

STATE OF WASHINGTON
OFFICE OF INSURANCE COMMISSIONER

FILED

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3 *In the Matter of*)
4)
5 YOURPEOPLE, INC. DBA ZENEFITS)
6 FTW INSURANCE SERVICES, ORDER)
7 NO. 16-0219 REVIEW OF INITIAL)
8 ORDER)
9)

OIC Agency No. 16-0129

OAH Docket No. 02-2017-INS-000009

2017 NOV 15 A 8:00

YOURPEOPLE, INC. DBA ZENEFITS HEARINGS UNIT
FTW INSURANCE SERVICES BRIEF OFFICE OF
RE: REVIEW OF INITIAL ORDER INSURANCE COMMISSIONER

10 INTRODUCTION

11 The Office of Administrative Hearings (“OAH”) correctly held that Zenefits may
12 lawfully offer access to its integrated online human resources, payroll, and employee benefits
13 platform (“HR platform”) to the general public for free. See Initial Order at ¶ 6.2. OAH also got
14 it right by acknowledging that all brokers can and do provide insureds with free benefit
15 administration services, including on-line tools that automate traditional paper processes such as
16 Zenefits’ benefit administration apps. See Initial Order at ¶ 5.9.

18 OAH missed the mark, however, in concluding that Zenefits’ benefit administration apps
19 and its HR platform are prohibited from communicating with each other unless Zenefits charges
20 a fee to its customers. The *integration* of Zenefits’ benefit administration apps with its HR
21 platform that the Initial Order takes issue with simply facilitates the exchange of information
22 between insured, broker, and insurer. It allows Zenefits to perform, digitally, core brokerage
23 functions such as eligibility determinations and enrollment that typically are accomplished by
24 fax, phone and mail. The practical effect of allowing benefits and human resources systems but
25 prohibiting them from speaking to each other is to outlaw convenience and require customers to
26 manually input the same data into separate systems to achieve the same result. This holding will
27 impose significant burden and expense on Washington businesses and consumers and will stifle
28

1 innovation without promoting any legitimate public policy goals. As such, this portion of the
2 Initial Order must be overturned.¹

3 **ARGUMENT**

4 **I. OAH Correctly Held That Licensees May Offer Free Or Discounted Services**
5 **On Equal Terms To All**

6 The Hearings Unit should affirm OAH's holding that Zenefits may offer free or
7 discounted services where they are "available to all, regardless of whether insurance is
8 purchased." Initial Order at ¶ 5.6. OAH appropriately rejected OIC's over-broad and
9 unprecedented interpretation of the anti-rebating statutes that would prohibit, without
10 qualification, "the giving or promising of anything of value to a prospective insured regardless of
11 ... any connection to an insurance transaction." OIC Post-Hr'g Br. at 4.

13 OAH's conclusion is consistent with the statutory language, the purpose of the anti-
14 rebating statutes, OIC precedent, the analysis of every other state to consider the issue, and
15 common sense:

- 16
- 17 • Washington's anti-rebating statutes require a connection between a benefit conferred and
18 an insurance transaction for a violation to occur. Non-insurance services that are
19 provided for free to the general public without any obligation to purchase, or even
20 consider purchasing, insurance cannot operate as an illegal rebate or inducement as a
21 matter of law. *See* Zenefits' Hearing Brief ("Zen. Hr'g Br.") at 13-16; Zenefits' Post-
22 Hearing Brief ("Zen. Post-Hr'g Br.") at 5-10.
 - 23 • Legislative history confirms that anti-rebating statutes exist to prevent discriminatory
24 treatment among insureds and to preserve insurer insolvency, not to stifle competition
25 and innovation at the expense of consumers. *See* Zen. Hr'g Br. at 16-19; Zen. Post-Hr'g
26 Br. at 10-11.
 - 27 • Every state besides Washington to interpret virtually identical statutory language has
28 concluded that benefits offered on equal terms to the general public do not constitute
illegal inducements or rebates. *See* Zen. Hr'g Br. at 19-21; Zen. Post-Hr'g Br. at 12-14.

26 ¹ In support of its position, Zenefits incorporates herein as if set forth in full all of the
27 briefs, exhibits, testimony, and argument submitted in the proceeding before the OAH, including
28 but not limited to Zenefits' June 30, 2017 Hearing Brief and attachments (attached hereto as Exhibit A) and its July 27, 2017 Post-Hearing Brief and attachments (attached hereto as Exhibit B).

- 1 • The interpretation of the anti-rebating statutes advanced by OIC in this proceeding is
2 inconsistent with agency enforcement precedent and the views of its own legal
3 department. *See* Zen. Hr’g Br. at 6-8, 21-22; Zen. Post-Hr’g Br. at 11-12, 14-16.
4 • Any other result would have broad-reaching, unintended consequences for Washington
5 consumers and other innovative Washington licensees. *See* Zen. Hr’g Br. at 22-23; Zen.
6 Post-Hr’g Br. at 25-27.
7 • None of Deputy Commissioner John Hamje’s post-hoc “public policy” rationales for
8 prohibiting licensees from offering free or discounted non-insurance services to the
9 general public hold water. *See* Zen. Hr’g Br. at 22-23; Zen. Post-Hr’g Br. at 16-19, 27-
10 32.

11 Allowing brokers to offer free or discounted services on equal terms to the general public
12 is also good public policy. As OAH observed, “Zenefits’ free core HR services promote
13 innovation and help small businesses grow, which is good for Washington.” Initial Order at
14 ¶ 5.7. Insurance regulators, within OIC and elsewhere, agree. *See, e.g.,* Ex. T (OIC Staff
15 Attorney M. Stickler: “Public policy considerations should permit this activity as consumers are
16 benefitted by convenience and ease of use for employee benefit management”); Ex. AG (in
17 concluding Zenefits’ platform is not an inducement, the Office of Montana’s State Auditor
18 observed: “This interpretation is also good public policy, as Zenefits may potentially provide
19 Montana small businesses with services they would otherwise not be able to afford”).

20 To adopt the sweeping prohibition endorsed by OIC in this proceeding would be
21 fundamentally anti-consumer and detrimental to the Washington business community, without
22 advancing any legitimate public policy. As such, the Hearings Unit should affirm OAH’s
23 finding that a licensee’s provision of free services on equal terms to all complies with
24 Washington law.

25 **II. The Hearings Unit Should Vacate OAH’s Finding That Integration Of**
26 **Zenefits’ Benefits Administration Services Constitutes A Rebate Or**
27 **Inducement**

28 While OAH correctly determined that brokers may offer free or discounted services to
the general public, the Hearings Unit should vacate OAH’s finding that Washington law

1 prohibits the offering of benefit administration apps that communicate with HR and payroll
2 systems to facilitate the efficient management and administration of insurance policies.

3 There is no dispute that brokers may without separate charge provide benefit
4 administration services to insureds. *See* Zen. Post-Hr'g Br. at 20-23.² Indeed, OAH
5 acknowledges that free incidental benefits administration services, including Zenefits' benefit
6 administration apps, are permissible. Initial Order at ¶ 5.9. It found, however, that Zenefits'
7 "integration" of "insurance information with payroll and other HR services" was an illegal rebate
8 because it is a "significant, heavily-promoted, special benefit" not made available to non-
9 insurance customers. Initial Order at ¶ 5.11. This does not justify OAH's ruling. The fact that
10 Zenefits' fully integrated platform is unique and provides value is irrelevant so long as the
11 platform and its interconnectedness provide the kind of incidental benefit administration services
12 that all brokers provide in one form or another, which is precisely the case here.

13
14
15 The integration of Zenefits' benefit administration apps with its HR platform facilitates
16 the core communication functions provided by traditional brokers every day. It is also precisely
17 the kind of "enhancement" designed to make operations "more efficient and convenient for the
18 insured" that the Maine Bureau of Insurance³ and other state insurance departments explicitly
19

20 ² As the Louisiana Department of Insurance recently advised, "[a]ny person engaging in
21 the business of insurance may offer certain services to insureds without charge and that do not
22 constitute rebating . . . when the services are *incidental to the policy of insurance and are offered*
23 *to all insureds.*" Louisiana Dep't of Ins. Advisory Letter 2015-01 (Revised March 14, 2017)
24 (emphasis added). Likewise, Maine observed that "[e]nhancements that operate to make the
25 producer's own services and operations more efficient and convenient for the insured" and
26 "system improvements, which could include software provided to employers, which make
27 information about group benefits provided through the producer more accessible to employers
28 and employees" are not considered prohibited rebates. Maine Dep't of Prof'l & Fin. Reg.,
Bureau of Ins., Bulletin No. 426 (2017). Iowa similarly has explained that "value-added
services" do not constitute rebates if they "are related to the type of insurance purchase." Iowa
Comm'r of Ins., Bulletin No. 08-15 (2008), *as amended by* Bulletin No. 08-16 (2008). OIC did
not address any of these authorities at any point in the proceedings.

³ Maine replaced its Bulletin 384, cited in Zenefits' Post-Hearing Brief, with Bulletin 426
on October 25, 2017 (attached hereto as Exhibit C), but the guidance did not change in any

1 permit and, in fact, seek to encourage.⁴

2 For example, to update dependent information an insured calls his or her broker who, in
3 turn, submits a form to the insurance carrier by fax or email. Zenefits' integrated offering
4 provides exactly the same communication function digitally – it facilitates the exchange of
5 information between the insured, broker, and insurer to streamline the administration of the
6 policy. Likewise, while a traditional broker would gather biographical details about prospective
7 insureds, prepare and submit various forms to the carrier to obtain a price quote, communicate
8 that quote to the customer, and then process the customer's request to purchase a policy, the
9 integration of insurance and HR databases allows Zenefits to perform most of the same functions
10 electronically, without the risk of material errors.

11
12 The Initial Order acknowledges that the integration offered by Zenefits enhances its
13 ability to perform what are undoubtedly core brokerage functions. In describing Zenefits'
14 platform, OAH observed that connecting an employer's insurance enrollment data with its
15 human resources databases allows for "information [to] be updated throughout the payroll and
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18 material respect as it relates to this matter. Although Bulletin 426 observes that the provision of
19 free payroll or human resource management may fall outside the scope of Maine's "value added"
exemption, it does not prohibit the *integration* of, that is, communication between, insurance
systems and human resources and payroll systems that is at issue here.

20 ⁴ See also New York Circular Letter No. 9 (2009) ("[I]nsurance producer[s] may provide a
21 service not specified in the insurance policy or contract to an insured or potential insured without
22 violating the anti-rebating and inducement [laws] if: (1) the service directly relates to the sale or
23 servicing of the policy . . . and (2) the insurer or insurance producer provides the service in a fair
24 and nondiscriminatory manner to like insureds."); New Jersey Dep't of Banking & Ins., Bulletin
25 No. 11-22 (2011) (the Department "does not construe the intent of these statutes and rules as
26 prohibiting the delivery by producers or insurers of services or other offerings for free or at a
27 discounted price in a fair and non-discriminatory way, so long as the services or other offerings
28 relate to or enhance the value of the insurance product being purchased"); Idaho Dep't of Ins.,
Bulletin No. 11-03 (2011) ("[s]ervices that fall within the traditional notion of 'customer service'
for which one would not normally expect an additional charge are not considered" illegal
inducements); N.H. Rev. Stat. 402:41(I)(d) (permitting provision of "value added service,
activity or product offered or provided without a fee, or at a reduced fee, that is related to the
coverage provided by the insurance contract . . . and is . . . [d]irectly related to the firm's
servicing of the insurance policy"); KY. Rev. Stat. 304.12-100(3) ("providing software to
administer an insured's employee benefit or risk management programs . . . or any other service
designed to assist in the efficient administration of a policyholder's insurance program" does not
constitute an illegal inducement or rebate).

1 insurance benefit sites without the need to fill out paperwork for each area” and “changes [made]
2 in one system will be automatically pushed to the others.” Initial Order at ¶¶ 4.23, 4.13. OAH
3 further acknowledged:

4 So after the employee is completed [sic] onboarding, Zenefits is: (1) Pushing the
5 employee information into Payroll . . . (2) Prompting the employee to enroll in
6 their benefit plans . . . (3) Calculating the deductions from their plans . . . (4)
7 Push[ing] their deductions back to payroll . . . (5) Stor[ing] everything in 1 happy,
8 central place so you have full and detailed records on every employee.

8 Initial Order at ¶ 4.12.

9 Prohibiting a licensee from offering an insurance platform that can communicate with
10 and import data from other human resources systems on the basis that such an offering is,
11 essentially, “too convenient” is an absurd result, clearly not contemplated by the anti-rebating
12 statutes. This ruling would have the perverse effect of outlawing efficient, modern, on-line
13 administration of insurance benefits and would force insureds to depend once again on
14 cumbersome and time-consuming paperwork, fax machines, and mail to manage their benefit
15 plans.
16

17 OAH’s conclusion that Zenefits’ integrated benefit administration apps constitute an
18 inducement because they are not offered to non-insurance customers also makes no sense from a
19 practical perspective. It is undisputed that: (1) Zenefits’ insurance benefits apps, and their
20 connectivity to other HR systems, have no practical use or value unless Zenefits has access to
21 policy and coverage data from insurance carriers; and (2) Zenefits’ benefits apps cannot access
22 policy and coverage data unless Zenefits is designated as broker of record. Hr’g Tr., Hazard
23 Testimony, July 11, 2017 at 41: 16-25; 42: 1-14; 45:4-25; 46: 1-20; 50: 9-25; 51: 1-10; 59: 14-25
24 (attached hereto as Exhibit D); 60: 1-7; Zen. Post-Hr’g Br. at 21-22. Thus, the practical, and
25 irrational, result of OAH’s order is that compliance with the anti-rebating statutes requires
26 Zenefits to offer non-insureds a service that is entirely useless to them.
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1 **III. Paragraph 6.3 Is Overbroad And Not Supported By The Initial Order**
2 **Findings Of Fact And Conclusions Of Law**

3 The holding at paragraph 6.3 of the Initial Order must also be rejected because it is
4 overbroad and inconsistent with the preceding findings of fact and conclusions of law.
5 Paragraph 6.3 purports to prohibit “offering valuable software functions or other valuable
6 benefits free . . . to those who purchase insurance through Zenefits or otherwise designate
7 Zenefits as broker as record.” Nothing in the Initial Order, however, supports such a sweeping
8 conclusion. OAH takes issue with free system integration offered only to insureds. Initial Order
9 ¶¶ 5.8 – 5.11. Paragraph 6.2, however, is not limited to Zenefits’ offer of “full HR integration.”
10 In fact, it appears to prohibit the provision of free software to insureds without qualification or
11 limitation – conflicting with the holding in paragraph 6.2 that HR integration *can* be offered to
12 “those who purchase insurance” as long as it is offered on equal terms to the general public.
13 This clearly was not the intent of OAH. In the event the Hearings Unit does not reject OAH’s
14 determination that Zenefits may not integrate its benefit administration apps with its HR
15 platform, the Hearings Unit should amend the associated holding to conform to the more limited
16 findings and conclusions set forth at paragraphs 5.8 through 5.11 of the Initial Order.
17

18 **IV. OAH Improperly Modified The Consent Order And Issue To Be Decided**

19 Finally, without authority or explanation OAH improperly modified the Consent Order
20 and the issue presented by the parties for decision in an attempt to limit the application of the
21 Initial Order to Zenefits. The Consent Order executed by Commissioner Kreidler and the
22 parties’ joint statement of the issue to be decided in this case address whether “RCW 48.30.140
23 and RCW 48.30.150 *prohibit a licensee like Zenefits*, acting directly or through affiliates, from
24 offering valuable software functions or other valuable benefits for free or at less than fair market
25 value to the public.” Ex. CR at ¶ 6 (emphasis added); Joint Stipulated Motion to Amend
26 Prehearing Order and Notice of Hearing (Apr. 27, 2017); OAH letter amending Prehearing Order
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1 and Notice of Hearing (May 23, 2017). Yet, OAH unilaterally revised the issue to be decided,
2 replacing the “licensee like Zenefits” language with just “Zenefits.” *See, e.g.*, Initial Order
3 ¶¶ 2.1, 2.2, 6.2, 6.3. Neither party requested in their briefs or at the hearing that the issue be
4 modified, and OAH offers no authority or reasoning for rejecting the language adopted by the
5 Commissioner in his Consent Order or for limiting the scope of the Initial Order. To be clear,
6 the order, if adopted, will still prohibit other Washington businesses that offer insurance and non-
7 insurance services from integrating their systems (for example, banks cannot integrate insurance
8 management databases with free checking accounts) regardless of whether this language is
9 reinserted. Nevertheless, the Initial Order must be amended to conform to the Commissioner’s
10 Consent Order and to the issue presented for consideration by both parties.
11

12 **V. Conclusion**

13
14 In concluding that offering free software functions to the general public does not
15 constitute a violation of the anti-rebating statutes, OAH appropriately recognized that Zenefits’
16 HR platform “promotes innovation and helps small businesses grow, which is good for
17 Washington.” Prohibiting Zenefits’ benefit administration apps from communicating with its
18 customers’ HR and payroll systems, however, does exactly the opposite, forcing Washington
19 small businesses to once again rely on cumbersome, inefficient, and costly manual processes and
20 paperwork in administrating their benefit plans.
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22 Zenefits respectfully requests that the Hearings Unit: (1) affirm OAH’s holding that the
23 anti-rebating statutes do not prohibit Zenefits, acting directly or through affiliates, from offering
24 valuable software functions or other valuable benefits free or at less than fair market value to the
25 general public, regardless of whether insurance is purchased; and (2) reject OAH’s conclusion,
26 set forth at paragraphs 5.8, 5.9, 5.10, 5.11 and 6.3, that the anti-rebating statutes prohibit Zenefits
27 from offering tools to insurance customers designed to facilitate and simplify the administration
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1 of insurance benefits.

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3 Dated this 15th day of November, 2017.

Respectfully submitted,

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Exhibit A

STATE OF WASHINGTON
OFFICE OF ADMINISTRATIVE HEARINGS

In the Matter of

YOURPEOPLE, INC. DBA
ZENEFTS FTW INSURANCE SERVICES,

Appellant.

Docket No. 02-2017-INS-00009

YOURPEOPLE, INC. DBA
ZENEFTS FTW INSURANCE SERVICES
HEARING BRIEF

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III. OIC’s interpretation of RCW 48.30.140 and RCW 48.30.150 is directly at odds with the conclusions of other states, which have interpreted identical or nearly-identical anti-rebating and anti-inducement statutes.	19
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INTRODUCTION

Washington's insurance regulator has improperly interpreted and applied two consumer protection statutes in a manner that raises prices for consumers while protecting politically connected insurance brokers from competition and innovation in the marketplace. The Insurance Commissioner's flawed interpretation of these statutes, if allowed to stand, harms not only Zenefits, but the very consumers these statutes were designed to protect. In sum, the Insurance Commissioner's conclusion that Zenefits violated Washington's anti-rebating and anti-inducement statutes, RCW 48.30.140 and RCW 48.30.150 (collectively "anti-rebating statutes"), by offering certain services free of charge to everyone on its online human resources platform has no basis in statutory language, legislative history, or agency precedent.

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The State of Washington stands alone in its interpretation of these statutes. Every other state to consider whether Zenefits' offering of certain free services violates substantially identical anti-rebating statutes has concluded unequivocally that it does not. In fact, the Office of the Insurance Commissioner ("OIC") itself concluded—not once, not twice, but *three* times—that Zenefits was not in violation of these statutes. Then, succumbing to political pressure from the traditional insurance producer¹ lobby, OIC reversed course and, without offering any legal or factual basis for doing so, threatened Zenefits with a cease and desist order if it did not start charging Washington customers for services previously offered for free.

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As discussed in more detail below, and as Zenefits will demonstrate at the hearing, Washington's anti-rebating statutes require there to be a connection between a benefit conferred and an insurance transaction for a violation to occur. Non-insurance services that are provided

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¹ Insurance agents and brokers are referred to collectively as insurance "producers."

