes § 70A.01, subdivision 2, (c): To provide formal regulatory controls for use if independent action and price competition fail.

The exemption of insurers from filing and approval requirements for commercial lines of insurance is stated differently for policy forms, rate schedules, and for guide "a" and excess rates. This is necessary to reflect the differing exemptions and conditions for exemption for these three areas. Subpart 1 of Part 2700.2470 exempts insurers from filing and approval requirements for commercial policy forms.

Subpart 2 of Part 2700.2470 provides exemption from filing requirements for commercial rates. Rates for lines governed by Chapter 70A are not subject to approval. In other words, a commercial insurer is not required to receive approval before being able to use its determined rates in Minnesota. It is referred to as a "file and use" system. The fact that commercial lines insurers have been required to file rates over the past eight years (since the repeal of the exemption rules) has not resulted in any power of the department or commissioner to prohibit the insurer from using those rates. It is necessary to re-establish the exemption for rate filings for commercial lines insurers, since it eliminates a procedural requirement that serves no true purpose for the department in conducting its regulatory duties. To eliminate this filing requirement will reduce unnecessary regulatory burdens on companies doing business in Minnesota.

Subpart 3 of Part 2700.2470 exempts insurers from filing requirements for two specialized sets of rates - guide "a" and excess rates - which are set individually for individual insureds. This exemption is contingent upon the insurer's maintenance of a file containing the information normally required to be filed with the Commissioner. This exemption states the longstanding policy of the Department of Commerce.

Subpart 4 of Part 2700.2470 specifically states that the exemption from filing forms and rates does not apply to rate service organizations, which publish standard policy forms and rates for use by a number of insurance companies. The department will effectively carry out the surveillance function implied in Minnesota Statutes § 70A.01, subdivision 2 (c) by reviewing the comparatively few forms and rate schedules published by rate service organizations and used by insurers as the basis of the majority of forms and rate schedules issued by insurers. Furthermore, by maintaining the authority to approve these forms, the department will sustain leverage to enforce its legal interpretation of general statutory provisions for most policies issued in Minnesota.

Part 2700.2480 requires an insurer to provide the Commissioner with any of the information which the previous rule exempts the insurer from filing. This requirement allows the department to investigate consumer complaints or to examine policies and rates when there is reason to question compliance with the requirements of the statutes. While the Commissioner can certainly require such information under the provisions of Minnesota Statutes §§ 70A.18 and 45.027, this rule is proposed to make the possibility of this request and the expected time period for response clear to those insurers who will be affected.

III. SMALL BUSINESS CONSIDERATIONS

Minnesota Statute § 14.115, subdivision 2. (1992) requires the commissioner, 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 businesses;
- 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.

In the process of considering the proposed rules, it was determined that the impact of rules falls exclusively upon insurance companies, and that few, if any, insurance companies qualify as small businesses. To the extent that a small business might be

affected by the rule, the various methods for reducing the impact of the rule on small business were considered.

- (a) The establishment of less stringent reporting requirements for small businesses were considered. Since the proposed rules will eliminate form and rate filing requirements for any commercial lines insurer, regardless of its size, it is not possible to further reduce reporting requirements for small businesses that might be affected by this rule.
- (b) The establishment of less stringent schedules or deadlines for compliance or reporting requirements was considered. To the extent that there are any small businesses affected, no less stringent schedules or deadlines are needed for the exemption.
- (c) Item c of subdivision 2 pertains to the consolidation or simplification of compliance or reporting requirements for small businesses. Since the small business would be exempt from filing, it is not possible to further simplify or consolidate the reporting requirements.
- (d) Since there are no design or operational standards required under the proposed rules, there is not need to establish performance standards for small businesses.
- (e) The exemption of small businesses from many or all requirements of this rule would increase the burden on small businesses. The rules should apply equally to affected small businesses to exempt them from filing requirements.

The Notice of Solicitation of Outside Opinion and Information published in the State Register on July 5, 1994, contained a notice to all small businesses to submit relevant comment or opinion. This notice was sent in advance of proposed rulemaking and was mailed to all person and entities on the department's mailing list for purposes of rulemaking notification. Any interested small business shall be given the opportunity to participate in the rulemaking process. (No comments were received on this issue pursuant to the Notice of Solicitation referred to above).

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.

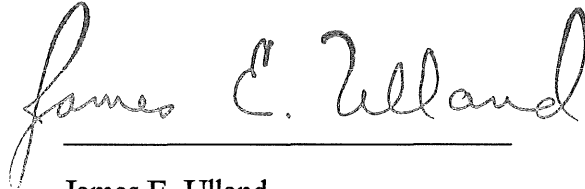
Minnesota Statutes, section 16A.1285, subdivisions 4 and 5, do not apply because the rules do not establish or adjust departmental charges.

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