1 for free to the general public without any obligation to purchase, or even to consider purchasing,
2 insurance cannot operate as an illegal rebate or inducement under RCW 48.30.140 and RCW
3 48.30.150 as a matter of law or sound public policy.
4

5 STANDARD OF REVIEW

6 In an appeal of an agency order, an Administrative Law Judge reviews the agency's
7 conclusions of law *de novo*. See *Len v. Office of the Superintendent of Pub. Instruction*, 188
8 Wash. App 1040, *10 & n.14 (July 2015) (holding Administrative Law Judge properly applied
9 *de novo* standard of review). Agency orders must be supported by clear and convincing
10 evidence. *Id.* at *4. In formal adjudicative proceedings under the Washington Administrative
11 Procedure Act, the agency has the burden of proof. *Id.* at *10; see also RCW 34.05.449(2);
12 WAC 181-86-170(2). The broad introduction of additional evidence is permissible pursuant to
13 RCW 34.05.449(2), and “[h]earings shall be conducted with the greatest degree of informality
14 consistent with fairness and the nature of the proceeding.” RCW 34.12.010.
15

16 STATEMENT OF FACTS

17 **I. Zenefits offers an integrated human resources, payroll, and employee benefits** 18 **software solution for small businesses in Washington.**

19 Zenefits is a software-as-a-service (“SaaS”) company founded in 2013 that operates an
20 integrated online platform that simplifies the administration of human resources (“HR”), payroll,
21 and employee benefits (insurance and non-insurance) for small businesses and non-profits.
22 Among other advances, Zenefits streamlines HR administration by automatically updating
23 information across multiple, previously disconnected HR, payroll, and benefit systems,
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1 eliminating the needless duplication of paperwork that plagues many small companies.²

2 Anyone may register an account by entering basic information at Zenefits.com.
3 Establishing a Zenefits account is free to everyone and gives customers immediate access to the
4 Zenefits dashboard, which provides a variety of HR management solutions for tasks such as
5 hiring and onboarding, managing payroll, generating reports, and administering insurance and
6 non-insurance benefits. Once a customer sets up an account, the next step is to import employee
7 data, which can be done manually or by linking the data to existing payroll systems. When
8 changes are made to employee data, the platform automatically updates that information across
9 applications, which simplifies on-boarding, off-boarding, benefits, and everything else along the
10 way.
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12
13 Customers may select services that best suit their needs by subscribing to one of Zenefits'
14 service "tiers" and selecting from a number of add-on applications ("apps"). Zenefits presently
15 offers four tiers of service: Bronze, Silver, Gold, and Platinum. Zen. Ex. BP. The Bronze tier
16 contains Zenefits' core apps: tools to manage hiring, onboarding and terminating employees, and
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19 ² In 2001, the U.S. Small Business Administration estimated that the average small
20 business owner spent as much as 25% of his or her time handling employee-related
21 paperwork. *SBA Report Finds Blizzard of Employee-Related Paperwork*, CHICAGO TRIBUNE
22 (Dec. 27, 2001), available at http://articles.chicagotribune.com/2001-12-27/business/0112270070_1_peos-professional-employer-organizations-small-firms. The time,
23 energy, and money that small businesses spend on paperwork have continued to increase ever
24 since. *Small Business Democrats Seek to Reduce Red Tape for Entrepreneurs*, TARGETED NEWS
25 SERV. (U.S.) (Mar. 29, 2017) ("For small firms, paperwork requirements are particularly
26 burdensome. . . . [P]aperwork compliance is especially costly for small firms."). Minimizing
27 paperwork for small businesses is particularly important because the cost of errors—on an I-9
28 form, for example—add up quickly. Frank A. Cania, *HR Connection: Reducing the Paperwork
Burden on Small Business*, DAILY REC. OF ROCHESTER, N.Y. (Apr. 3, 2017), available at 2017
WLNR 10742679 (explaining how small businesses face fines that can be "financially
devastating" when completing paperwork by hand).

1 employee information; and to generate, among other things, employee directories, organizational
2 charts, and payroll reports. *Id.* The Bronze tier is free and available in all states except
3 Washington.³
4

5 Customers interested in increasing their service level may select the Silver tier, which
6 costs \$5 per employee per month and includes, in addition to the Bronze offerings, access to paid
7 time off, advanced onboarding, Affordable Care Act compliance, and advanced reporting
8 services. *Id.* The Gold tier costs \$8 per employee per month and adds payroll management to
9 the suite of offerings. *Id.* Finally, the Platinum tier adds access to a Certified Human Resources
10 Specialist and costs \$12 per employee per month. *Id.*
11

12 In addition to the services included in subscription tiers, Zenefits also offers certain
13 services for a fee on an à la carte basis. Zen. Ex. AR. Customers can choose to add services that
14 manage commuter benefits, time and attendance for hourly employees, background checks,
15 flexible spending accounts, health savings accounts, and contractor payments. *Id.* Zenefits also
16 gives its customers access to a rapidly expanding roster of third party applications offered by
17

18 ³ The offering of certain basic services for free while charging for more advanced
19 proprietary features—frequently referred to as a “freemium” pricing strategy—is a common
20 practice, particularly in the SaaS industry. Vineet Kumar, *Making “Freemium” Work*, HARV.
21 BUS. REV. 701, 701 (May 2014) (Attachment 1) (“Over the past decade ‘freemium’—a
22 combination of ‘free’ and ‘premium’—has become the dominant business model among internet
23 start-ups and smartphone app developers. Users get basic features at no cost and can access
24 richer functionality for a subscription fee.”); *see also, e.g., Freemium*, WIKIPEDIA, *available at*
25 <https://en.wikipedia.org/wiki/Freemium> (last visited June 30, 2017) (“Cloud service providers—
26 ranging from infrastructure providers (‘IaaS’) [and] platform providers (‘PaaS’) to software
27 services providers (‘SaaS’)—use freemium pattern in their business models.”). Freemium
28 pricing is neither unique nor offered to induce consumers to purchase insurance; rather, it is a
well-established practice that, among other things, allows consumers to effectively evaluate and
test the functionality of cloud-based services that cannot be replicated in a static environment. A
wide variety of internet-based businesses, from Amazon, to LinkedIn, to Badoo, to The New
York Times on-line edition, employ this model. *Id.*

1 companies such as Uber for company transportation services, eShares for stock option
2 management, and Ubiquity for 401(k) plan management.⁴ *Id.*; *see also* Zen. Ex. BO. Zenefits is
3 a licensed insurance producer and customers can elect to use Zenefits for insurance services,
4 including management of their medical, dental, vision, and life and disability policies, if they
5 designate Zenefits as their “broker of record.” Zen. Ex. BP. Insurance premium rates are set by
6 the carriers whose products the employer selects, and as broker of record Zenefits earns
7 commissions from those carriers. *Id.*

9 The Bronze, or free, tier of services is available to everyone and anyone, with absolutely
10 no obligation to purchase insurance from Zenefits. *See* Zen. Ex. AR; Zen. Ex. BP.⁵ All users
11 have access to the same products and services, on the same terms, regardless of whether they buy
12 insurance through Zenefits. Similarly, the company offers no discounts on fee-based services or
13 special benefits if an employer does elect to designate Zenefits as its broker of record. *See* Zen.
14 Ex. BP. In short, customers receive no special favor or advantage by purchasing insurance
15 through Zenefits, illustrated by the fact that, both historically and today, the majority of Zenefits
16 accounts in Washington do not use Zenefits for any insurance business.

18 **II. OIC concluded three times that Zenefits’ business model does not violate**
19 **Washington’s anti-rebating statutes.**

20 As Zenefits’ unique suite of offerings gained traction in the marketplace, they also drew
21

22 ⁴ Customers using these apps typically pay third party vendors directly and Zenefits may
23 receive an integration fee or reseller’s commission from the vendors.

24 ⁵ Zenefits introduced its tiered pricing model in late 2016. Previous pricing models
25 operated in a similar fashion in that some services were free to everyone, other services involved
26 a charge from a third party vendor of that service, and other services were available for a fee that
27 Zenefits charged to users directly. At no point in time, under any pricing model, have free
28 services been contingent on purchasing insurance.

1 the attention of traditional producers and their trade associations who felt threatened by this new
2 and innovative business model, including the Independent Insurance Agents & Brokers
3 Association of Washington (“IIABW”) and its national lobbying arm, the Independent Insurance
4 Agents & Brokers Association of America (“IIABA”). See Zen. Ex. AO. As early as the
5 summer of 2014, Washington insurance producers, fearful they could not compete with Zenefits,
6 began to complain to OIC about Zenefits’ free HR services. See, e.g., Zen. Ex. F; Zen. Ex. W.

8 **a. OIC’s Investigations Unit concluded, and its chief attorney confirmed, that
9 Zenefits’ business model does not violate the anti-rebating statutes.**

10 In response to one of those complaints, Mark Durphy, OIC’s Investigations Manager,
11 Legal Affairs Division, reviewed Zenefits and on June 30, 2014, reported to the complaining
12 broker:

13 We received information from Zenefits that clients are not required to use
14 Zenefits as their insurance broker to receive their other services. A client may
15 purchase their HR and payroll services “à la carte” and there is no mandatory
16 linkage of non-insurance functions to the insurance related functions. . . . At this
point we have no indication that Zenefits is offering rebates or illegal inducements
regarding the sale of insurance.

17 Zen. Ex. F. On December 2, 2014, Deputy Insurance Commissioner for Legal Affairs, AnnaLisa
18 Gellermann—OIC’s chief attorney—confirmed that she, Commissioner Michael Kreidler, and
19 Chief Deputy Commissioner Jim Odiorne met with Zenefits to review its platform, and that “we
20 concluded because the software is provided for free to all consumers, regardless of the decision
21 to purchase insurance, it did not constitute an inducement.” Zen. Ex. I.

22 John Hamje, Deputy Insurance Commissioner for Consumer Protection, who often acted
23 as the agency’s point of contact for Washington producers and the IIABW, apparently was not
24 satisfied. On December 5, 2014, shortly after he met with IIABW’s Executive Vice President
25 Daniel Holst and its top lobbyist Bill Stauffacher “about the rebate/inducement issue,” Hamje
26

1 pleaded with Gellermann: “I really think we should take another look at Zenefits and rebating
2 and soon. Please include me in the discussion. Is there anything that you suggest I share with
3 Dan [Holst] in the meantime?” Zen. Ex. K. Two days later, Hamje assured Holst: “The OIC has
4 not given its blessing to the Zenefits business model. We are continuing our review of it.” Zen.
5 Ex. M (emphasis in original).⁶

7 **OIC’s Legal Affairs Division conducted another investigation, again concluding**
8 **Zenefits does not violate anti-rebating statutes.**

9 On the heels of IIABW’s outreach to Hamje, OIC conducted another, more in-depth
10 analysis of Zenefits’ business model. That task was assigned to Marcia Stickler (“Stickler”), an
11 OIC Staff Attorney. On January 9, 2015, Stickler issued an “Informal Legal Opinion re:
12 Compliance of Zenefits with RCW 48.30.150” (“Stickler memo”) in which she concluded
13 unequivocally that Zenefits was not in violation of the Washington statute. Zen. Ex. T.⁷
14 Stickler’s memo noted that the statute “requires that a prohibited inducement have some
15 connection with an insurance transaction or otherwise be an inducement, or incentive, to the
16

17 ⁶ The record reflects that this assurance was not entirely accurate. *See* Zen. Ex. K (on Dec.
18 8, following Hamje’s Dec. 5 request to “take another look” at Zenefits, Gellermann reported only
19 “we *may* be considering something” (emphasis added)).

20 ⁷ Stickler’s memo contrasted Washington’s statute with Utah’s anti-inducement statute.
21 Although Utah originally concluded the Zenefits platform violated its anti-inducement law, the
22 statute at issue there, as Stickler noted, was “very different” from those of Washington and other
23 states. Zen. Ex. T. Utah’s law specifically prohibited “insurer[s] [or] third party administrator[s]
24 who contract[] with an insurer” from providing non-insurance services such as “payroll services
25 . . . performance reviews . . . accounting services” or other HR services unless the insurer pays a
26 fee “that shall equal or exceed the fair market value of the item.” Utah Code Ann. § 31A-23a-
27 402.5(5)(b), (8), (9) (2014) (repealed 2015) (Attachment 2); *see also* National Association of
28 Insurance Commissioners’ (“NAIC”) Model Unfair Trade Practices Act, MDL-880, at 4(H)(1),
29 (“Model Act”). Shortly after the Utah Department of Insurance found Zenefits in violation, the
30 state legislature amended the anti-inducement statute to expressly permit producers to offer free
31 services offered on the same terms to all with no obligation to purchase insurance. *See* Utah
32 Code Ann. § 31A-23a-402.5 (2015) (Attachment 3).

1 purchase of insurance.” *Id.* As Stickler correctly observed:

2 Zenefits offers the human resources applications without charge or obligation to
3 the general public and does not depend on or seek insurance business as a result.
4 Those who do buy insurance through Zenefits get no special reward or privilege,
5 i.e., a rebate. Since the insurance and non-insurance products/services offered by
6 Zenefits are available to the general public without cost and there is no
7 inducement or relation to the insurance products it offers, Zenefits does not
8 violate the illegal inducement statute. . . .

9 Inasmuch as small businesses and consumers benefit from this service, and the
10 purchase of insurance is not connected to the other services, and the user will get
11 no enhanced benefit if he or she does purchase insurance from Zenefits, there is
12 not a violation of the illegal inducement or rebate statute.

13 *Id.* Stickler further concluded that “[p]ublic policy considerations should permit this activity as
14 consumers are benefitted by convenience and ease of use for employee benefit management
15 unrelated to the purchase or solicitation of insurance.” *Id.*

16 **c. OIC rejected the conclusions reached by its Investigations Unit and its Legal**
17 **Affairs Division and opened yet another investigation of Zenefits.**

18 This, apparently, was not the conclusion Hamje was hoping for. Within weeks, OIC
19 senior deputies, including Hamje, decided to reject Stickler’s analysis and opened a formal
20 investigation into Zenefits on February 23, 2015. *See* Zen. Ex. W. The memo directing Durphy
21 to conduct a formal investigation provided no explanation for the about-face, besides noting that
22 “complaints had been received by the OIC about Zenefits from Washington producers as well as
23 the [IIABW]” and “[i]nformation about Zenefits’ operations was subsequently discussed by the
24 OIC’s Executive Management Team and it was determined that further inquiry into Zenefits
25 operations was needed.”⁸ *Id.* On the same day that OIC launched a formal investigation into

26 ⁸ Later in the summer of 2015, Stickler disputed Durphy’s suggestion that her memo was
27 somehow not on point because it was limited to an analysis of “Washington’s rebating laws vs.

1 Zenefits, Hamje assured Wes Bissett, Senior Counsel, Government Affairs of the national
2 IIABA, that “Zenefits and its business model are currently under review.” Zen. Ex. X.

3
4 **III. OIC’s “formal investigation” uncovered no facts justifying its reversal.**

5 According to materials produced by OIC to Zenefits pursuant to a public records request,
6 in the *eighteen months* between launching a formal investigation and announcing in August 2016
7 that it would seek a cease and desist order against Zenefits, OIC uncovered no additional facts or
8 evidence of any significance, let alone anything that would justify the rejection of Stickler’s
9 analysis. Indeed, the record reflects that OIC did little more than interview 28 customers who
10 had elected to designate Zenefits as their broker of record, and meet regularly with the traditional
11 producer lobby who considered Zenefits a competitive threat. *See* Zen. Ex. AI; Zen. Ex. AZ.⁹
12 The memoranda of interviews conducted by OIC Investigators Deb Calhoun and Harvey
13 Churchill confirm that customers received no benefits or discounts in exchange for designating
14 Zenefits as their broker of record. *See, e.g.,* Zen. Ex. AI, at 1 (Zenefits “was very up front that
15 they did not need to sign up for insurance benefits through Zenefits” to obtain the free services).
16 They further reflect that customers were nearly uniformly pleased with Zenefits’ services and
17 that those who did elect to use Zenefits as broker of record did so not because of the free services
18 but because “Zenefits made it a much simpler process” or because they were “unhappy with their
19 current insurance broker.” *Id.* at 7.
20
21
22

23 Utah’s,” informing him: “That’s not entirely true—management had second thoughts.” Zen. Ex.
24 AF.

25 ⁹ Zenefits also provided detailed information and data in response to OIC requests on a
26 number of occasions. *See, e.g.,* Zen. Ex. AR.

1 With interviews complete, OIC appeared ready to make a determination in late summer
2 of 2015. *See* Zen. Ex. AJ; Zen. Ex. AK. OIC records reflect that the OIC senior deputies met to
3 discuss Zenefits on September 14, 2015. Zen. Ex. BK. Although a three-page draft Final Report
4 of Investigation emerged from that meeting, that report contained no legal analysis and had a
5 blank space for the agency's ultimate—presumably still undetermined—conclusion. *Id.* The
6 record also reflects that responsibility for the Zenefits investigation was transferred from
7 Gellermann's Legal Affairs department—which had concluded there was no violation—to
8 Hamje's Consumer Protection department on October 5, 2015. Zen. Ex. BJ at 1.

9
10 Records obtained from OIC reflect little fact-finding or activity by the agency between
11 October 2015 and August 1, 2016, when OIC completed its Final Investigative Report. Hamje,
12 however, continued to make himself regularly available to the IIABW, its members, and its
13 lobbyists, who kept up a constant drumbeat of pressure and complaints. *See, e.g.,* Zen. Ex. AF
14 (Wells Fargo complaint); Zen. Ex. AH (July 28, 2015, IIABW inquiry into “your department’s
15 response to Zenefits” and Hamje’s response: “Our investigation regarding Zenefits continues”);
16 Zen. Ex. AJ (Aug. 20, 2015, IIABW inquiry to Hamje: “John, Bill Stauffacher, Wes Bissett and I
17 would like to meet with you by phone briefly to discuss the Zenefits rebating issue”); Zen. Ex.
18 AL (Sept. 10, 2015, IIABW staff met with Hamje); Zen. Ex. AO (same); Zen. Ex. AS (Oct. 5,
19 2015, complaint from Bob Wallin Insurance, Inc.); Zen. Ex. BJ at 8-12 (Feb. 26, 2016, Hamje
20 meeting with Holst and Bissett regarding Zenefits in which Holst notes that he has “never taken
21 pot shots at OIC—but this is something [the Commissioner] will hear about from [IIABW]
22 members”); *id.* at 11 (Feb. 26, 2016, Hamje call with Chris Free, a member of the
23 Commissioner’s Life and Disability Agent and Broker Advisory Committee, in which Free
24 complains about Zenefits).

1 On August 1, 2016—a year and a half after rejecting the investigative and legal team’s
2 findings—OIC issued its Final Investigative Report. That Report is notable for a number of
3 reasons. Most notably, unlike the Stickler memo, the Report contains no legal analysis or
4 statutory interpretation, no consideration of the purpose of the anti-rebating statutes, and no
5 application of the facts to the law. The 13-page Report simply concludes that the allegation that
6 Zenefits is violating the inducement laws “is substantiated,” without explaining how or why.
7 Zen. Ex. AZ. In fact, the Report confirmed, once again, the lack of any connection between the
8 free services and an insurance transaction:
9

10 All of the above listed Zenefits HR features, except for the Insurance Benefits
11 feature *are available to any employer regardless of whether or not they chose to*
12 *use Zenefits as their insurance producer. If an employer chooses to use Zenefits*
13 *as their insurance producer, they receive no additional benefits through the*
14 *Zenefits Dashboard or cloud-based program. Employers may also use the above*
15 *listed HR features and elect to have their insurance benefits administered through*
16 *their current broker of record. Zenefits does not require anyone to become an*
17 *insurance client to access the core HR features offered by Zenefits cloud-based*
18 *program. Furthermore, since Zenefits is a licensed Washington producer, an*
19 *employer can opt not to use any of the Zenefits HR programs or cloud-based*
20 *software, and still use Zenefits as their insurance producer. Additionally, the*
21 *features of the HR program that do require a fee are billed at the same rate for*
22 *insurance and non-insurance customers. . . . The Zenefits representative*
23 *explained to [the customers interviewed by OIC] that it was not a requirement*
24 *that they participate in the benefits feature of the HR platform in order to access*
25 *the other features of the free software platform.*

26 *Id.* (emphases added). Nonetheless, OIC’s Final Report found Zenefits in violation of RCW
27 48.30.140 and RCW 48.30.150.

28 Notably, OIC did not provide Zenefits with a copy of its Final Report or any other
rationale for its decision.¹⁰ Zenefits did not learn about OIC’s conclusion until several weeks

¹⁰ Zenefits was later able to obtain the Report through a public records request.

1 later, when its counsel received a call from OIC on August 17, 2016, informing him that a cease
2 and desist order was imminent. The decision came as a surprise to Zenefits, since the company
3 had not heard from OIC in many months and reasonably assumed the agency had declined to
4 take action. To this day, Zenefits has not been provided with a rationale for OIC's decision.
5

6 **IV. Zenefits entered into a Consent Order with OIC.**

7 Faced with the prospect of a cease and desist order which would have prevented the
8 company from doing business in Washington and disrupted brokerage services for its
9 Washington customers, Zenefits entered into the Consent Order on November 23, 2016. Zenefits
10 agreed to temporarily modify its offerings in Washington and "begin to charge Washington
11 customers for the previously free apps and functionality," subject to its right to appeal OIC's
12 determination "that RCW 48.30.140 and RCW 48.30.150 prohibit a licensee like Zenefits, acting
13 directly or through affiliates, from offering valuable software functions or other valuable benefits
14 for free or at less than fair market value to the public." Zen. Ex. CR. As a result, Washington is
15 now the only state in the nation to force small businesses and nonprofits to pay for technology
16 and services that are free everywhere else.
17

18 Zenefits immediately took steps to comply with the Consent Order, which was a time-
19 consuming, costly, and disruptive process. Zenefits diverted employees and other resources to
20 notify hundreds of Washington customers that they would need to start paying for services they
21 were receiving for free. Zenefits also had to reprogram its platform, revise marketing materials,
22 and train employees, among other things, to ensure compliance with the Consent Order.
23

24 As noted above, the complaints that OIC received about Zenefits came from the
25 traditional producer community and its lobbyists, not from consumers. Consumers, however,
26 became very engaged when they learned about OIC's requirement that Zenefits charge for all
27

1 services. They accused OIC of “protecting an antiquated insurance broker model,” “hurting
2 small business owners,” imposing a “tax on business,” and “doing the OPPOSITE of what you
3 should be doing . . . helping consumers get the most for their money.” Zen. Ex. BA; Zen. Ex.
4 BC; Zen. Ex. BD.

5
6 Numerous other Zenefits customers confirmed that: they turned to Zenefits because it
7 helped them more efficiently manage their human resources and payroll administration; they felt
8 no pressure to designate Zenefits as their broker of record or to purchase insurance products
9 through Zenefits; if they did designate Zenefits as broker of record, they did so knowing that
10 they were not required to do so in order to access Zenefits’ free services; Zenefits’ free services
11 did not induce them to purchase insurance through Zenefits; and they incurred significant costs
12 as a result of OIC’s requirement that Zenefits charge for previously free services. *See* Zen. Ex.
13 BQ (Affidavit of Jennifer Biely); Zen. Ex. BR (Affidavit of John Traynor); Zen. Ex. BS
14 (Affidavit of Bryan Abell); Zen. Ex. BT (Affidavit of Casey Otley); Zen. Ex. BU (Affidavit of
15 Mark Dorsey). As a result of the Consent Order, Zenefits estimates that by year’s end,
16 Washington small businesses will have been forced to pay hundreds of thousands of dollars for
17 previously free services.
18

19 ARGUMENT

20 **I. Zenefits has not violated Washington’s anti-rebating statutes, which require a** 21 **connection between an “incentive” and an “insurance transaction.”**

22 Washington’s anti-rebating statutes on their face apply only when an incentive is offered
23 in connection with an insurance transaction. Statutory construction begins by reading the text of
24 the statute involved. *State v. Avery*, 103 Wash. App. 527, 532 (2000). If a statute is
25 unambiguous after a review of the plain meaning, the court’s inquiry ends. *Lake v. Woodcreek*
26 *Homeowners Ass’n*, 169 Wash. 2d 516, 526 (2010). Washington’s anti-rebating statute provides
27
28 ZENEFITS’ HEARING BRIEF -- PAGE 13

1 in relevant part:

2 [N]o insurer, insurance producer, or title insurance agent shall, *as an inducement*
3 *to insurance*, or after insurance has been effected, directly or indirectly, offer,
4 promise, allow, give, set off, or pay to the insured or to any employee of the
5 insured, any rebate, discount, abatement, or reduction of premium or any part
6 thereof named in any insurance contract, or any commission thereon, or earnings,
profits, dividends, or other benefit, or any other valuable consideration or
inducement whatsoever which is not expressly provided for in the policy.

7 RCW 48.30.140(1) (emphasis added). Similarly, RCW 48.30.150 provides in pertinent part:

8 No insurer, insurance producer, title insurance agent, or other person shall, *as an*
9 *inducement to insurance, or in connection with any insurance transaction*,
10 provide in any policy for, or offer, or sell, buy, or offer or promise to buy or give,
11 or promise, or allow to, or on behalf of, the insured or prospective insured in any
12 manner whatsoever . . . shares of stock . . . profits or special returns . . . prizes,
wares, gift cards, gift certificates, or merchandise of an aggregate value in excess
of one hundred dollars per person in the aggregate in any consecutive twelve-
month period.

13 These statutes' operative provisions make abundantly clear that there must be a
14 connection between the benefit conferred and an insurance transaction. Only those benefits
15 offered "in connection with any insurance transaction" or "as an inducement to insurance"
16 violate the statutes. This stands to reason: benefits offered in the absence of an insurance
17 transaction, or irrespective of whether insurance is transacted, by definition cannot function as a
18 rebate or inducement to insurance because one need not purchase insurance to get them.
19

20 The requirement of a connection between an "inducement" and the purchase of insurance
21 is further underscored by section 48.30.140's prohibition on "valuable consideration," effectively
22 prohibiting insurance producers from offering or providing additional benefits in exchange for
23 buying insurance. *See, e.g.*, Restatement (Second) of Contracts § 71 (consideration "must be
24 bargained for" and provided "in exchange" for the parties' agreement).
25

26 A benefit provided by an insurance producer that remains the same regardless of whether
27

1 the consumer buys an insurance policy, and that is provided as part of a package of non-
2 insurance services, has no such nexus to an insurance transaction. Services, such as those in
3 Zenefits' Bronze tier, that are provided free to the general public, with no obligation to purchase
4 insurance thus cannot operate as an inducement to insurance. *Cf. McGuire v. Am. Family Mut.*
5 *Ins. Co.*, 448 Fed. App'x 801, 812 (10th Cir. 2011) (holding that a producer's payment of an
6 insured's premium "was a special favor or advantage not generally available to others and
7 therefore constitutes discriminatory rebating").¹¹

9 It is undisputed that Zenefits' model does not discriminate between consumers based on
10 who purchases insurance through Zenefits. Zen. Ex. BP; Zen. Ex. BO. OIC agrees that: (1)
11 every Zenefits user has access to the same products and services, on the same terms, regardless
12 of whether they purchase or even inquire about insurance; (2) there is no special benefit for
13 purchasing insurance; and (3) there is no penalty for deciding not to purchase insurance. *See*
14 *Zen. Ex. F; Zen. Ex. I; Zen. Ex. T.* All Zenefits accountholders—the majority of whom do not
15 use Zenefits for insurance—have the same access to the same non-insurance services on the
16 same terms and at the same prices as the minority of customers who do elect to use Zenefits for
17

18
19
20 ¹¹ Even if there were not a nexus requirement, the narrow and precise statutory language of
21 RCW 48.30.150 precludes an expansive reading of the statute to prohibit the offering of free
22 services on an integrated HR platform. The statute prohibits the offering of three very specific
23 categories of items as an inducement to the sale of insurance: "(a) Any shares of stock or other
24 securities issued or at any time to be issued on any interest therein or rights thereto; or (b) Any
25 special advisory board contract, or other contract, agreement or understanding of any kind,
26 offering, providing for, or promising any profits or special returns or special dividends; or (c)
27 Any prizes, goods, wares, gift cards, gift certificates, or merchandise of an aggregate value in
28 excess of one hundred dollars" RCW 48.30.150. The offering of certain free services as
part of an integrated HR and benefits platform is not and cannot reasonably be interpreted to be
"shares of stock or securities," a "contract" providing "profits or special returns or special
dividends," or a "prize," "good," "ware," "gift card," "gift certificate," or "merchandise."

1 insurance. At no point does Zenefits offer, sell, buy, or offer or promise to buy or give, allow,
2 give, set off, or pay its insured customers a rebate or benefit if they purchase insurance, which is
3 required to violate the statutes.
4

5 OIC has acknowledged as much, concluding on at least three different occasions that
6 Zenefits' business model does not violate RCW 48.30.140 and RCW 48.30.150. In June 2014,
7 Durphy, in consultation with the OIC Legal Affairs department, concluded that Zenefits was not
8 in violation of RCW 48.30.140 or RCW 48.30.150 because "[Zenefits is] not offering anything
9 for free to a client *in exchange for them being their broker.*" Zen. Ex. F (emphasis added).
10 Gellermann, Commissioner Kreidler, and others met with Zenefits and its counsel in the fall of
11 2014 to learn more about the Zenefits platform and services, and subsequently "concluded
12 because the software is provided free to all consumers, regardless of the decision to purchase
13 insurance, it did not constitute an inducement." Zen. Ex. I. Staff attorney Stickler came to the
14 same conclusion in her thorough legal and factual analysis on January 9, 2015. Zen. Ex. T.
15

16 **II. Legislative history makes clear that anti-rebating statutes exist to prevent**
17 **discriminatory treatment and preserve insurer solvency, not to stifle competition**
18 **and innovation to the detriment of consumers.**

19 The common sense reading of the statutory language reflected in Durphy's,
20 Gellermann's, and Stickler's analyses is consistent with the policy goals underlying anti-rebating
21 and anti-inducement statutes. *See State ex rel. Faulk v. CSG Job Ctr.*, 816 P.2d 725, 729 (Wash.
22 1991) ("A statute is to be interpreted in a manner that is consistent with its underlying
23 purpose."). Some historical background is necessary to understand the purpose and genesis of
24 these statutes. In the post-Civil War nineteenth century, the insurance industry grew
25 dramatically, creating high demand for brokers. *See Robert H. Jerry & Reginald L. Robinson,*
26 *Statutory Prohibitions on the Negotiation of Insurance Agent Commissions: Substantive Due*
27

1 *Process Review Under State Constitutions*, 51 Ohio St. L. J. 773, 776-77 (1990). Competition
2 among insurers to retain brokers was fierce, and insurers offered lucrative commission packages
3 to retain their services. *Id.* Brokers, in turn, frequently offered to pay, or “rebate,” a portion of
4 their commission to their customers in order to secure their business. *Id.* This practice had the
5 effect of lowering a customer’s effective premium and resulted in unfair discrimination among
6 insureds, with some receiving lower premiums than others with the same risk characteristics for
7 identical coverage. *Id.*

8
9 To combat discrimination and protect consumers, nearly every state adopted anti-rebating
10 statutes in the late-nineteenth and early-twentieth centuries. As leading commentators note:

11
12 In these early years, much of the public’s revulsion at insurance industry abuses
13 centered on preferential treatment. . . . Whether the preferential treatment for one
14 class of insureds was overt or covert, the effect was the same: when an insurer
15 allowed *some members of a similarly-situated class of insureds to pay a lower
16 premium than other insureds*, the insureds who did not enjoy the benefit
17 subsidized the others. That was widely perceived as being fundamentally unfair.

18 *Id.* at 779 (emphasis added).

19 The anti-rebating statutes were also prompted by concern that rebating increased the risk
20 of insurer insolvency. As two commentators explain: “If the premium advertised by the insurer
21 is presumed to be fair, reasonable, and sufficient to provide a reserve to meet future claims,
22 giving rebates to insureds could, in the long-run, prevent the insurer from meeting its
23 obligations.”¹² *Id.* at 780; see also Mark Frankel, *Insurance Agent Commission Deregulation:
24 Anti-Rebate Laws and an Alternative to Repeal*, 2 J. Ins. Reg. 255, 255 (1983) (Attachment 4).

25 ¹² OIC has acknowledged that Zenefits’ offering of free services does not present an
26 insolvency risk. See Zen. Ex. T (“Zenefits apparently bears the cost of providing the non-
27 insurance services alone, and so the insurer’s revenue and ability to pay claims is unaffected.”).

1 Over the course of a century, courts uniformly have recognized that these statutes were
2 intended to protect *consumers* from discriminatory pricing—not to protect producers from
3 competition and entrench outdated business practices that raise consumer costs and compromise
4 customer service. *See, e.g., Calvin Phillips & Co. v. Fishback*, 84 Wash. 124, 129 (1915) (“The
5 evident intent of the [anti-rebating] statute . . . is to establish uniform rates of insurance
6 throughout the state, and to maintain an absolute standard of insurance rates.”); *Gibson v. New*
7 *York Life Ins. Co.*, 102 Wash. 180, 183 (1918) (“One of the purposes of the [anti-rebating]
8 statute was to require that the policy and the application should constitute the entire contract.”);
9 *Wolfe v. Philippine Inv. Co., Inc.*, 175 Wash. 165, 168 (1933) (“The purpose of [the anti-
10 rebating] statute was to establish uniform insurance rates throughout the state and to maintain a
11 standard of such rates.”); *Cliffside Nursing Home Inc. v. Estate of Wolf*, 2014 WL 223384, No.
12 4154/2013, at *3 (N.Y. Sup. Ct. Jan. 14, 2014) (“The purpose of the anti-rebate statutes is to
13 ensure that insurance providers, including brokers, ‘provide insurance in a nondiscriminatory
14 manner to like insureds or potential insureds, and to prohibit such an insurer or insurance
15 producer from providing an insured or potential insured with any special benefit not afforded to
16 other insureds or potential insureds.”); *McGuire*, 448 Fed. App’x at 810 (“In construing the
17 ordinary words of these statutes and applying Kansas’ most fundamental rule in determining the
18 legislature’s intent from those words, it is clear that the legislature’s intent in passing [the anti-
19 rebating laws] was to prevent or prohibit unfair discrimination practices in the business of
20 insurance.”); State of New York Ins. Dept., Circular Letter No. 9 at 1, Mar. 3, 2009 (Attachment
21 5) (recognizing underlying purpose behind anti-rebating law was to protect consumers from
22 discrimination by insurers).

26 In sum, nothing in the statutory language or the history and purpose of the anti-rebating
27 ZENEFITS’ HEARING BRIEF – PAGE 18
28

1 statutes prohibits a company like Zenefits from offering certain free human resources services
2 when those services are available on equal terms to the general public regardless of whether they
3 purchase insurance through Zenefits.
4

5 **III. OIC's interpretation of RCW 48.30.140 and RCW 48.30.150 is directly at odds with**
6 **the conclusions of other states, which have interpreted identical or nearly-identical**
7 **anti-rebating and anti-inducement statutes.**

8 Numerous regulators who specifically examined Zenefits' business model have found
9 that it does not violate the anti-rebating and anti-inducement statutes of their states, which are
10 substantively identical to Washington's statutes. The North Carolina Department of Justice, for
11 example, recently concluded that Zenefits "is not engaging in rebating in violation" of North
12 Carolina insurance laws because "Zenefits is not offering its free platform in exchange for
13 brokering insurance . . . [and] [c]onsumers are not penalized for not using Zenefits as its
14 insurance broker." Zen. Ex. Y. The Office of Montana's State Auditor concluded that Zenefits'
15 platform is not a rebate or inducement, and that "[t]his interpretation is also good public policy,
16 as Zenefits may potentially provide Montana small businesses with services they would
17 otherwise not be able to afford." Zen. Ex. AG. Michigan, Indiana, Arizona, Connecticut, and
18 Maryland reached similar conclusions in interpreting their anti-rebating and anti-inducement
19 statutes. Zen. Ex. P (Michigan); Zen. Ex. R (Indiana); Zen. Ex. S (Arizona); Zen. Ex. Z
20 (Connecticut); Zen. Ex. AW (Maryland).
21

22 Guidance involving analogous situations issued by regulators in other states also makes
23 clear that Zenefits' business model does not constitute an illegal inducement or rebate. For
24 instance:

- 25 • The Louisiana Department of Insurance recently concluded that "where the
26 thing of value is available to the general public, the recipient of the thing of
27 value has received no special favor or advantage through the contract of
28 insurance." Zen. Ex. BX. As a result, "it cannot be reasonably asserted that

1 the thing of value served as valuable consideration or inducement to the
2 contract because its recipient could obtain the thing of value irrespective of
3 any contractual relationship regarding insurance.” *Id.*

- 4 • New York similarly concluded that a broker offering a free online wellness
5 program to customers does not create an unlawful inducement “as long as
6 access to the wellness program’s free services is not contingent upon the
7 purchase of insurance policies sold by the broker or the solicitation thereof by
8 either the broker or the wellness program provider, or limited to the broker’s
9 clients.” Zen. Ex. C.
- 10 • Kansas also found that the key question in determining an anti-rebating statute
11 violation is “whether the company has provided or arranged for or an insured
12 has received any special favor or advantage that is not generally available to
13 others.” Zen. Ex. A.
- 14 • Several other states agree that anti-inducement statutes “do not prohibit the
15 use of a ‘gift’ as a marketing tool when the ‘gift’ is given whether or not the
16 individual actually purchases or renews the insurance.” Zen. Ex. E (Rhode
17 Island Dep’t of Business Regulation Bulletin No. 2009-9); *see also* Zen. Ex. V
18 (Tennessee Dep’t of Commerce and Ins. Bulletin (“Gifts and valuable
19 consideration offered to potential consumers irrespective of whether they
20 purchase a policy, such as gift offers for requesting an insurance quote, will
21 not be considered an inducement to a policy in violation of the rebating
22 statute.”)).

23 These states—following the unambiguous statutory language requiring an inducement “to
24 insurance” or “in connection with an insurance transaction”—got it exactly right. Although not
25 binding in Washington, these decisions are instructive because the respective anti-rebating and
26 anti-inducement statutes are identical in all material respects to Washington’s anti-rebating
27 statutes. Most states’ anti-rebating and anti-inducement statutes, including Washington’s, are
28 modeled on Section 4 of the Model Act, which prohibits “paying or allowing or giving or
offering to pay, allow, or give, directly or indirectly, *as inducement to [an insurance] policy*, any
rebate of premiums payable on the policy, or any special favor or advantage in the dividends or
other benefits thereon, or any valuable consideration or inducement whatever not specified in the
policy.” Zen. Ex. CL (emphasis added).

1 Notably, OIC has acknowledged the importance of consistency and uniformity among
2 state regulators in its 2017-2023 Strategic Plan. See Office of the Insurance Commissioner,
3 Strategic Plan 2017-2023, at 6 (July 2016), available at
4 <https://www.insurance.wa.gov/sites/default/files/documents/OIC-2017-2023-strategic-plan.pdf>.
5

6 In sum, OIC's order is not only inconsistent with the statutory language, the legislative history,
7 its own analyses, and the conclusions of every state to consider similar statutes; it is also
8 inconsistent with its own policy goal of promoting consistency across states.

9 **IV. OIC's conclusion is inconsistent with OIC precedent.**

10 In other contexts—including instances in which, unlike here, a licensee provided valuable
11 benefits exclusively to insurance customers—OIC has acknowledged the public policy benefit of
12 allowing insurers to offer free services to consumers. For example, in September 2015, OIC
13 considered whether BlueCross BlueShield (“BCBS”) violated RCW 48.30.140 and RCW
14 48.30.150 by offering insurance customers free identity protection services. Zen. Ex. AM; Zen.
15 Ex. AN. Charles Brown, OIC Senior Insurance Enforcement Specialist (viewed as the agency
16 expert on the anti-rebating statutes (Zen. Ex. AN)), noted to Gellermann: “It doesn’t make sense
17 to me from a consumer protection or regulatory standpoint to tell [BCBS] they cannot offer
18 subscribers identity theft protection services. . . . I tend to agree with the carriers that this
19 offering does not pose the kind of threat or problem the inducement and rebate statutes were
20 intended to address.” Zen. Ex. AN. Gellermann agreed, noting that “[a]s a matter of policy, I
21 don’t see that this offering raises the problem that the rebate and inducement statutes were
22 intended to prevent.” Zen. Ex. AM. Brown and Gellermann recommended telling BCBS: “[W]e
23 do not intend to take any regulatory action to block this program.” Zen. Ex. AM; Zen. Ex. AN.
24 The lack of any public documents reflecting action against BCBS suggests that is exactly what
25
26
27

1 OIC did.

2 OIC's contemporaneous, conflicting conclusions regarding BCBS and Zenefits cannot be
3 reconciled, and demonstrate the arbitrary and capricious nature of OIC's Consent Order. Unlike
4 Zenefits' offering, BCBS's identity protection service was made available *only to insurance*
5 *customers* and only "*after insurance has been effected.*" Zen. Ex. AM (emphasis added). If
6 BCBS did not violate RCW 48.30.140 and RCW 48.30.150 when it provided free non-insurance
7 services exclusively to its insurance customers, Zenefits, *a fortiori*, does not violate the statutes
8 when it makes non-insurance services available on equal terms to everyone.
9

10 **V. OIC's overly expansive interpretation of the anti-rebating statutes will have**
11 **negative, unintended consequences for other consumers and industries doing**
12 **business in Washington.**

13 OIC's overly expansive interpretation of the anti-rebating statutes will have significant
14 consequences not only for Zenefits and its Washington customers, but for many other consumers
15 and companies doing business in Washington. Many businesses, including banks, travel
16 companies, retailers, and payroll companies, offer both discounted or free services *and* are
17 licensed producers offering insurance products in Washington. OIC has provided no legitimate
18 reason why these businesses are not also running afoul of the statutes according to its
19 interpretation, and its failure to do so reflects the unprincipled, misguided, and ends-driven
20 approach it has taken to its investigation of Zenefits.
21

22 For example, online discount retailer Overstock.com offers deep discounts on a wide
23 variety of consumer products to the general public, as well as free shipping, dining rewards, and
24 other rewards to its Club O Gold members. Zen. Ex. CA. Its affiliate, Overstock.com Insurance
25 Agency, holds an active insurance producer license in Washington. *Id.* OIC's conclusion that
26 Washington's anti-rebating statutes "prohibit a licensee like Zenefits, acting directly or through
27

1 affiliates, from offering . . . valuable benefits for free or at less than fair market value to the
2 public” would mean that Overstock.com may not offer discounts or membership rewards and
3 benefits to Washington consumers without violating the anti-rebating statutes. Similarly,
4 Expedia, Inc., an online travel company, offers a host of free benefits and discounted travel-
5 related services, and also holds an active insurance producer license in Washington. Zen. Ex.
6 BZ. Indeed, Expedia’s revenue from its travel insurance products is a growing segment of its
7 business. Zen. Ex. BZ at 62. Under OIC’s interpretation, Expedia is prohibited from offering
8 free benefits or discounts to Washington consumers because, by OIC’s reckoning, these benefits
9 are illegal inducements to purchase travel insurance from Expedia. There are hosts of other
10 examples in these and other industries. *See, e.g.,* Zenefits Ex. BV (Costco wholesale discounts
11 and insurance); Zen. Ex. BY (ADP employer and professional employer organization services,
12 including insurance, and “Perks at Work” discounts); Zen. Ex. CB (USAA Bank free checking,
13 car rental discounts, and insurance).

16 CONCLUSION

17 It is undisputed that Zenefits offers its platform and its free and fee-based services on
18 equal terms to any business regardless of whether it elects to use Zenefits as an insurance broker.
19 It is also undisputed that customers who choose to purchase insurance through Zenefits receive
20 no special or additional benefits. OIC’s contorted and unprecedented interpretation of RCW
21 48.30.140 and RCW 48.30.150 to find a violation under these circumstances finds no support in
22 the statutory text—which requires a nexus between free offerings and insurance—or the
23 legislative history—which makes clear that these statutes were designed to prevent
24 discriminatory treatment of consumers and preserve insurer solvency, *not* to protect an
25 entrenched and politically powerful lobby at the expense of Washington consumers and small

1 businesses.

2 The anti-rebating statutes are blunt tools. Interpreted too broadly, they have the potential
3 to frustrate innovation and harm consumers. Affirming OIC's Consent Order would do just that.
4 Zenefits' integrated platform reduces the administrative complexity of managing HR functions;
5 gives small businesses access to benefits programs that were, until now, too complicated or
6 costly to administer; increases the ease of HR compliance; and creates jobs by freeing up small
7 business owners to focus on growing their businesses. Requiring Zenefits to charge more to
8 access these services simply because it holds an insurance producer license will hurt the very
9 consumers these statutes were intended to protect.
10

11 For all of the foregoing reasons, the Court should rule that RCW 48.30.140 and RCW
12 48.30.150 do not prohibit a licensee like Zenefits, acting directly or through affiliates, from
13 offering valuable software functions or other valuable benefits for free or at less than fair market
14 value to the public, and should reverse OIC's conclusion to the contrary as reflected in the
15 Consent Order.
16

1 Dated this 30th day of June, 2017. Respectfully submitted,

2
3
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CERTIFICATE OF SERVICE

I hereby certify that on this 30th day of June, 2017, a true and correct copy of the foregoing *YourPeople, Inc. dba Zenefits FTW Insurance Services' Hearing Brief* together with *Attachments* was served from Washington, DC to the following individuals:

Via Facsimile, and FedEx, Priority Overnight

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/s/ Jennifer A. Fleury
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Attachment 1

MARKETING ##
The key to effective
mobile discounts

**DEFEND YOUR
RESEARCH** ##
In the afternoon, the
moral slope gets
slipperier

**VISION
STATEMENT** ##
Where did the
graphical icons on
our tech gadgets
come from?

COLUMN ##
Carter Roberts on
strategy and climate
change

IdeaWatch

New Thinking, Research in Progress hbr.org

STRATEGY

Making “Freemium” Work

Many start-ups fail to recognize the challenges of this popular business model.

by Vineet Kumar

Over the past decade “freemium”—a combination of “free” and “premium”—has become the dominant business model among internet start-ups and smartphone app developers. Users get basic features at no cost and can access richer functionality for a subscription fee. If you’ve networked on LinkedIn, shared files through Dropbox, watched TV shows through Hulu, or searched for a mate on Match, you’ve experienced the model firsthand. It works for B2B companies as well—examples include Box, Splunk, and Yammer.

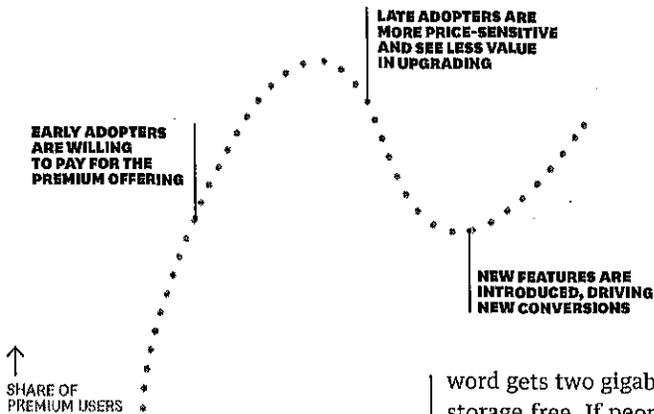
Several factors contribute to the appeal of a freemium strategy. Because free features are a potent marketing tool, the model allows a new venture to scale up and attract a user base

without expending resources on costly ad campaigns or a traditional sales force. The monthly subscription fees typically charged are proving to be a more sustainable source of revenue than the advertising model prevalent among online firms in the early 2000s. Social networks are powerful drivers: Many services offer incentives for referring friends (which is more appealing when the product is free). And freemium is more successful than 30-day free trials or other limited-term offers, because customers have become wary of cumbersome cancellation processes and find indefinite free access more compelling.

But despite its popularity and clear benefits, freemium is still poorly understood. It has inherent challenges, as demonstrated by the many start-ups that have tried but failed to make it work. For several years I have studied freemium models in depth—by coauthoring (with my HBS colleagues Bharat Anand, Sunil Gupta, and Felix Oberholzer-Gee) a case on the *New York Times's* paywall strategy (a variation of the freemium model); conducting a deep dive into the user data of a storage and synchronization company; and coauthoring (with my HBS colleagues Clarence Lee and Sunil Gupta) a working paper on how freemium companies can use referrals to spur usage and upgrades. Through this work I've come up with six questions that start-ups considering a freemium model should ask.

What should be free? Let's say you've created a digital product that has 20 features and you've chosen five that will be free to anyone who registers on your site. Users who want the other 15 will have to pay. How do you know whether you've made the right choices? And if you suspect that you haven't, what should you do?

Recall that one of the chief purposes of freemium is to attract new users. If you're not succeeding with that goal, it probably means that your free offerings are not compelling enough and you need to provide more or better features free. If you're generating lots of traffic but few people are paying to upgrade, you may have the opposite problem: Your free offerings are too



THE LIFE CYCLE OF UPGRADES

Freemium companies typically see the share of paid subscriptions (and therefore cash flow) rise and fall and then rise again in a predictable way over time. Those that don't account for this phenomenon risk failure.

rich, and it's time to cut back. This kind of tuning was evident at the *New York Times* website. After years of unrestricted access, in 2011 the paper began limiting users to 20 free articles a month; people had to subscribe if they wanted to read more. Over subsequent months the company realized it was still giving away too much and was getting too few subscribers as a result, so in 2012 it cut the number of free monthly articles to 10. Start-ups should expect to need similar tweaking to find the optimal balance between traffic and paying customers. The balancing act can be tricky: Users may revolt when asked to pay for things they are accustomed to getting free.

Do customers fully understand the premium offer? Communicating two sets of benefits complicates your marketing efforts. If customers don't clearly grasp what they would gain by upgrading, you will monetize fewer of them than you otherwise might.

Dropbox and LinkedIn are a study in contrasts. The former has attracted 200 million users with a simple proposition: Everyone who enters a username and a pass-

word gets two gigabytes of cloud-based storage free. If people run out of space, they can pay \$9.99 a month (or, alternatively, \$99 a year) for 100 GB of storage. The free version is adequate for basic documents, but anyone who wants to back up photos or other media quickly hits the limit, and the reasons to upgrade are obvious.

For many LinkedIn users, the advantages of upgrading are murkier. I've used LinkedIn for several years to keep in touch with colleagues, and I routinely receive e-mails urging me to upgrade—but the ongoing value of doing so is not apparent. (The company offers four premium subscriptions, some aimed at specific customer segments, such as recruiters or salespeople, and most featuring deeper search functionality, better e-mail capability, and more visibility into who has viewed your profile.) Although LinkedIn is successful—it was one of the first freemium companies to go public—it could probably monetize more users if the distinctions between its free and paid offerings were clearer.

What is your target conversion rate? Imagine that you're the CEO of a freemium start-up and you're handed a report showing your conversion rate (the percentage of free users who have upgraded to a premium plan) for the most recent quarter. What figure do you hope to see?

A rate of 1% is probably too low, especially if you rely on subscription revenue alone. (Some players, including the *New York Times* and LinkedIn, also collect online ad revenue.) It signals either that too much of what you're providing is free—giving users little reason to upgrade—or that consumers don't understand or value your premium features.

But, less obviously, a very high conversion rate isn't necessarily good. Remember that one of the benefits of a freemium model is the ability to generate traffic.

Suppose that 50% of the users of your free product upgrade to premium. You might think that your model is working well; but perhaps your free product is not very compelling, which will limit your potential acquisitions. All other things being equal, you would do better to convert 5% of 2 million monthly visitors, for example, than to convert 50% of 100,000 visitors. The best long-term strategy is generally to aim for a moderate conversion rate (in my research, I've found that most companies' range from 2% to 5%) coupled with a high volume of traffic. If you're targeting a small market, you should aim for a higher rate.

Are you prepared for the conversion life cycle? Let's assume you're attracting plenty of traffic and new users, and your conversion rate is 5%. You want to forecast growth and revenue. Can you simply draw a couple of straight lines, on the assumption that the rate will hold steady?

No. Early adopters are less price-sensitive than others, so they are more likely to upgrade. And often they are people for whom the value proposition is unusually compelling. (For instance, recruiters were

early adopters of LinkedIn, because their business depends on their ability to identify and connect with professionals.) So over time, conversion rates typically dip as the user base expands to include people who are more price-sensitive or who see less value in the service. Although freemium companies universally have a very low marginal cost for each new user—otherwise the model wouldn't make sense—those costs aren't zero. At a minimum, free users put demands on server space and customer service.

Companies that fail to understand these realities may feel a cash crunch as the number of free users grows and the cost of servicing them therefore rises. This is often the reason that companies launched with freemium models pivot away, converting to free time-limited trials or eliminating free offerings altogether. Start-ups that have recently made such a switch include LogMeIn, whose software provides remote access to PCs, and SugarSync, a cloud storage company that competes with Dropbox.

Are users becoming evangelists?

It's important to recognize the full value

of your free users, which takes two forms: Some of them become subscribers, and some draw in new members who become subscribers. In our HBS working paper and in ongoing research, we have found that a free user is typically worth 15% to 25% as much as a premium subscriber, with significant value stemming from referrals. We have also found that firms can increase the value of referrals by carefully managing referral incentives and communications. If you're considering a freemium model, pay close attention to why and how satisfied users might help your product go viral.

Are you committed to ongoing innovation? It's a mistake to see freemium merely as a customer acquisition tool and to drop the free version when new customers stop coming in or when the upgrade rate dives. Users who join late are typically harder to convert; therefore, in order to keep increasing upgrades, you'll need to keep increasing the value of your premium services. Smart companies view freemium not only as a revenue model but also as a commitment to innovation.

Dropbox is a good example. When it launched, in 2008, it was primarily a service for backing up files. It then began offering shared folders, making it a collaboration tool. Newer features allow for automatic syncing of smartphones and other devices and for automatic uploading of photos. Over time the user interface has improved as well. Each new feature has increased the value of the premium offering.

In today's digital era, when the marginal costs of many products are dropping, businesses will increasingly turn to the freemium model. Across industries ranging from media (where companies are forced to rely less on advertising revenue and more on subscriber revenue) to education (where players may eventually seek to monetize mostly free online courses), the model is destined to grow more attractive. Companies can boost their odds of success by considering the six key questions above.

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How Four Companies Use the Model

Among the biggest decisions facing "freemium" businesses are which features to make free and how much to charge for the rest. Here's a look at several approaches:

	Dropbox	LinkedIn	NYTimes.com	Spotify
WHAT IT IS	A cloud storage and file-sharing service	A social media site for professional networking	A digital, enhanced version of the print newspaper	A music streaming and downloading service
WHAT'S FREE	2 GB of storage, with up to 16 GB more for referring friends	Creating a profile, making connections, basic communication	10 articles a month	Unlimited music, interspersed with ads
WHAT'S PREMIUM	100 GB of storage for \$9.99 a month	Advanced searches and communication, starting at \$19.95 a month	Full access, starting at \$3.75 a week	Downloads and ad-free streaming for \$9.99 a month
HOW MANY USE IT	More than 200 million users (free and premium)	277 million users (free and premium) at the end of 2013	53.8 million visitors in December 2013; 760,000 subscribers	24 million users, of whom 6 million are subscribers

Attachment 2

2014 Utah Code Ann. § 31A-23a-402.5

2014 Utah Code Archive

Utah Code Annotated > Title 31A Insurance Code > Chapter 23a Insurance Marketing Licensing Producers, Consultants, and Reinsurance Intermediaries > Part 4 Marketing Practices

31A-23a-402.5. Inducements.

- (1) (a) Except as provided in Subsection (2), a producer, consultant, or other licensee under this title, or an officer or employee of a licensee, may not induce a person to enter into, continue, or terminate an insurance contract by offering a benefit that is not:
 - (i) specified in the insurance contract; or
 - (ii) directly related to the insurance contract.(b) An insurer may not make or knowingly allow an agreement of insurance that is not clearly expressed in the insurance contract to be issued or renewed.
(c) A licensee under this title may not absorb the tax under Section 31A-3-301.
- (2) This section does not apply to a title insurer, an individual title insurance producer, or agency title insurance producer, or an officer or employee of a title insurer, an individual title insurance producer, or an agency title insurance producer.
- (3) Items not prohibited by Subsection (1) include an insurer:
 - (a) reducing premiums because of expense savings;
 - (b) providing to a policyholder or insured one or more incentives, as defined by the commissioner by rule made in accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, to participate in a program or activity designed to reduce claims or claim expenses, including:
 - (i) a premium discount offered to a small or large employer group based on a wellness program if:
 - (A) the premium discount for the employer group does not exceed 20% of the group premium; and
 - (B) the premium discount based on the wellness program is offered uniformly by the insurer to all employer groups in the large or small group market;
 - (ii) a premium discount offered to employees of a small or large employer group in an amount that does not exceed federal limits on wellness program incentives; or
 - (iii) a combination of premium discounts offered to the employer group and the employees of an employer group, based on a wellness program, if:
 - (A) the premium discounts for the employer group comply with Subsection (3)(b)(i); and
 - (B) the premium discounts for the employees of an employer group comply with Subsection (3)(b)(ii); or
 - (c) receiving premiums under an installment payment plan.
- (4) Items not prohibited by Subsection (1) include a producer, consultant, or other licensee, or an officer or employee of a licensee, either directly or through a third party:
 - (a) engaging in a usual kind of social courtesy if receipt of the social courtesy is not conditioned on a quote or the purchase of a particular insurance product;

2014 Utah Code Ann. § 31A-23a-402.5

- (b) extending credit on a premium to the insured:
 - (i) without interest, for no more than 90 days from the effective date of the insurance contract;
 - (ii) for interest that is not less than the legal rate under *Section 15-1-1*, on the unpaid balance after the time period described in Subsection (4)(b)(i); and
 - (iii) except that an installment or payroll deduction payment of premiums on an insurance contract issued under an insurer's mass marketing program is not considered an extension of credit for purposes of this Subsection (4)(b);
- (c) preparing or conducting a survey that:
 - (i) is directly related to an accident and health insurance policy purchased from the licensee; or
 - (ii) is used by the licensee to assess the benefit needs and preferences of insureds, employers, or employees directly related to an insurance product sold by the licensee;
- (d) providing limited human resource services that are directly related to an insurance product sold by the licensee, including:
 - (i) answering questions directly related to:
 - (A) an employee benefit offering or administration, if the insurance product purchased from the licensee is accident and health insurance or health insurance; and
 - (B) employment practices liability, if the insurance product offered by or purchased from the licensee is property or casualty insurance; and
 - (ii) providing limited human resource compliance training and education directly pertaining to an insurance product purchased from the licensee;
- (e) providing the following types of information or guidance:
 - (i) providing guidance directly related to compliance with federal and state laws for an insurance product purchased from the licensee;
 - (ii) providing a workshop or seminar addressing an insurance issue that is directly related to an insurance product purchased from the licensee; or
 - (iii) providing information regarding:
 - (A) employee benefit issues;
 - (B) directly related insurance regulatory and legislative updates; or
 - (C) similar education about an insurance product sold by the licensee and how the insurance product interacts with tax law;
- (f) preparing or providing a form that is directly related to an insurance product purchased from, or offered by, the licensee;
- (g) preparing or providing documents directly related to a premium only cafeteria plan within the meaning of *Section 125, Internal Revenue Code*, or a flexible spending account, but not providing ongoing administration of a flexible spending account;
- (h) providing enrollment and billing assistance, including:
 - (i) providing benefit statements or new hire insurance benefits packages; and
 - (ii) providing technology services such as an electronic enrollment platform or application system;
- (i) communicating coverages in writing and in consultation with the insured and employees;
- (j) providing employee communication materials and notifications directly related to an insurance product purchased from a licensee;
- (k) providing claims management and resolution to the extent permitted under the licensee's license;

2014 Utah Code Ann. § 31A-23a-402.5

- (l) providing underwriting or actuarial analysis or services;
 - (m) negotiating with an insurer regarding the placement and pricing of an insurance product;
 - (n) recommending placement and coverage options;
 - (o) providing a health fair or providing assistance or advice on establishing or operating a wellness program, but not providing any payment for or direct operation of the wellness program;
 - (p) providing COBRA and Utah mini-COBRA administration, consultations, and other services directly related to an insurance product purchased from the licensee;
 - (q) assisting with a summary plan description, including providing a summary plan description wraparound;
 - (r) providing information necessary for the preparation of documents directly related to the Employee Retirement Income Security Act of 1974, 29 U.S.C. Sec. 1001, et seq., as amended;
 - (s) providing information or services directly related to the Health Insurance Portability and Accountability Act of 1996, Pub. L. 104-191, 110 Stat. 1936, as amended, such as services directly related to health care access, portability, and renewability when offered in connection with accident and health insurance sold by a licensee;
 - (t) sending proof of coverage to a third party with a legitimate interest in coverage;
 - (u) providing information in a form approved by the commissioner and directly related to determining whether an insurance product sold by the licensee meets the requirements of a third party contract that requires or references insurance coverage;
 - (v) facilitating risk management services directly related to property and casualty insurance products sold or offered for sale by the licensee, including:
 - (i) risk management;
 - (ii) claims and loss control services;
 - (iii) risk assessment consulting, including analysis of:
 - (A) employer's job descriptions; or
 - (B) employer's safety procedures or manuals; and
 - (iv) providing information and training on best practices;
 - (w) otherwise providing services that are legitimately part of servicing an insurance product purchased from a licensee; and
 - (x) providing other directly related services approved by the department.
- (5) An inducement prohibited under Subsection (1) includes a producer, consultant, or other licensee, or an officer or employee of a licensee:
- (a)
 - (i) providing a rebate;
 - (ii) paying the salary of an employee of a person who purchases an insurance product from the licensee; or
 - (iii) if the licensee is an insurer, or a third party administrator who contracts with an insurer, paying the salary for an onsite staff member to perform an act prohibited under Subsection (5)(b)(xii); or
 - (b) engaging in one or more of the following unless a fee is paid in accordance with Subsection (8):
 - (i) performing background checks of prospective employees;
 - (ii) providing legal services by a person licensed to practice law;

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- (iii) performing drug testing that is directly related to an insurance product purchased from the licensee;
 - (iv) preparing employer or employee handbooks, except that a licensee may:
 - (A) provide information for a medical benefit section of an employee handbook;
 - (B) provide information for the section of an employee handbook directly related to an employment practices liability insurance product purchased from the licensee; or
 - (C) prepare or print an employee benefit enrollment guide;
 - (v) providing job descriptions, postings, and applications for a person;
 - (vi) providing payroll services;
 - (vii) providing performance reviews or performance review training;
 - (viii) providing union advice;
 - (ix) providing accounting services;
 - (x) providing data analysis information technology programs, except as provided in Subsection (4)(h)(ii);
 - (xi) providing administration of health reimbursement accounts or health savings accounts; or
 - (xii) if the licensee is an insurer, or a third party administrator who contracts with an insurer, the insurer issuing an insurance policy that lists in the insurance policy one or more of the following prohibited benefits:
 - (A) performing background checks of prospective employees;
 - (B) providing legal services by a person licensed to practice law;
 - (C) performing drug testing that is directly related to an insurance product purchased from the insurer;
 - (D) preparing employer or employee handbooks;
 - (E) providing job descriptions postings, and applications;
 - (F) providing payroll services;
 - (G) providing performance reviews or performance review training;
 - (H) providing union advice;
 - (I) providing accounting services;
 - (J) providing discrimination testing; or
 - (K) providing data analysis information technology programs.
- (6) A producer, consultant, or other licensee or an officer or employee of a licensee shall itemize and bill separately from any other insurance product or service offered or provided under Subsection (5)(b).
- (7)
- (a) A de minimis gift or meal not to exceed a fair market value of \$ 25 for each individual receiving the gift or meal is presumed to be a social courtesy not conditioned on a quote or purchase of a particular insurance product for purposes of Subsection (4)(a).
 - (b) Notwithstanding Subsection (4)(a), a de minimis gift or meal not to exceed \$ 10 may be conditioned on receipt of a quote of a particular insurance product.
- (8) If as provided under Subsection (5)(b) a producer, consultant, or other licensee is paid a fee to provide an item listed in Subsection (5)(b), the licensee shall comply with Subsection 31A-23a-501(2) in charging the fee, except that the fee paid for the item shall equal or exceed the fair market value of the item.
- (9) For purposes of this section, "fair market value" is determined on the basis of what an individual insured or policyholder would pay on the open market for that item.

History

C. 1953, 31A-23a-402.5, enacted by L. 2011, ch. 62, § 5; 2012, ch. 253, § 24; 2012, ch. 279, § 9; 2013, ch. 319, § 29; L. 2014, ch. 290, § 26; L. 2014, ch. 300, § 26.

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Attachment 3

Utah Code Ann. § 31A-23a-402.5

Statutes current with 2017 legislation effective through May 1, 2017

**Utah Code Annotated > Title 31A Insurance Code > Chapter 23a Insurance Marketing —
Licensing Producers, Consultants, and Reinsurance Intermediaries > Part 4 Marketing Practices**

31A-23a-402.5. Inducements.

- (1)
 - (a) Except as provided in Subsection (2), a producer, consultant, or other licensee under this title, or an officer or employee of a licensee, may not induce a person to enter into, continue, or terminate an insurance contract by offering a benefit that is not:
 - (i) specified in the insurance contract; or
 - (ii) directly related to the insurance contract.
 - (b) An insurer may not make or knowingly allow an agreement of insurance that is not clearly expressed in the insurance contract to be issued or renewed.
 - (c) A licensee under this title may not absorb the tax under Section 31A-3-301.
- (2) This section does not apply to a title insurer, an individual title insurance producer, or agency title insurance producer, or an officer or employee of a title insurer, an individual title insurance producer, or an agency title insurance producer.
- (3) Items not prohibited by Subsection (1) include an insurer:
 - (a) reducing premiums because of expense savings;
 - (b) providing to a policyholder or insured one or more incentives, as defined by the commissioner by rule made in accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, to participate in a program or activity designed to reduce claims or claim expenses, including:
 - (i) a premium discount offered to a small or large employer group based on a wellness program if:
 - (A) the premium discount for the employer group does not exceed 20% of the group premium; and
 - (B) the premium discount based on the wellness program is offered uniformly by the insurer to all employer groups in the large or small group market;
 - (ii) a premium discount offered to employees of a small or large employer group in an amount that does not exceed federal limits on wellness program incentives; or
 - (iii) a combination of premium discounts offered to the employer group and the employees of an employer group, based on a wellness program, if:
 - (A) the premium discounts for the employer group comply with Subsection (3)(b)(i); and
 - (B) the premium discounts for the employees of an employer group comply with Subsection (3)(b)(ii); or
 - (c) receiving premiums under an installment payment plan.

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- (4) Items not prohibited by Subsection (1) include a producer, consultant, or other licensee, or an officer or employee of a licensee, either directly or through a third party:
- (a) engaging in a usual kind of social courtesy if receipt of the social courtesy is not conditioned on a quote or the purchase of a particular insurance product;
 - (b) extending credit on a premium to the insured:
 - (i) without interest, for no more than 90 days from the effective date of the insurance contract;
 - (ii) for interest that is not less than the legal rate under Section 15-1-1, on the unpaid balance after the time period described in Subsection (4)(b)(i); and
 - (iii) except that an installment or payroll deduction payment of premiums on an insurance contract issued under an insurer's mass marketing program is not considered an extension of credit for purposes of this Subsection (4)(b);
 - (c) preparing or conducting a survey that:
 - (i) is directly related to an accident and health insurance policy purchased from the licensee; or
 - (ii) is used by the licensee to assess the benefit needs and preferences of insureds, employers, or employees directly related to an insurance product sold by the licensee;
 - (d) providing limited human resource services that are directly related to an insurance product sold by the licensee, including:
 - (i) answering questions directly related to:
 - (A) an employee benefit offering or administration, if the insurance product purchased from the licensee is accident and health insurance or health insurance; and
 - (B) employment practices liability, if the insurance product offered by or purchased from the licensee is property or casualty insurance; and
 - (ii) providing limited human resource compliance training and education directly pertaining to an insurance product purchased from the licensee;
 - (e) providing the following types of information or guidance:
 - (i) providing guidance directly related to compliance with federal and state laws for an insurance product purchased from the licensee;
 - (ii) providing a workshop or seminar addressing an insurance issue that is directly related to an insurance product purchased from the licensee; or
 - (iii) providing information regarding:
 - (A) employee benefit issues;
 - (B) directly related insurance regulatory and legislative updates; or
 - (C) similar education about an insurance product sold by the licensee and how the insurance product interacts with tax law;
 - (f) preparing or providing a form that is directly related to an insurance product purchased from, or offered by, the licensee;
 - (g) preparing or providing documents directly related to a premium only cafeteria plan within the meaning of *Section 125, Internal Revenue Code*, or a flexible spending account, but not providing ongoing administration of a flexible spending account;
 - (h) providing enrollment and billing assistance, including:
 - (i) providing benefit statements or new hire insurance benefits packages; and

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- (II) providing technology services such as an electronic enrollment platform or application system;
 - (I) communicating coverages in writing and in consultation with the insured and employees;
 - (J) providing employee communication materials and notifications directly related to an insurance product purchased from a licensee;
 - (K) providing claims management and resolution to the extent permitted under the licensee's license;
 - (L) providing underwriting or actuarial analysis or services;
 - (M) negotiating with an insurer regarding the placement and pricing of an insurance product;
 - (N) recommending placement and coverage options;
 - (O) providing a health fair or providing assistance or advice on establishing or operating a wellness program, but not providing any payment for or direct operation of the wellness program;
 - (P) providing COBRA and Utah mini-COBRA administration, consultations, and other services directly related to an insurance product purchased from the licensee;
 - (Q) assisting with a summary plan description, including providing a summary plan description wraparound;
 - (R) providing information necessary for the preparation of documents directly related to the Employee Retirement Income Security Act of 1974, 29 U.S.C. Sec. 1001, et seq., as amended;
 - (S) providing information or services directly related to the Health Insurance Portability and Accountability Act of 1996, Pub. L. 104-191, 110 Stat. 1936, as amended, such as services directly related to health care access, portability, and renewability when offered in connection with accident and health insurance sold by a licensee;
 - (T) sending proof of coverage to a third party with a legitimate interest in coverage;
 - (U) providing information in a form approved by the commissioner and directly related to determining whether an insurance product sold by the licensee meets the requirements of a third party contract that requires or references insurance coverage;
 - (V) facilitating risk management services directly related to property and casualty insurance products sold or offered for sale by the licensee, including:
 - (I) risk management;
 - (II) claims and loss control services;
 - (III) risk assessment consulting, including analysis of:
 - (A) employer's job descriptions; or
 - (B) employer's safety procedures or manuals; and
 - (IV) providing information and training on best practices;
 - (W) otherwise providing services that are legitimately part of servicing an insurance product purchased from a licensee; and
 - (X) providing other directly related services approved by the department.
- (5) An inducement prohibited under Subsection (1) includes a producer, consultant, or other licensee, or an officer or employee of a licensee:
- (a)
 - (I) providing a rebate;
 - (II) paying the salary of an employee of a person who purchases an insurance product from the licensee; or

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- (iii) if the licensee is an insurer, or a third party administrator who contracts with an insurer, paying the salary for an onsite staff member to perform an act prohibited under Subsection (5)(b)(xii); or
- (b) except as provided in Subsection (10), engaging in one or more of the following, unless a fee is paid in accordance with Subsection (8):
 - (i) performing background checks of prospective employees;
 - (ii) providing legal services by a person licensed to practice law;
 - (iii) performing drug testing that is directly related to an insurance product purchased from the licensee;
 - (iv) preparing employer or employee handbooks, except that a licensee may:
 - (A) provide information for a medical benefit section of an employee handbook;
 - (B) provide information for the section of an employee handbook directly related to an employment practices liability insurance product purchased from the licensee; or
 - (C) prepare or print an employee benefit enrollment guide;
 - (v) providing job descriptions, postings, and applications for a person;
 - (vi) providing payroll services;
 - (vii) providing performance reviews or performance review training;
 - (viii) providing union advice;
 - (ix) providing accounting services;
 - (x) providing data analysis information technology programs, except as provided in Subsection (4)(h)(ii);
 - (xi) providing administration of health reimbursement accounts or health savings accounts; or
 - (xii) if the licensee is an insurer, or a third party administrator who contracts with an insurer, the insurer issuing an insurance policy that lists in the insurance policy one or more of the following prohibited benefits:
 - (A) performing background checks of prospective employees;
 - (B) providing legal services by a person licensed to practice law;
 - (C) performing drug testing that is directly related to an insurance product purchased from the insurer;
 - (D) preparing employer or employee handbooks;
 - (E) providing job descriptions postings, and applications;
 - (F) providing payroll services;
 - (G) providing performance reviews or performance review training;
 - (H) providing union advice;
 - (I) providing accounting services;
 - (J) providing discrimination testing; or
 - (K) providing data analysis information technology programs.
- (6) A producer, consultant, or other licensee or an officer or employee of a licensee shall itemize and bill separately from any other insurance product or service offered or provided under Subsection (5)(b).
- (7)

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- (a) A de minimis gift or meal not to exceed a fair market value of \$100 for each individual receiving the gift or meal is presumed to be a social courtesy not conditioned on a quote or purchase of a particular insurance product for purposes of Subsection (4)(a).
- (b) Notwithstanding Subsection (4)(a), a de minimis gift or meal not to exceed \$10 may be conditioned on receipt of a quote of a particular insurance product.
- (8) If as provided under Subsection (5)(b) a producer, consultant, or other licensee is paid a fee to provide an item listed in Subsection (5)(b), the licensee shall comply with Subsection 31A-23a-501(2) in charging the fee, except that the fee paid for the item shall equal or exceed the fair market value of the item.
- (9) For purposes of this section, "fair market value" means what a knowledgeable, willing, and unpressured buyer would pay for a product or service to a knowledgeable, willing, and unpressured seller in the open market without any connection to other goods, services, including insurance services, or contracts, including insurance contracts, sold by the producer, consultant, or other licensee, or an officer or employee of the licensee.
- (10) Notwithstanding any other provision of this section, a producer, consultant, or other licensee, or an officer or employee of a licensee, may offer, make available, or provide goods or services, whether or not the goods or services are directly related to an insurance contract, for free or for less than fair market value if:
 - (a) the goods or services are available on the same terms to the general public;
 - (b) receipt of the goods or services is not contingent upon the immediate or future purchase, continuation, or termination of an insurance product or receipt of a quote for an insurance product; and
 - (c) the producer, consultant, or other licensee, or an officer or an employee of a licensee, does not retroactively charge for the goods or services based on an event subsequent to receipt of the goods or services.
- (11)
 - (a) A producer, consultant, or other licensee, or an officer or employee of a licensee, that provides or offers goods or services that are not described in Subsection (3) or (4) for free or less than fair market value shall conspicuously disclose to the recipient before the purchase of insurance, receipt of a quote for insurance, or designation of an agent of record, that receipt of the goods or services is not contingent on the purchase, continuation, or termination of an insurance product or receiving a quote for an insurance product.
 - (b) A producer, consultant, or other licensee, or an officer or employee of the licensee, may comply with this Subsection (11) by an oral or written disclosure.

History

C. 1953, 31A-23a-402.5, enacted by L. 2011, ch. 62, § 5; 2012, ch. 253, § 24; 2012, ch. 279, § 9; 2013, ch. 319, § 29; L. 2014, ch. 290, § 26; L. 2014, ch. 300, § 26; L. 2015, ch. 145, § 1; L. 2015, ch. 244, § 33.

Annotations

Notes

Federal Law.

The Internal Revenue Code, cited in Subsection (4)(g), is Title 26 of the U.S. Code.

The Health Insurance Portability and Accountability Act, cited in Subsection (4)(s), is 42 USCS § 300gg et seq.

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Effective Dates. —

This section takes effect on March 18, 2011.

Amendment Notes.

The 2012 amendment by ch. 253, effective May 8, 2012, added "offered by or" in (4)(d)(i)(B) and added "premium only cafeteria plan within the meaning of Section 125, Internal Revenue Code, or a" in (4)(g).

The 2012 amendment by ch. 279, effective May 8, 2012, substituted "including" for "or" in the introductory language of (3)(b) and added (3)(b)(i) through (3)(b)(iii).

The 2013 amendment, effective May 14, 2013, added "producer, consultant, or other" in the introductory language of (1)(a), (4), and (5) and in (8); in (2), substituted "an individual title insurance producer, or agency title insurance" for "a title" and "an individual title insurance producer, or an agency title insurance" for "or title"; added "a quote or" in (4)(a); substituted "property and casualty" for "the" in the introductory language of (4)(v); added "including analysis of" in the introductory language of (4)(v)(iii); added (4)(v)(iii)(A), (4)(v)(iii)(B), (4)(v)(iv), (6), and (7)(b); deleted "that purchases an employment practices liability insurance product from the licensee" at the end of (5)(b)(v); redesignated former (6) and (7) as (7)(a) and (8); substituted "a quote or" for "the" in (7)(a); updated an internal reference in the introductory language of (5)(b); and made related and stylistic changes.

The 2014 amendment by ch. 290, effective May 13, 2014, added "including providing a summary plan description wraparound" in (4)(q); rewrote (5)(a)(i), which formerly read: "providing a premium or commission rebate"; and deleted "if the de minimis gift or meal is provided by the insurer and not by a producer or consultant" at the end of (7)(b).

The 2014 amendment by ch. 300, effective May 13, 2014, added "including providing a summary plan description wraparound" in (4)(q); deleted "premium or commission" before "rebate" in (5)(a)(i); added "a fair market value of" in (7)(a); deleted "if the de minimis gift or meal is provided by the insurer and not by a producer or consultant" at the end of (7)(b); and added (9).

The 2015 amendment by ch. 145, effective May 30, 2015, added "except as provided in Subsection (10)" in the introductory language of (5)(b) and added (10) and (11).

The 2015 amendment by ch. 244, effective May 12, 2015, substituted "\$100" for "\$25" in (7)(a) and rewrote (9), which formerly read: "For purposes of this section, 'fair market value' is determined on the basis of what an individual insured or policyholder would pay on the open market for that item."

This section has been reconciled by the Office of Legislative Research and General Counsel.

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Attachment 4



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INSURANCE AGENT COMMISSION DEREGULATION: ANTIREBATE LAWS AND AN ALTERNATIVE TO REPEAL

by

Mark Frankel

INTRODUCTION

Every state has an "antirebate" law that prohibits salespersons from offering portions of their commissions to persuade customers to purchase insurance. Recently, antirebate laws have been challenged in the state of Wisconsin by the insurance commissioner, in the states of Florida, Virginia, and California by insurance salespersons, and in the United States Congress by Representative John LaFalce. It is timely, therefore, to examine the history of antirebate laws, the legal significance of antirebate laws, and an alternative to repeal.

Antirebate laws were originally enacted as an antitrust measure to protect smaller insurance companies from insolvency and to protect consumers from exorbitant rates. States have since enacted more pertinent laws such as "legal reserve" regulations to guard against financial instability and rate-setting regulations to control premiums. Nonetheless, antirebate laws play an important, albeit subtle, role for the enforcement of "replacement" laws which discourage the substituting of new policies for existing policies. In the context of federal deregulation of retail pricing and fixed stockbroker commissions, however, most reformers regard antirebate laws as mere price-fixing mechanisms. While it is appealing to support the repeal of laws that prohibit negotiation between buyer and seller, and potentially lower prices, a more complete analysis of antirebate laws reveals their importance for maintaining a stable insurance marketplace.

Consumers, advocates, and lawmakers who are truly concerned about the high cost of insurance should examine savings bank life insurance which features no commissions at all and has proven to be a trustworthy and efficient means of marketing insurance in three states.

HISTORICAL BACKGROUND

The decline of agrarian based communities and the rise of urban industrial society saw people's dependency on their families decline and dependency on the wage system rise. Upon the death of breadwinners there was no longer a farm based support group from which widows and orphans could draw. Fundamentalist notions of gambling soon gave way to concern for protection of widows and orphans and insurance came to be regarded as an "altruistic type of exchange."¹ Between 1865 and 1905, the combined assets of the insurance industry swelled from 150 million to 5 billion dol-

lars.² Expansion of individual companies was bought at any cost, and the result was high pressure sales, deceptive policies, and very high commissions to attract agents.

"Deferred dividend" policies were introduced and were in great demand as they promised larger interest rates on premiums than any other investments of the time. Excessive commissions gave agents a margin of funds they could rebate to reluctant customers to convince them to purchase insurance from the agent's company. A limited parallel in 1983 might be those banks that offer ten dollars to customers to open an Individual Retirement Account. The difference is that insurance rebates often amounted to fifty percent or more of the first year premium for some buyers while other buyers received nothing. The companies structured policies so that many unfortunate policyholders lost their life savings to such "insurance" plans simply for having missed one premium payment. Similarly, many companies offered "industrial" or burial insurance to the working poor which paid almost no dividends and also was susceptible to forfeiture if a premium payment was missed.³

NEW YORK: THE DEVELOPMENT OF MODERN INSURANCE REGULATION

In 1889 New York State enacted the first antirebate statute, and twenty-one states followed by 1895. In addition, thirty companies made an agreement to stop rebates.⁴ The law and the agreement were largely ineffective and high commissions and rebates persisted.⁵ Rebates were necessary in the environment of cutthroat competition and such legal devices as "advisory board contracts" were one of the means created to evade the law.⁶

Public outrage against the insurance industry grew as it had against the railroads and oil companies during the same period. Insurance premiums were a large expense in the depression of the 1890s, and muckrakers indulged the public skepticism by exposing decreasing dividends, shady investments, shady political activity, high living, and nepotism by the captains of the insurance industry.^{7,8}

The New York State Legislature held the Armstrong investigation in 1906 which some historians now describe as "the quintessence of public outrage during the progressive era."⁹ Rebating was prominent among the problems addressed because of its relationship to other concerns such as expenses for new business, keeping agents in line, and destructive competition among companies. Basically, the committee feared for the financial stability of smaller companies because the monopolistic efforts of the larger companies had forced the cost of attracting new business to precarious heights. Antirebate laws were already on the books but they were ineffective, so the following reforms were recommended: (1) limits on amounts of insurance individual companies could sell, (2) fixed commissions based on a percentage of premiums, (3) elimination of bonuses for agents, (4) limits on renewal commissions, and (5) elimination of company loans to agents. The committee concluded:

*The illegal and wasteful practice of rebating
has its source in undue competition and has*

thriven upon the excessive commissions and advances allowed to agents. The limitation upon the amount of new business and the curtailment of the amounts available for expenses in obtaining business, together with the prohibition of discrimination in the amount of compensation paid for different plans of insurance, and of special rewards based upon the aggregates of insurance written will, it is believed, prove an effective remedy for this evil.¹⁰

The investigation produced a "public catharsis"¹¹ which resulted in criminal convictions and the restructuring of the existing insurance law. New York led the country in reform by asserting the state's power to regulate the national activities of any company that sold insurance in New York. To this day, New York plays a prominent part in the sale of insurance across the country because most insurance is sold by companies who sell in New York.¹²

MASSACHUSETTS: THE ORIGIN OF SAVINGS BANK LIFE INSURANCE

The Armstrong committee did not address the unique problems of industrial insurance, but in Massachusetts, Louis Brandeis, as counsel for the New England Policy Holder's Protection Committee, "became the people's advocate in life insurance matters."¹³ The Armstrong investigation had focused primarily on the problems created by deceptive investments which were being paraded as life insurance. For the "wage earner," insurance meant coverage for last expenses, and there were over fifteen million industrial policyholders in 1906. While rebating was not a part of industrial insurance marketing, Brandeis determined that there was "extraordinary wastefulness necessarily attendant upon the present system of supplying life insurance for the common man."¹⁴

The waste in industrial insurance was caused by

- (1) The initial expense on issue of policies taken in connection with the large percentage of policies lapsed.
- (2) The expense of house-to-house collection of weekly premiums.¹⁵

Insurance companies maintained that the discontinuance of premium payments that caused high lapse rates was evidence of "thriftness." Brandeis responded that

... surely the thrifty who persevere should not be compelled to submit to a system which requires such great and largely useless sacrifices in the supposed interest of a small minority.

The thrifty working man, like people of larger means, should have the opportunity of obtaining life insurance at more nearly its necessarily [sic] cost.¹⁶

The Brandeis remedy, savings bank life insurance (SBLI), was authorized in Massachusetts in 1907, in New York in 1938, and in Connecticut in 1942. As the name implies, SBLI is sold only in savings banks. Generally the provisions in an SBLI policy are comparable to those of policies issued by commercial life insurance companies, but there are several important differences. No commissions are charged, a first year dividend is paid, and cash value is available in the first year.

Because SBLI was enacted as an alternative to burial insurance and because insurance companies have successfully asserted their financial interest in limiting the scope of SBLI, restrictions exist on the amount of SBLI consumers can obtain. In Connecticut, the maximum is \$5,000; in New York, the maximum is \$30,000; and in Massachusetts, the maximum is \$43,000. (In Massachusetts, the maximum that can be obtained from any one bank is \$5,000.) Given these low limits, it is no mystery why SBLI sales account for only 2.1 percent of the life market in Connecticut, 2.6 percent in New York, and 7.3 percent in Massachusetts.¹⁷

It will become apparent throughout this article that the problems currently associated with antirebate laws are the same problems that Brandeis associated with industrial insurance marketing. It will also become clear that SBLI is still the most appropriate solution.

LEGAL ANALYSIS

Judicial interpretation of antirebate laws by appellate courts is scarce, perhaps indicating general compliance by agents. Kimball and Jackson maintained in 1960 that some rebating occurs, but it is too discreet to be detected.¹⁸ An informal inquiry by the author of some fifty career life insurance agents and staff managers revealed virtually no knowledge of any rebating activity.

The Supreme Court had an opportunity to rule generally on commissions paid to insurance agents, however, and rebating loomed in the opinion. The court held in an opinion written by Justice Brandeis that a New Jersey statute limiting insurance agents' commissions on a fire policy to a reasonable amount not exceeding that paid other local agents was not void as a denial of due process. Since agents' commissions are a percentage of premiums and since the state may regulate rates, there is a presumption of constitutionality.¹⁹ The decision focused on some of the concerns addressed by the Armstrong investigation—namely, high rates, solvency of insurers, and rate discrimination:

Excessive commissions may result in an unreasonably high rate level or an impairment of the financial stability of the insurer. . . . Moreover, lack of a uniform scale of commissions allowed local agents for the same service may encourage unfair discrimination among policyholders by facilitating the forbidden practice of rebating.²⁰

Concern for high rates and rate discrimination persists as testimony before a House Subcommittee in 1981 revealed. Company insolvency is no longer a significant problem due to the states' enactment of "legal reserve" balance requirements and rate-setting safeguards.

FINANCIAL STABILITY

Several early cases have recognized the importance of antirebate laws for promoting financial stability and competition among companies.²¹ Solvency of insurance companies has been promoted legislatively by both legal reserve regulations and rate-setting regulations. Commissions have been broadly set, as sanctioned by *O'Gorman*, as part of the adjustment of premiums.²² Most states have set specific commission rates ranging from 5 to 25 percent of premiums for property and casualty insurance. New York is the only state to enact explicit maximum commissions for life insurance (55 percent of first year premiums), but there is an extraterritorial impact as New York imposes its insurance law upon the national activities of companies that sell in New York. The remainder of the insurance companies pay commissions of up to 120 percent of the first year premium.²³ By setting limits on commissions, rate-setting regulations diminish the rise of expenses to attract new business that plagued the insurance industry in earlier years.

RATE DISCRIMINATION

Discrimination in insurance law means the unequal treatment of people who are in the same insurance class and have the same life expectancy. In principle, the notion that each should pay according to the risk he or she contributes to the common pool, when applied to the expenses of obtaining new business, implies that each should pay the expenses incurred by the agent and company in selling him a policy. Therefore, if commissions are based on a standard structure and rebates are based on legitimate market forces, there should be no discrimination. The Supreme Court of Maine recognized this in 1891 and held that rebating is not discriminatory provided the base cost of the insurance is not discriminatory.²⁴ More recently, the Supreme Court of Washington has held that rebating is not discriminatory when the reduction in premium on a casualty policy is based on the lower expense of mass marketing.²⁵

Most rebating cases were decided before rate-setting regulations, however, and this may explain why case law has taken a more expansive view of discrimination. Implicitly, courts have incorporated the Armstrong committee finding that rebating caused escalation of commissions and, ultimately, escalation of insurance premiums. Case law has upheld the prohibition of rebating on the grounds that rebating promotes insurance rates that would be too high for too many in order to benefit too few. More specifically, courts have upheld antirebate statutes for the following reasons:

1. Stabilization and standardization of rates.²⁶
2. Elimination of preferential treatment as to the cost of a policy.²⁷
3. Classification and treatment of risks in the same way.²⁸
4. Insuring that inducements to purchase be found in the policy.²⁹
5. Prevention of certain associations from conspiring to get lower rates.³⁰

Most insurance salespersons still maintain a very expansive view of discrimination. The Subcommittee on General Oversight of the Committee on Small Business of the House of Representatives held a hearing on September 21, 1981 to examine the merits of enacting a federal law to end antirebate laws in the states. An agent for Mutual Benefit Life stated that

rebating is discriminatory simply because some policyholders would pay more for their insurance than others:

The life insurance industry has stood for fairness and its keynote has been the same rate to each person of the same qualifications. Mr. Ronald Reagan at 70 would pay exactly the same rate as Mr. Pauper at 70 under the same medical conditions and the same size policy. Rebating destroys that great moral backbone in life insurance.³¹

Rebating would cause some insureds to pay more for the same coverage than others in the same actuarial class, but given state commission regulation; theoretically, no policyholder would pay more than he would without the existence of rebates. Susan Mitchell, Insurance Commissioner of Wisconsin, asserts that insurance law permits discrimination based on the expense of attracting new business and that it is not unfair to allow the sophisticated buyer to earn a price reduction:

In any marketplace, the sophisticated buyer has an advantage over the uninformed buyer. Under insurance law, price discrimination is prohibited when it is not based on the nature and degree of risks or expenses (emphasis added).³²

Indeed, price discrimination has *legislatively* been determined by legislators to be equitable when based on the lower marketing costs of SBLI, group insurance, and mass marketing.

Julius Vogel, senior vice-president and chief actuary of Prudential Insurance Company, when speaking against repeal of antirebate laws, contended that the cost of insurance would be driven up for smaller purchasers of insurance to subsidize rebates for larger purchasers who have the economic leverage to demand and receive a rebate.³³ Vogel predicted that commission rates would be passed along to consumers in the form of increased premiums and decreased dividends.³⁴

Mr. Vogel's employer, Prudential, is regulated by the State of New York and therefore could not raise its commissions without a modification of New York law. Those companies not doing business in New York are regulated by various other state laws, many of which would need revision to protect against abuse. Any federal rebate law passed without consideration of existing state laws would certainly lead to confusion in state legislatures. These governmental bodies would be confronted for the first time in fifty years with the need for changes in archaic and dormant insurance laws.

REPLACEMENT

The most persistent abuse in life insurance sales is replacement of existing policies with new policies. Since commissions are based solely on first year premiums, many salespeople spend much of their careers persuading policyholders to forfeit their old policies and purchase new insurance.

Replacement is frowned upon because insureds lose the lower premium

associated with a purchase at a younger age and because cancellation of an insurance policy means surrender of cash values, dividends, and loan privileges which do not accrue until a policy has been owned for a number of years. New York State requires agents to complete disclosure statements for insureds and the state insurance department whenever a policy is replaced; nonetheless, agents are accomplished at jumping through the hoops the law erects, and replacement is common.

The repeal of antirebate laws could encourage a wave of replacement that could undermine the savings element of whole life insurance.³⁵ By way of illustration, consider an agent who sells a policy issued by a company doing business in New York who earns a commission of about \$275. At the end of the first or second year of policy ownership, most insureds are reluctant to replace life policies because new coverage usually costs a little more due to advanced age and because purchase of a new policy delays receipt of cash values, dividends, and loan values. Reluctance on the part of agents derives from fear of completing disclosure forms, thereby subjecting the transaction to the scrutiny of the state insurance department. If agents could offer insureds a new policy at a slightly higher premium, but with a rebate of half the agents' commission (for example, \$137), it would be in the best interest of the policyholders to replace insurance yearly. Assuming good health, the increased cost, loss of cash values, and loss of dividends would be less than a 25 percent price reduction (i.e., a 25 percent reduction based on a rebate of approximately one half of the agent's 55 percent first year commission).

Given such a scenario, agents would have a reliable yearly clientele, but premiums would rise to keep up with the expense of commissions, and dividends would probably decline. Ultimately it would be impractical for companies to issue policies that are expected to be in force for more than one year or that have a savings element. The ramifications of repeal of antirebate laws for rate discrimination, replacement, and company solvency are not beyond the scope and control of state insurance law, but it would be irresponsible for the federal government to embark on a wholesale repeal without regard for complementary state regulation.

PRICE FIXING

Congressman LaFalce, in introducing his legislation to deregulate insurance agent commissions, characterized antirebate laws as "anti-competitive," and "one of the most costly and enduring price fixing schemes ever perpetrated upon the American public."³⁶ It was seldom mentioned during LaFalce's committee hearings that repeal would bring a return to the cutthroat conditions that existed prior to the passage of antirebate laws, nor was there any concern that monopolization would recur. Apparently concern has shifted from "trust busting" to consumer protection from fixed prices. (It is ironic that laws originally enacted to prevent monopolization are now being labeled anticompetitive).

In recent years, fair trade laws have been repealed, fixed stockbroker commissions have been deregulated, and professionals have been allowed to advertise. Mr. Nader summed up the philosophy of deregulation as follows:

Regulation by governments should not be permitted where there is a good likelihood that competition could replace the rate regulation. . . . It is most definitely the case in insurance services.³⁷

It is argued, based on projections of savings to consumers, that the competition resulting from deregulation (of life insurance commissions) will be so insignificant as to mitigate against restructuring sixty-year-old insurance laws. However, deregulation of securities dealers' commissions has not overwhelmed the industry, and most applaud the results. Discount brokerage firms have offered reductions in commission rates of up to 80 percent but have managed to capture only 10 percent of the market in seven years.³⁸

The opportunities that would arise in insurance are already being realized by agents who circumvent antirebate laws. Gordon Bowers of Discount Insurance Service of Richmond, Virginia testified that

While it is certain that many people still need an agent to sell them on the idea of owning life insurance, it is equally as certain that there is a very large and rapidly growing segment of our population that recognizes life insurance as the economic necessity it is. These people need little or no encouragement to buy the protection they need. Nevertheless, they must buy that protection through the same costly distribution system that was designed to sell insurance to people who would not have bought it otherwise. There is absolutely no conscionable reason for this to continue any longer.³⁹

There is no law anywhere to prevent companies from lowering commissions to agents to meet consumer demands for discount insurance, and such moves by companies could have an effect similar to repeal of antirebate laws.⁴⁰ Bowers asserts, however, that the law should

. . . put the control of negotiations in the hands of the person on the firing line rather than in the manufacturer's hands, which is where it rests today.⁴¹

Few agents share Bower's enthusiasm because it is feared that negotiating commissions would become a costly part of the sales process. The author believes that very few buyers would enter into such negotiation given (1) buyers' reluctance to do comparison shopping for life insurance (and to a lesser degree for property and casualty insurance) and (2) the superior negotiating skill of insurance salespeople. Salespeople have an arsenal of products and persuasions they can offer/use to meet the reluctance of buyers when that reluctance is merely based on a small difference in price. As one salesman testified:

Life insurance is not sold on price. . . . A man does not turn down an offer of a policy because

the rate is \$28.74 but only when the love for himself is greater than the love he professes for others, and he wants to use the money for himself rather than those he professes to love and care about.⁴²

Just as rebates were not part of industrial insurance sales, they are not likely to be offered for life insurance today. Quite simply, price is not a great barrier to sales compared to the prejudice against insurance.

To allow companies to compete while restricting the range of agents' negotiations by antirebate laws is analogous to allowing competition at the wholesale but not the retail level. Such agreements in the sale of consumer goods were banned in 1975 by the Consumer Goods Pricing Act which repealed the "fair trade" laws. Formisano, in evaluating the experience of retailers since the repeal of fair trade laws found that discount merchants have emerged with little emphasis on service, while small retailers have survived by emphasizing personalized service.⁴³ Similarly, Burstein characterizes fixed commissions as "bundling" and advocates an alternative approach which would allow buyers to seek out and purchase only the package of specific services they need. He believes the insurance business should redefine product service and sales to eliminate what he sees as economic inefficiency and impingement of the right of free trade.⁴⁴ Another alternative to fixed commissions examined by Formisano is "net pricing" which allows agents to determine their own compensation based upon costs, the marketplace, and regulatory law.

This article does not dispute that antirebate laws operate as an artificial support for the existing marketing structure. Repeal of antirebate laws, however, will not lower the cost of insurance to the mass of buyers as effectively as explicit limits on commissions do. Lower commissions and repeal of antirebate laws are not mutually exclusive, and one expects that in time reform will occur in the states along these lines. Certainly, the federal government has the authority to preempt the whole area of insurance regulation, but the abuses of present antirebate laws neither call for preemption nor the inevitable creation of a new federal bureaucracy to enforce such preemption. While the purpose of uniformity might be served by federal regulation, uniformity should hardly be a goal of a free market economy.

CONCLUSIONS

1. Repeal of antirebate laws could promote a large increase in replacement of policies and thus produce higher insurance rates and a restriction on the variety of life insurance products sold.
2. Most policyholders are unlikely to benefit from repeal of antirebate laws because most insurance buyers are neither knowledgeable about insurance nor prepared to assume a strong bargaining position relative to insurance agents.
3. An alternative should exist to allow buyers who actively seek out insurance to purchase policies without participating in the present marketing system with its attendant artificial price supports.
4. SBLI is an alternative to repeal:

The sacrifice incident to the present industrial insurance system can be avoided only by providing an institution for insurance which will recognize that its function is not to induce working people to take insurance regardless of whether they really want it or can afford to carry it, but rather supply insurance upon proper terms to those who do want it and can carry it—an institution which will recognize that the best method of increasing the demand for life insurance is not eloquent persuasion, but, as in the case of other necessities of life, is to furnish a good article at a low price.⁴⁵

It is as true today as it was in 1906 that savings bank life insurance is one of the least expensive and most accessible means for marketing low cost insurance. Where rebating would allow a discount from commissions, SBLI eliminates commissions. Where rebating would provide an insurance contract to buyers that does not accumulate any value for at least one year, SBLI policies accumulate cash value and dividends in the first year. Moreover, rebating could give rise to rate discrimination, widespread replacement, and a diminished array of insurance policies for all buyers. SBLI can complement state insurance laws without disrupting their regulatory schemes.

By reaffirming and bolstering the Brandeis way, insurance can approach the ideal of a group of people joining together by contributing to a common fund so that money will be made available upon misfortune to any one of them.

NOTES

¹H. Roger Grant, *Insurance Reform* (Ames, Iowa: Iowa State University, 1979), p. 4.

²*Ibid.*

³*Ibid.*, p. 25.

⁴*Ibid.*, p. 13.

⁵M. Keller, *The Life Insurance Enterprise, 1885-1910* (Cambridge, Massachusetts: Harvard University, 1963), p. 73.

⁶*State Life Insurance Co. v. Strong*, 86 N.W. 825 (Sup. Ct. Mich. 1901); *Citizens Life Ins. Co. v. Commissioner of Insurance*, 87 N.W. 126 (Sup. Ct. Mich. 1901); *McNaughton v. Des Moines Life Ins. Co.*, 122 N.W. 764 (Sup. Ct. Wis. 1909); *Richmond v. Conservative Life Ins. Co. et al.*, 165 N.W. 286 (Sup. Ct. Wis. 1917). Some inducements to purchase, however, are not considered rebates. *Northern Assurance Co. v. Meyer*, 194 N.W. 617 (Sup. Ct. Mich. 1923), held that it was not a rebate to use the "crude and decadent method of lubricating solicitation of business" of buying drinks for the client.

⁷H. Roger Grant, *Insurance Reform*, p. 41.

⁸Public skepticism was reflected in a popular novel of the time entitled the *Light Fingred Gentry* by David Graham Phillips which described the wealth of insurance companies as "stealings from millions of working men and women and children of the poorest most ignorant class" and described an insurance company president as follows:

The fact was that Frosdick, like almost all "captains of industry," was a mere helpless appetite with only the courage of an insane and wholly unscrupulous hunger. But for the lawyers he would not have been able to gratify it. In modern industrialism the lawyer is the honeybird that leads the strong but stupid bear to the forest hive—and the honeybird gets as a reward only what the bear permits.

⁹H. Roger Grant, *Insurance Reform*, p. 38.

¹⁰Hearing Before the Subcommittee on General Oversight of the Committee on Small Business, House of Representatives, Ninety-Seventh Congress, First Session (Washington: U.S. Government Printing Office, 1981), pp. 420-421. Hereafter cited as "Hearing."

¹¹M. Keller, *The Life Insurance Enterprise, 1885-1910*, p. 245.

¹²Efforts to repeal the 1906 New York law enjoyed remarkable success in 1910, but Charles Evans Hughes, chief investigator for the Armstrong investigation, had ridden his popularity to the governorship and he vetoed the resulting legislation. (M. Keller, *The Life Insurance Enterprise, 1885-1910*, p. 260). Mr. Hughes was later to become Associate Justice of the Supreme Court, presidential candidate, and Chief Justice of the Supreme Court.

¹³Alpheus Thomas Mason, *The Brandeis Way* (Princeton, New Jersey: Princeton University, 1938), p. 88.

¹⁴Louis D. Brandeis, "Wage-Earners' Life Insurance," *Collier's, the National Weekly* 37:25 (September 15, 1906), reprinted in Mason, p. 317.

¹⁵*Ibid.*, p. 318.

¹⁶*Ibid.*, p. 321.

¹⁷Hearing, p. 102.

¹⁸Spencer L. Kimball and Bartlett A. Jackson, "The Regulation of Insurance Marketing," *Columbia Law Review* 61 (1961), pp. 141-192.

¹⁹*O'Gorman and Young Inc. v. Hartford Fire Insurance Co.*, 262 U.S. 251 (1931).

²⁰*Ibid.*, p. 257.

²¹*People v. Formosa*, 30 N.E. 492 (C.A.N.Y. 1892); *City of New York Insurance Co., et al. v. Greenwood International Co.*, 155 SO. 346 (Sup. Ct. Miss. 1934); *General Insurance Co. of America v. Earle*, 65 P.2d. 1414 (Sup. Ct. OR. 1937).

²²See, note 19, *supra*.

²³In practice, New York allows generous "expenses" for agents. The real commission paid to agents combining the 55 percent and expenses can amount to as much as 90 percent of the first year premiums.

²⁴*State v. Shwarzchild*, 22 Atl. 164 (1891).

²⁵*Independent Insurance Agents and Brokers of Washington v. Herman*, 486 P.2d. 1068 (1971).

²⁶*Calvin Phillips and Co. v. Fishback*, 146 P. 181 (Wash. 1915); *Leonard v. American Life & Annuity Co.*, 77 S.E. 43 (Sup. Ct. GA. 1913); *In re Brownings Estate*, 22 NYS 652 (1940).

²⁷*Smathers v. Bankers Life Ins. Co.*, 65 SE 746 (Sup. Ct. N.C. 1909); *Bernblum v. Travelers Ins. Co. of Hartford Connecticut*, 105 S.W. 2d. 941 (Sup. Ct. MO. 1937).

²⁸*Hilton v. Commonwealth*, 105 S.W. 956 (Sup. Ct. 1907).

²⁹*Bernblum, Clausen v. New York Life*, 276 N.W. 427 (Sup. Ct. IA. 1937).

³⁰*Lyman v. Ramey*, 242 S.W. 21 (C.A. KY. 1922).

³¹Hearing, p. 93.

³²Ibid., p. 8.

³³Ibid., p. 84.

³⁴Vogel's assumption that smaller policyholders would not enjoy rebates is contradicted by Ralph Nader who envisions "groups of consumers joining together to qualify for discounted group insurance purchase rates" (Hearing, p. 24). Nader's perception is well taken for such price sensitive products as homeowners and automobile insurance, but for life insurance, the idea of groups forming to qualify for lower rates is implausible.

³⁵Most individual policies sold are whole life, and for many, the savings element of these plans is the only savings an insured has and the only means by which he can supplement retirement income or purchase additional insurance as his responsibilities grow.

³⁶*Congressional Record*, September 16, 1981, p. H6321.

³⁷Hearing, p. 21.

³⁸Leslie Wayne, "The Discounters Storm Wall Street," *New York Times*, December 26, 1982, sec. 3., p. 1.

³⁹Hearing, pp. 42-43.

⁴⁰Cases have held that insurance companies can even join together to unilaterally lower commission rates without violating antitrust regulations, *Grecht v. American Insurance Co.*, 344 F. Supp. 1056 (W.D. MO. 1971); *California League of Ind. Ins. Pro. v. Aetna Ins.*, 175 F. Supp. 857 (N.D. CA. 1959).

⁴¹Hearing, p. 50.

⁴²Ibid., pp. 93-94.

⁴³Ibid., p. 73.

⁴⁴Ibid., pp. 34-35.

⁴⁵See, note 14, *supra*, p. 321.

Attachment 5



STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

David A. Paterson
Governor

Eric R. Dinallo
Superintendent

Circular Letter No. 9 (2009)

March 3, 2009

TO: All licensed insurance agents and brokers

RE: Permissible services of insurance agents and brokers; rebating and inducements

STATUTORY REFERENCE: Sections 2324, 2502, 4224, 6409, 6504, and 6904 of the Insurance Law

The purpose of this Circular Letter is to provide guidance and clarification to licensed insurance agents and brokers (collectively, "insurance producers") as to what kinds of services (often referred to as "value-added" services) may be provided to insureds or potential insureds without running afoul of the rebating and inducement provisions set forth in the New York Insurance Law. In response to numerous inquiries regarding these services, the Insurance Department's Office of General Counsel ("OGC") has in recent years issued a number of opinions on the subject. The Department recognizes that the nature of services that an insurance producer may provide in connection with sale or service of insurance continue to evolve, but even in changing conditions, certain underlying principles can guide licensees in their conduct.

There are a number of sections of the Insurance Law that pertain to rebating and inducements, and each has specific applicability to different kinds of insurance or, in the case of Insurance Law § 2502, a specific kind of relationship. Although the language and scope of Insurance Law §§ 2324, 4224, 6409, 6504, and 6904 differ in some respects, collectively those provisions prohibit an authorized insurer, licensed insurance producer, or any person acting on behalf of any such insurer or insurance producer from directly or indirectly paying or offering to pay an insured any rebate from the insurance premium specified in the insurance policy or contract, or giving or offering to give any valuable consideration or inducement, not specified in the insurance policy or contract.¹ Insurance Law § 2502 imposes similar prohibitions against inducements on banks and other specified financial entities, including persons engaged in the business of financing the purchase of real or personal property.

As a general matter, an insurer or insurance producer may not provide or offer to provide an insured or potential insured with any special benefit or discount, including any rebate from the premium, or any service or other incentive in conjunction with the sale of insurance, that is not specified in the policy or contract, or vice versa.² For example, an insurer or insurance producer may not provide "free" insurance or offer to pay part of the insurance premium for an insured or potential insured as an incentive to purchase goods, services or even other insurance. The purpose of New York's rebating and inducement provisions is to require an insurer or licensed insurance producer to provide insurance in a nondiscriminatory manner to like insureds or potential insureds, and to prohibit such an insurer or insurance producer from providing an insured or potential insured with any special benefit not afforded to other insureds or potential insureds. See, e.g., McGee v. Felter, 75 Misc. 349 (Co. Ct. Kings Co. 1912) ("The vice is not in the giving of a rebate, inducement, or consideration, but the giving of any rebate, inducement, or consideration not specified in the policy."). Indeed, the legislative history of Insurance Law §§ 2324 and 4224 shows that the two statutes are intended to reach discrimination, through rebating of any special favor or advantage, between insureds who are equal risks, without specifying the favor or advantage in the policy or contract.

Of course, under the Insurance Law, an insurance broker, but not an insurance agent, may charge an insured a service fee for providing insurance-related services, provided that the broker obtains a written service fee agreement in accordance with Insurance Law § 2119(c). Further, both an insurance broker and an insurance agent may, in accordance with Insurance Law § 2119(a) and (b), charge a fee for insurance consulting services pursuant to a written consulting agreement. However, the fees charged should be reasonable, and like insureds (or potential insureds) should be charged

the same amounts for the same services. See Circular Letter No. 9 (2006) (discussing service fee agreements).

Apart from an arrangement pursuant to Insurance Law § 2119, an insurer or insurance producer may provide a service not specified in the insurance policy or contract to an insured or potential insured without violating the anti-rebating and inducement provisions of the Insurance Law if:

1. the service directly relates to the sale or servicing of the policy or provides general information about insurance or risk reduction³; and
2. the insurer or insurance producer provides the service in a fair and nondiscriminatory manner to like insureds or potential insureds.

The following services generally will fall within the scope of services that an insurance producer may lawfully provide in connection with insurance sold by the producer if provided incidental to the insurance and in a fair and nondiscriminatory manner:

- Risk assessments, including identifying sources of risk and developing strategies for eliminating or limiting those risks;
- Insurance consulting services⁴ or other insurance-related advice;
- Insurance-related regulatory and legislative updates;
- Certain claims assistance services (including the preparation of claims forms), but excluding claims adjustment, unless the exceptions set forth in Insurance Law § 2101(g) are satisfied,⁵
- Tax preparation on behalf of an employer of Schedule A of the Internal Revenue Service Form 5500 Annual Return/Report of Employee Benefit Plan, which requests information regarding insurance contract coverage, fees, and commissions, investment and annuity contracts, and welfare benefit contracts;
- Information to group policy or contract holders and members under group insurance policies currently in place, as well as forms needed for plan administration, enrollment in a plan, insurer website links, and answers to frequently asked questions related to the insurance (including, for example, access through a website, created by the insurance producer, to an employee benefit portal that contains such information);
- Certain services performed pursuant to the federal Consolidated Omnibus Budget Reconciliation Act ("COBRA"), such as billing former employees, collecting the insurance premiums, and forwarding the aggregate premiums to the employer policy or contract holder or to the insurer, when offered in connection with the provision of accident and health insurance; and
- Certain services provided in accordance with the federal Health Insurance Portability and Accountability Act, such as those pertaining to health care access, portability, and renewability, when offered in connection with the provision of accident and health insurance.

However, because they are too attenuated to the provision of insurance, or would otherwise violate the law because the services are not specified in the policy, the following services, if provided by an insurance producer to an insured or prospective insured for "free" or at a reduced fee, or otherwise offered in conjunction with insurance services, could, in the Department's estimation, run afoul of the rebating and inducement provisions set forth in the Insurance Law. Thus, careful consideration should be given to:

- Flexible spending administration services;
- Legal services;
- Payroll services, such as providing employers with check creation and distribution services for their employees;
- Referrals to third-party service providers through which an insured or prospective insured may receive a discounted rate while the producer is the producer of record;
- Advice regarding compliance with federal and state laws concerning human resource issues not relating to the insurance provided;
- Management of employee benefit programs, such as retirement programs and time-off/leave of absence programs, other than the insurance sold by the producer;
- Preparation of employee benefit statements listing all of the benefits provided to employees by the employer that are unrelated to the insurance purchased;

- Development of employee handbooks and training, which are unrelated to the insurance purchased; and
- Services related to employee compensation, discipline, job descriptions, leaves of absence, organizational development, business policies and practices, safety, staffing, and recruiting that are unrelated to the insurance purchased.

Special mention of so-called "wellness programs," too, is warranted. Generally speaking, a wellness program is one designed to promote health and prevent disease, and which provides rewards or incentives for participation. On September 25, 2008, Governor David A. Paterson signed Chapter 592 of the Laws of 2008 into law. Chapter 592 adds a new section to the Insurance Law, § 3239, which is styled "Wellness programs." The statute authorizes an insurer to offer a wellness program in conjunction with a group accident and health insurance policy or group subscriber contract, provided that the program is specified in the policy or contract. The legislation also amends Insurance Law § 4224(c) to expressly exclude a wellness program, as described in Insurance Law § 3239, from the rebating and inducement prohibitions set forth in the Insurance Law, provided that the program is specified in the policy or contract. Chapter 592 confirms the Department's practice of requiring an insurer to specify in an accident and health or life insurance policy or contract any wellness program offered in conjunction with the policy or contract in order to comply with the rebating and inducement provisions of Insurance Law § 4224(c).

Please be advised that the above lists are not exclusive, and are instead intended for illustrative purposes. To be sure, the Department intends, from time to time, to revisit the instant Circular Letter to update the list of services that, based on the Department's interpretation of the governing legal framework, insurance producers may lawfully offer to insureds and prospective insureds.

Please direct any questions regarding this circular letter to Joana Lucashuk, Senior Attorney, at jlucashu@ins.state.ny.us or (212) 480-2125.

Very truly yours,

Paul A. Zuckerman
Assistant Deputy Superintendent and Counsel

¹ Section 2324 applies to most kinds of insurance that § 4224 does not, including most property/casualty insurance; § 4224 applies to life insurance, accident and health insurance, and annuities; § 6409 applies to title insurance; § 6504 applies to mortgage guaranty insurance; and § 6904 applies to financial guaranty insurance. Under Insurance Law §§ 2324 and 6409, the recipient of the rebate or inducement also stands in violation of the law.

² Even if the policy or contract specifies a particular good or service and makes it available to all persons of the same class, the Department still may find the endorsement unacceptable, if the policy or contract and/or the insurer's activities run afoul of any other relevant provisions of the Insurance Law, separate and apart from the rebating and inducement provisions. Thus, in reviewing policy or contract forms, the Department looks to see that the goods or services offered in the policy or contract have a legitimate nexus to the insurance coverage provided under the policy or contract, and are necessarily or properly incidental to the insurer's insurance business. See Insurance Law § 1113(a); see also Insurance Law §§ 1106, 1610, 1714 and 4205.

³ OGC opinions have stated that the service must be a service that the producer "normally performs or arranges." See, e.g., OGC Opinion 07-10-13 (Oct. 31, 2007); OGC Opinion 07-07-17 (July 23, 2007); and OGC Opinion 06-09-14 (Sept. 21, 2006). However, on reflection, this standard implies an inelastic and unadaptable approach to producer activities, which was not the Department's intent.

⁴ Insurance consulting services include "examining, appraising, reviewing or evaluating any insurance policy, bond, annuity or pension or profit-sharing contract, plan or program," as well as "making recommendations or giving advice" with regard to the foregoing. Ins. Law § 2119(a)(1).

⁵ This is one instance where the distinction between an insurance agent and broker is meaningful. Whereas an insurance agent may, under certain circumstances, adjust claims only on behalf of the insurer, a broker may do so only on behalf of the insured.

Exhibit B

STATE OF WASHINGTON
OFFICE OF ADMINISTRATIVE HEARINGS

In the Matter of

YOURPEOPLE, INC. DBA
ZENEFTS FTW INSURANCE SERVICES,

Appellant.

Docket No. 02-2017-INS-00009

YOURPEOPLE, INC. DBA
ZENEFTS FTW INSURANCE SERVICES'
POST-HEARING BRIEF

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<i>Muckleshoot Indian Tribe v. Washington Dep’t of Ecology</i> , 112 Wash. App. 712 (2002).....	6
<i>Port of Seattle v. Pollution Control Hr’gs Bd.</i> , 151 Wash. 2d 568 (2004).....	4
<i>Pub. Water Supply Co. v. DiPasquale</i> , 735 A.2d 378 (Del. 1999)	5
<i>Seatoma Convalescent Ctr. v. Dep’t of Soc. & Health Servs.</i> , 82 Wash. App. 495 (1996).....	4
<i>Sturgeon v. Frost</i> , 136 S.Ct. 1061 (2016).....	6
<i>Wolfe v. Philippine Inv. Co., Inc.</i> , 175 Wash. 165 (1933).....	11
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1	RCW 48.30.140(6)(a)	22
2	RCW 48.30.150	7, 11, 22, 34
3	RCW 48.30.150(3)(a)	22
4	RCW 48.30.157	21, 22
5	WAC 284-17-835.....	22, 23
6	Wash. Rev. Code Ann. § 48.30.140.....	7, 34
7	Washington Administrative Procedure Act	5
8	Other Authorities	
9	Black’s Law Dictionary	20
10	Idaho Dep’t of Ins.,	
11	Bulletin No. 11-03 (2011)	20
12	Illinois Dep’t of Ins., Company	
13	Bulletin No. 2012-11 (2012).....	20
14	Iowa Comm’r of Ins.,	
15	Bulletin No. 08-15 (2008) <i>as amended</i> by Bulletin No. 08-16 (2008)	20
16	Maine Dep’t of Professional & Fin. Regulation, Bureau of Insurance,	
17	Bulletin No. 384 (2012)	20
18	New Jersey Dep’t of Banking & Ins.,	
19	Bulletin No. 11-22 (2011)	20
20	New York Circular Letter No. 9 (2009)	20
21	OFFICE OF INSURANCE COMMISSIONER, PROMOTIONAL GAMES OF CHANCE (2016),	
22	https://www.insurance.wa.gov/promotional-games-chance	23
23	South Carolina Dep’t of Ins.,	
24	Bulletin No. 2009-10 (2009)	20
25	Restatement (Second) of Contracts § 71	7
26	Zenefits, LICENSING (2017),	
27	https://zenefits.com/licenses	4

INTRODUCTION

1
2 The hearing confirmed what the record reflects—the Office of the Insurance
3 Commissioner (“OIC”) has no legal or factual basis to support its order that Washington’s anti-
4 rebating and anti-inducement statutes “prohibit a licensee like Zenefits, acting directly or through
5 affiliates, from offering valuable software functions or other valuable benefits for free or at less
6 than fair market value to the public.”
7

8 The anti-rebating and inducement statutes (collectively “anti-rebating statutes”) require
9 that a benefit have some nexus to insurance to be an illegal rebate or inducement. A free or
10 discounted service cannot be an inducement to insurance where the recipient could obtain the
11 benefit or advantage irrespective of any actual or prospective contractual relationship regarding
12 insurance. It is a matter of plain logic that people do not purchase expensive insurance policies
13 or change brokers to in order to obtain software available to the public that they otherwise can
14 get for free.
15

16 None of the inconsistent and undocumented justifications offered by OIC for the first
17 time at the hearing (thereby necessitating this brief) requires otherwise. To the contrary, OIC’s
18 contorted interpretations: ignore the statutory language; undermine the purpose of these statutes
19 by putting the interests of politically-connected local brokers ahead of consumers who are forced
20 to pay for services available for free in every other state; are contrary to agency precedent; have
21 been rejected by every other state; result in unintended consequences for a host of other
22 licensees; and make for bad public policy that stifles innovation and imposes additional costs on
23 Washington small businesses and non-profits. OIC’s post-hoc justifications, derived with a
24 complete disregard of agency process and procedure, deserve no credence. Instead, the Court
25 should be guided by the contemporaneous legal analyses of OIC’s Legal Affairs Division
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27
28

1 concluding that the offering of non-insurance services for free to the general public without any
2 obligation to purchase, or even consider purchasing, insurance by Zenefits and companies like
3 Zenefits cannot operate as an illegal rebate or inducement as a matter of law and sound public
4 policy.

5
6 **STATEMENT OF UNDISPUTED FACTS**

7 Zenefits offers an online, cloud-based, software-as-a-service platform that integrates the
8 administration of human resources (“HR”), payroll and employee benefits. Zenefits refers to the
9 software functions as applications, or “apps.” Zen. Ex. CR at ¶ 3(a). Zenefits offers the limited
10 set of core HR apps on this platform free of charge to the public. *Id.* Zenefits does not require
11 anyone to become an insurance client, sit for a pitch or demonstration or otherwise entertain an
12 insurance transaction to use the core HR apps, which include tools to manage hiring, onboarding
13 and terminating employees and employee information and to generate, among other things,
14 employee directories, organization charts and payroll reports. Hr’g Tr., Hazard Testimony, June
15 11, 2017 (“Haz. Tr.”); Hr’g Tr., Kalb Testimony, June 13, 2017 (“Kalb Tr.”); Zen. Ex. CR at
16 ¶ 3(b); Zen. Ex. BP. Many Zenefits customers sign up for these apps directly through Zenefits’
17 website, without ever interacting with a salesperson. Haz. Tr.; Kalb Tr.

19 Zenefits also offers certain premium, non-insurance apps for a fee. Consent Order, Zen.
20 Ex. CR at ¶ 3(c). Zenefits offers the non-insurance apps for the same price regardless of whether
21 the customer designates Zenefits as its insurance broker of record. *Id.* Examples of these non-
22 insurance premium features that require a fee include apps for commuter benefits, time-and-
23 attendance tracking and Zenefits payroll. *Id.* Much like the Apple app store, Zenefits also
24 makes non-insurance third party apps available on its platform, providing customers with a
25 broader range of tools for managing HR. *Id.* Zenefits does not charge its users for the
26
27
28

1 integration of the third-party apps. *Id.* Zenefits may or may not receive a commission or fee
2 from the provider of a third-party app for the integration of its app into the Zenefits platform.,
3 much how the Apple app store and other app stores function. *Id.* at ¶ 3(d).

4 Certain insurance-related features centered on insurance enrollment and administration
5 require the customer to designate Zenefits as its broker of record because otherwise Zenefits does
6 not have the ability to access enrollment and other data from insurance carriers. *Id.*; Haz. Tr.
7 Zenefits, like all brokers, collects insurance commissions on the policies it administers. Zen. Ex.
8 CR at ¶ 3(d). The large majority of Zenefits' Washington accounts (over two-thirds) did not
9 designate Zenefits as their broker of record. *Id.* at ¶ 3(e). Indeed, Zenefits derived 79% of its
10 new customer revenue in the first six months of 2017 from non-insurance services. Haz. Tr.

11
12 All Zenefits account holders have access to the same non-insurance services on the same
13 terms and at the same prices as the minority of customers who elect to use Zenefits for insurance
14 services. *Id.* Zenefits offers no extra benefit for purchasing insurance. *Id.*; Attachment 1, Hr'g
15 Tr., Hamje Testimony, June 12, 2017, at 155: 3-5 ("Hamje Tr."). There is no penalty for
16 deciding not to purchase insurance. *Id.*

17
18 Zenefits' customers did not feel any pressure to designate Zenefits as their broker of
19 record and were aware that they did not need to purchase insurance through Zenefits to access
20 the free services. *See* Zen. Exs. BQ at ¶¶ 9, 11; BR at ¶ 9; BS at ¶ 6; BT at ¶ 8; BU at ¶ 6. Small
21 business owner Stefan Kalb and other customers were never solicited to purchase insurance by
22 Zenefits and did not even consider designating Zenefits as broker of record. Kalb Tr.; *see also*
23 Zen. Ex. BU at ¶ 6 (no sales pitch); OIC Ex. 14 at 5 (N. Done confirmed no discussion of
24 "insurance benefit type questions"). Zenefits makes clear in its Terms of Service and
25 prominently on its website that customers are not required to make Zenefits their broker to use
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1 non-insurance services. Zen. Ex. BW at 3; *see also* Hamje Tr. at. 116; 16-20 (“clients are not
2 required to use Zenefits as their insurance broker to receive their other services”); Zenefits,
3 LICENSING (2017), <https://zenefits.com/licenses>.

4 Many of those who did select Zenefits as their broker of record did so because they were
5 unhappy with their existing broker or were paying “huge fees.” Zen. Ex. BQ at ¶ 10; OIC Ex. 14
6 at 26 (Calhoun interview of C. Mills). Zenefits’ apps and software saved its customers time and
7 money and allowed them to run their businesses more efficiently. Zen. Ex. BQ at ¶¶ 6-8; Zen.
8 Ex. BR at ¶¶ 5-7. The Consent Order imposed significant costs and burdens on Washington
9 small businesses like ShelfEngine, Molly’s, Enlearn, C-Labs Corporation, Oasis, Nuun and
10 Company, Inc. and Bonanza, Inc. Kalb Tr.; Zen. Exs. BQ at ¶ 12 (Enlearn); BR at ¶¶ 10-11 (C-
11 Labs); BS at ¶ 9 (Oasis); BT at ¶ 9 (Nuun); BU at ¶ 9 (Bonanza).

12 STANDARD OF REVIEW

13
14 An Administrative Law Judge reviews an agency’s conclusions of law *de novo* on appeal.
15
16 *Len v. Office of the Superintendent of Pub. Instruction*, 188 Wash. App. 1040, *10 & n.14 (July
17 2015) (administrative law judge properly applied *de novo* standard of review); *see also Port of*
18 *Seattle v. Pollution Control Hr’gs Bd.*, 151 Wash. 2d 568 (2004) (noting that “[t]he process of
19 applying the law to the facts . . . is a question of law and is subject to *de novo* review”). Notably,
20 the only authority cited by OIC for the proposition that it is entitled to deference, *Seatoma*
21 *Convalescent Ctr. v. Dep’t of Soc. & Health Servs.*, 82 Wash. App. 495, 518 (1996), held that
22 “question[s] of statutory construction and/or implementation . . . [are] questions of law which we
23 review *de novo*.”(emphasis added).

24
25 Even if it were appropriate in certain circumstances to defer to an agency’s legal
26 interpretation while conducting *de novo* review, deference is inappropriate here because, as
27
28

1 discussed in more detail below, the Consent Order is supported by no legal analysis, the agency
2 departed from its own precedent and it failed to follow its investigation and enforcement
3 protocols. *See Chandler v. OIC*, No. 57853-7-1, 2007 WL 2171365, at *10 (Wash. Ct. App. July
4 30, 2007) (under *de novo* review, arbitrary agency procedures that “disregard the facts and
5 circumstances, and [that] are unreasoned and without consideration” should be rejected); *see also*
6 *City of Redmond v. Central Puget Sound Growth Management Hr’gs Bd.*, 136 Wash. 2d 38, 47
7 (Wa. 1998) (noting that “arbitrary” agency action means “willful and unreasoning action, taken
8 without regard to or consideration of the facts and circumstances surrounding the action”).
9

10 Contrary to OIC’s assertion, a court need not defer to an agency’s interpretation of a
11 statute it administers simply because the agency asserts after the fact that it is “plausible.”
12 Rather, “it is ultimately for the court to determine the purpose and meaning of statutes, even
13 when the court’s interpretation is contrary to that of the agency charged with carrying out the
14 law.” *City of Redmond*, 136 Wash. 2d at 46; *see also Chicago Title Ins. Co. v. Washington State*
15 *Office of Ins. Comm’r*, 178 Wash. 2d 120 (2013) (“[B]oth history and uncontradicted authority
16 make clear that it is emphatically the province and duty of the judiciary branch to say what the
17 law is.”).
18

19 Agency orders must be supported by clear and convincing evidence, with the agency
20 bearing the burden of proof in formal adjudicative proceedings under the Washington
21 Administrative Procedure Act. *Len*, at *4, *10.
22

23 ARGUMENT

24 **I. Washington law does not prohibit licensees like Zenefits from offering non-** 25 **insurance benefits for free to the general public.**

26 OIC’s Consent Order is contrary to Washington law, legislative history, public policy,
27 and OIC precedent. By their plain text, Washington’s anti-rebating statutes do not prohibit
28

1 Zenefits or other licensees from offering free non-insurance benefits on equal terms to the
2 general public. This statutory interpretation is not only consistent with the findings of every
3 other state with similar anti-rebating statutes, it is supported by both OIC's own precedent and
4 the conclusions of its Legal Affairs Division, which three times determined that Zenefits'
5 offering of free HR apps and software does not constitute an illegal rebate or inducement.
6

7 **A. The plain language of the Washington anti-rebating statutes requires a**
8 **nexus to an insurance transaction.**

9 This case turns on the statutory phrases "inducement to insurance," "in connection with
10 any insurance transaction" and "or any other valuable consideration or inducement" and how
11 they are read in the context of the anti-rebating statutes. The Court must not attempt to "glean
12 the meaning of a particular word from that word alone, but rather from the Legislature's intent
13 within the statute as a whole." *Muckleshoot Indian Tribe v. Washington Dep't of Ecology*, 112
14 Wash. App. 712, 720-21 (2002); *see also Sturgeon v. Frost*, 136 S.Ct. 1061, 1070 (2016) ("It is a
15 fundamental canon of statutory construction that the words of a statute must be read in their
16 context . . ." (internal quotation marks omitted)). Washington's anti-rebating statutes provide, in
17 relevant part:
18

19 [N]o insurer, insurance producer, or title insurance agent shall, *as an inducement*
20 *to insurance*, or after insurance has been effected, directly or indirectly, offer,
21 promise, allow, give, set off, or pay to the insured or to any employee of the
22 insured, any rebate, discount, abatement, or reduction of premium, or any part
thereof named in any insurance contract, or any commission thereon, or earnings,
profits, dividends, or other benefit, *or any other valuable consideration or*
inducement whatsoever which is not expressly provided for in the policy.

23 Wash. Rev. Code Ann. § ("RCW") 48.30.140 (emphases added).

24 No insurer, insurance producer, title insurance agent, or other person shall, *as an*
25 *inducement to insurance*, or *in connection with any insurance transaction*,
26 provide in any policy for, or offer, or sell, buy, or offer or promise to buy or give,
or promise, or allow to, or on behalf of, the insured or prospective insured in any
manner whatsoever . . .

- 27 (a) Any shares of stock or other securities . . .
28 (b) Any special advisory board contract, or other contract . . . providing

1 for . . . profits or special returns or special dividends . . .
2 (c) Any prizes, wares, gift cards, gift certificates, or merchandise of an
3 aggregate value in excess of one hundred dollars per person in the
4 aggregate in any consecutive twelve month period.

5 RCW 48.30.150 (emphasis added).

6 Separately or together, the only plausible reading of these statutes is that for a benefit to
7 be an illegal “inducement *to insurance*” or “valuable consideration or inducement” it must have
8 some concrete—more than speculative—connection, or nexus, to an insurance transaction.
9 Defining “inducement to insurance” as broader than consideration offered in exchange for an
10 insurance transaction would render the inclusion of the narrower term “consideration”
11 superfluous.¹

12 Black’s Law Dictionary defines the term “inducement” as the “*benefit or advantage*
13 *which the promisor is to receive from a contract.*” Common sense dictates that a benefit or
14 advantage cannot be an inducement to insurance where the recipient could obtain the benefit or
15 advantage irrespective of any insurance transaction. This does not mean, as OIC attributes to
16 Zenefits, that a contract of insurance must result from the offered benefit or advantage, but it
17 does mean there must be some nexus to an insurance transaction. Where the benefit or
18 advantage is available on equal terms, without condition, to insureds and non-insureds alike, it is
19 not a “benefit or advantage which the promisor is to receive from a contract” and, thus, is not an
20 “inducement to insurance.”

21 The Louisiana Department of Insurance analyzed a virtually identical statute² and
22 concluded that “*where a thing of value is offered on equal terms to the general public . . . it*

23
24 ¹ See Restatement (Second) of Contracts § 71 (consideration “must be bargained for” and provided
25 “in exchange” for the parties’ agreement).

26 ² Louisiana’s statute, like Washington’s, centers on the phrases “as inducement to such insurance . . .
27 . or any valuable consideration or inducement whatsoever” and “as inducement to insurance or annuity or
28 in connection therewith.” Zen. Ex. BX at 5-6.

1 cannot be reasonably asserted that the thing of value served as valuable consideration or
2 inducement to the contract because its recipient could obtain the thing of value irrespective of
3 any contractual relationship regarding insurance.” Zen. Ex. BX at 6 (emphasis added). In
4 assessing the meaning and placement of the terms “inducement” and “consideration” in the
5 context of these statutes, and in particular the significance of the term “or,” the Department
6 reasoned:

7
8 “[C]onsideration” in a bargain is the exchange of price by a promisor for his
9 promise. Consideration in a bargained for exchange is generally necessary for the
10 creation of a contract. . . . [W]here there is no contractual relationship in which
11 a regulated entity gives a thing of value to another person or entity, there is no
12 “valuable consideration or inducement” furnished by the regulated person or
13 entity. *Although the word “inducement” can have a broader meaning, it cannot
14 be easily maintained that the word “inducement” means any and therefore every
15 motivation that a person may have.*

16
17 Otherwise, the statute would be so broad as to encompass any motive not
18 recounted in the contract of insurance as a rebate. In construing the statute in
19 conformity with its general purpose as far as the words fairly permit, we therefore
20 advise that *the word “inducement” is synonymous with the word
21 “consideration”* and is the reason why the word “or” is interposed between the
22 two, meaning that the consideration *is* the inducement in a bargained for
23 exchange. It is not out of the ordinary in construing a statute to give a word a
24 more precise meaning based on the neighboring words in the statute. Equating
25 “consideration” with “inducement” is not undermined by the general reluctance to
26 interpret statutes in a way that leads to surplus terminology. Surplus terminology
27 sometimes results from “a perhaps regrettable but not uncommon sort of lawyerly
28 iteration (“give, grant, bargain, sell, and convey”). But the cannon against
surplusage merely favors that interpretation which avoids surplusage. It is not
intended to require that a statute pursue its purposes at all costs. *Therefore, La.
R.S. 22: 1964(8) should not be interpreted as prohibiting a person engaging in
the business of insurance from giving things of value outside of a contractual
arrangement where there is no insurance contract or relationship.* Such a broad
interpretation would result in prohibiting common and ordinary business activities
where such prohibition bears no reasonable relation to the evils sought to be cured
by the Unfair Trade Practices Act.

The same result necessarily follows in situations where a person engaged in the

1 business of insurance gives a thing of value to a person with whom he has a
2 contractual relationship, provided that the thing of value is offered on equal terms
to the general public.

3 *Id.* at 5-6 (emphases added).

4 The conclusion that an “inducement to insurance” must involve an actual or contemplated
5 exchange (i.e., consideration) intended to result in an insurance transaction is also supported by
6 the Washington legislature’s use of very specific, insurance transaction-related terms in
7 describing the types of prohibited inducements and rebates in other portions of the statutes. For
8 example, Section 140 identifies a list of illegal rebates (“rebate, discount, abatement, or
9 reduction of premium, or any part thereof named in any insurance contract, or any commission
10 thereon, or earnings, profits; dividends”), all of which would naturally arise out of an insurance
11 transaction.
12

13 Likewise, Zenefits’ free apps and services are not offered “in connection with” an
14 insurance transaction. Washington law defines an insurance transaction as the sale, solicitation
15 or negotiation of insurance. RCW 48.01.060. The offering of free non-insurance services with
16 no obligation to purchase insurance, sit for a pitch or demonstration, or even consider the
17 purchase of insurance has *no connection with* the solicitation or negotiation of insurance.³ The
18 evidence in this case confirms that no person could be “induced to purchase insurance” by a
19 benefit available to the general public that she could receive without purchasing insurance. It is
20 undisputed that the large majority of Zenefits customers do not designate Zenefits as a broker of
21
22

23 ³ To the extent OIC argues that *anything* provided to an insured constitutes a rebate because the
24 clause “or after insurance has been effected” in Section 140 does not include the word “inducement,” this
25 theory also fails. This clause is clearly qualified by the language at the end of Section 140 “or any other
26 valuable consideration or inducement”, which establishes that a benefit either offered in contemplation
27 with an insurance transaction or following an insurance transaction must be “valuable consideration or
28 inducement.” This argument also makes no sense, as it would result in certain benefits being legal prior
to the consummation of an insurance transaction but illegal after the transaction.

1 record. As Stefan Kalb testified, customers are not required to sit through an insurance pitch or
2 be solicited for insurance services; in fact, they can sign up for accounts on Zenefits' website
3 without even speaking to a salesperson. Zenefits customers confirm, and OIC concedes, there is
4 no obligation to designate Zenefits as broker of record in order to access either its free or paid
5 non-insurance apps and services. The minority of customers that did elect to use Zenefits for
6 insurance services did so for a variety of reasons unrelated to Zenefits' free apps and services,
7 including dissatisfaction with existing brokers and the fees charged by their existing brokers. In
8 sum, the only reasonable interpretation of the anti-rebating statutes is the one adopted by
9 Louisiana, and as shown below, every other state to consider similar statutes and OIC's Legal
10 Affairs Division, that a benefit provided by an insurance producer that remains available on the
11 same terms to insurance and non-insurance customers alike regardless of whether the customer
12 buys an insurance policy cannot constitute an "inducement to insurance" (the "common
13 interpretation").
14
15

16 **B. The common interpretation is supported by the legislative history.**

17 As discussed in detail in Zenefits' Hearing Brief, the anti-rebating statutes were intended
18 to protect *consumers* from discriminatory pricing and to preserve insurer solvency, not to protect
19 *producers* from competition and stifle competition and innovation at the expense of
20 consumers.⁴ See, e.g., *Wolfe v. Philippine Inv. Co., Inc.*, 175 Wash. 165, 168 (1933) ("The
21 purpose of [the anti-rebating] statute was to establish uniform insurance rates throughout the
22 state and to maintain a standard of such rates."); see also Zen. Hr'g Br. at 18 (collecting
23 cases). Nothing in the history of these statutes, any court opinion, or regulatory guidance
24

25 _____
26 ⁴ As discussed in more detail below, OIC's reliance on a 21-year old letter written by an out-of-
27 state Attorney General for an entirely different purpose does not establish otherwise.
28

1 suggests that Zenefits and other innovative companies should be prohibited from providing free
2 HR or other services to the general public, on equal terms to insured and non-insured alike.

3 **C. OIC's own legal department agreed with the common interpretation.**

4 On at least three different occasions, OIC's Legal Affairs Division agreed with the
5 common interpretation.

- 6 • In June 2014, OIC Investigations Manager Mark Durphy, in consultation with the
7 OIC Legal Affairs department, concluded that Zenefits was not in violation
8 because it was "not offering anything for free to a client *in exchange for them*
9 *being their broker.*" Zen. Ex. F (emphasis added).
- 10 • Following a meeting with Zenefits and its counsel in the fall of 2014 to learn
11 more about the Zenefits platform and services, Deputy Commissioner for Legal
12 Affairs AnnaLisa Gellermann, Commissioner Kreidler and Chief Deputy Jim
13 Odiorne "concluded because the software is provided free to all consumers,
14 regardless of the decision to purchase insurance, it did not constitute an
15 inducement." Zen. Ex. I.
- 16 • In her detailed legal analysis of January 9, 2015, Staff Attorney Marcia Stickler
17 concluded that RCW 48.30.150 "requires that a prohibited inducement have *some*
18 *connection with an insurance transaction* or otherwise be an inducement, *or*
19 *incentive*, to the purchase of insurance" and that there was no such "connection"
20 or "incentive" here because the free services are available to the general public
21 and "those who buy insurance through Zenefits get no special reward or
22 privilege." Zen. Ex. T at 1.

23 Notably, Stickler's 2015 analysis requiring a nexus to an insurance transaction is consistent with
24 long-standing OIC legal interpretation of the anti-rebating statutes. In a 2008 legal analysis of
25 sweepstakes programs offered by insurers, OIC focused on the issue of nexus, concluding that
26 "the *nexus* between a consumer entering a sweepstakes and experiencing a specific solicitation to
27 insurance or being asked/persuaded to apply for or purchase a contract of insurance is
28 questionable." Zen. Ex. D at 1, 5 (emphasis added).

The record reflects, and OIC concedes, that these are the *only* legal analyses of the anti-
rebating statutes, or their application to Zenefits, generated in the course of OIC's two-year

1 investigation of Zenefits. *See, e.g.*, Hamje Tr. at 94: 18-25, 95: 1-24, 96: 2-22, 102: 1-12., To
 2 this day, OIC cannot—or will not—explain why it ultimately rejected these analyses and took
 3 the unprecedented step of ignoring the advice of and transferring this case out of its legal
 4 department, which Hamje acknowledged has responsibility for “legal interpretation of the
 5 insurance code.” Hamje Tr. at 111: 1-22, 166: 3-8, 169: 8-13, 170: 1-25, 171: 1-7; Zen Ex. CT.
 6 Nor can it point to any document that reflects the contrary theories offered at the hearing. Hamje
 7 Tr. at 95: 18-25, 96:1-24, 97:2-22, 98:7-18. Instead, OIC relies exclusively on the testimony of
 8 the *former* Deputy for Consumer Protection who has not held a legal role since 2005, conceded
 9 that he was not authorized to speak on behalf of the agency, did not discuss his testimony with
 10 Commissioner Kriedler or Gellermann to confirm it reflected the agency’s views, and could not
 11 explain why he “disregarded” Stickler’s memo. *See* Hamje Tr. at 104: 6-16, 105: 11-17; 158:
 12 21-25, 159: 1-8; 166: 3-8, 169: 6-8.

13
 14
 15 **D. All other states with similar statutes agree with the OIC Legal Affairs’s interpretation.**

16 Washington’s anti-rebating statutes are not unique. Like the majority of states,
 17 Washington’s statutes are substantially similar to the National Association of Insurance
 18 Commissioners’ Model Law. Every other state to interpret virtually identical statutory language
 19 has concluded, consistent with OIC’s Legal Affairs Division, that a benefit must have some
 20 nexus to an insurance transaction and that benefits offered on equal terms to the general public
 21 do not constitute illegal inducements or rebates.

State	Statutory Language	Agency Conclusion
<i>Analyzing Zenefits’ Business Model</i>		
Maryland	Prohibits “any valuable consideration or other inducement” as “an inducement to the insurance.”	No violation because “[a]ccess to the Zenefits platform is free to anyone without obligation to purchase insurance and the <i>free access is provided on equal terms to the</i>

1		Zen. Ex. CI.	<i>general public.</i> ” Zen. Ex. AW at 2 (emphasis added).
2	Montana	Prohibits offering “any valuable consideration or inducement whatsoever” as “inducement to such insurance.” Zen. Ex. CK.	Zenefits’ software “does not induce a person to purchase insurance through Zenefits” because “[t]he <i>software can be used free with or without the purchase of insurance policies</i> through Zenefits.” Zen. Ex. AG at 1-2 (emphasis added).
3			
4			
5	North Carolina	Prohibits “as an inducement to insurance, or after insurance has been effected . . . any valuable consideration or inducement whatever” Zen. Ex. CM.	“[T]here is <i>no exchange</i> by Zenefits for access to its free software in return for representing consumers as its insurance broker. [T]here is no exchange for free services for purchase of an insurance contract. While consumers receive access to Zenefits’ services, this <i>access is not contingent upon</i> completing an insurance application or entering into an insurance contract. On its website, it specifically states that ‘to enjoy the benefits of the Zenefits.com platform, you are not required to use us as its broker.’” Zen. Ex. Y at 3 (emphasis added).
6			
7			
8			
9			
10	<i>Analyzing Anti-Rebating Statutes More Broadly</i>		
11	Kansas	Prohibits offering “any valuable consideration or inducement whatever” as “inducement to such insurance contract or annuity or in connection therewith.” Zen. Ex. CG.	“[T]he <i>key</i> is whether the company has provided or arranged for or an insured has received any special favor or advantage that is <i>not generally available to others.</i> ” Zen. Ex. A at 2 (emphasis added).
12			
13			
14			
15	New York	Prohibits “any valuable consideration whatever” as “an inducement to any person to insure.” Zen. Ex. CN.	Offering a free wellness program to customers does not create “an unlawful inducement” “as long as access to the wellness program’s free services is <i>not contingent upon the purchase</i> of insurance policies sold by the broker <i>or the solicitation</i> thereof by either the broker or the wellness program provider, or limited to the broker’s clients.” Zen. Ex. C (emphasis added).
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19	Tennessee	Prohibits “any valuable consideration or inducement” as “an inducement to the policy.” Zen. Ex. CP.	“[G]ifts and valuable consideration offered to potential customers <i>irrespective of whether they purchase a policy</i> . . . will not be considered an inducement to a policy in violation of the rebating statute.” Zen. Ex V. (emphasis added).
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23 Michigan, Arizona, Indiana, Connecticut, and Rhode Island have reached similar

24 conclusions. *See* Zen. Exs. E, P, S, R, Z. No regulator applying similar statutes patterned after

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1 the Model Law—other than OIC—has found otherwise.⁵ Hamje “rejected” all of these opinions
2 without even reading most of them, asserting that it was not “appropriate” to research the views
3 of other states, despite his acknowledgment of the value of consistency across state lines. Hamje
4 Tr. at 160: 2-6, 161: 8-25, 162: 1-15. Interestingly, Hamje had no similar concern when he asked
5 lobbyists for competing brokers what they were hearing from other states. Zen. Ex. AH; Hamje
6 Tr. at 180: 5-25, 181: 1-3 (“if there was information that other state departments were taking
7 action on, I wanted to hear about it [from the Big I] and share it with people internally”).
8

9 **E. This common interpretation is consistent with OIC precedent.**

10 The universally accepted conclusion that free services offered to the general public
11 without condition do not violate the anti-rebating statutes is also consistent with OIC’s
12 precedent. OIC’s exhaustive list of other anti-rebating enforcement actions reveals that the
13 agency only takes action when there is a connection between a benefit and an insurance
14 transaction, and that never before has OIC brought an enforcement action against a broker
15 providing a benefit to the general public with no strings attached. Every case relied on by OIC
16 involved garden variety rebating schemes where a customer was required either to purchase
17 insurance or to receive a quote or sales pitch in exchange for receiving the benefit. Zen. Ex. Q.
18 For example, with respect to the matters cited at the hearing by Hamje:
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21 ⁵ As discussed in the prehearing brief, Sticker’s memo contrasted Washington’s statute with Utah’s
22 anti-inducement statute. Although Utah originally concluded the Zenefits platform violated its anti-
23 inducement law, the statute at issue there, as Stickler noted, was “very different” from those of
24 Washington and other states. Zen. Ex. T. Utah’s law specifically prohibited “insurer[s] [or] third party
25 administrator[s] who contract[] with an insurer” from providing non-insurance services such as “payroll
26 services . . . performance reviews . . . accounting services” or other HR services unless the insurer pays a
27 fee “that shall equal or exceed the fair market value of the item.” Utah Code Ann. § 31A-23a-
28 402.5(5)(b), (8), (9) (2014) (repealed 2015); *see also* Zen. Ex. CL. Shortly after the Utah Department of
Insurance found Zenefits in violation, the state legislature amended the anti-inducement statute to
expressly permit producers to offer free services offered on the same terms to all with no obligation to
purchase insurance. *See* Utah Code Ann. § 31A-23a-402.5 (2015).

- 1 • Bruce Longemier required offered \$100 gift cards in exchange for meetings and Danny
2 Harlow required attendance at an insurance seminar. Zen. Ex. Q at 3.
- 3 • Potter Insurance, iCan, Keith Coe, Thomas Davis and John Clayton were giving cash,
4 raffle tickets, discount cards or referral fees to insurance customers in exchange for
5 business and referrals. Zen. Ex. Q at 3-4.

6 Each of these classic forms of rebating involves cash or cash equivalent gifts and have a
7 clear nexus to an insurance transaction. None is remotely analogous to the situation presented
8 here, which even Hamje acknowledged was “not an ordinary case.” Hamje Tr. at 210: 12-14.
9 As established by Hazard, Kalb and the Consent Order itself, Zenefits offers its free HR apps and
10 software to the general public with no strings attached; insurance customers receive no extra
11 benefits for signing up for insurance; and customers are not required to sit through insurance
12 pitches or even interact with sales staff in order to use the free apps and services. As Kalb
13 testified, small businesses can create an account and access free HR services without a platform
14 demonstration, insurance pitch, phone calls or email solicitation. Indeed, it never crossed Kalb’s
15 mind to purchase or inquire about insurance.

16 Even where there is a clear link between a benefit and an insurance transaction, OIC has
17 declined to take action when doing so would harm consumers. This is best exemplified by the
18 agency’s handling of Blue Cross Blue Shield’s offering of free identity protection services. In
19 September 2015, Gellermann and OIC Senior Enforcement Specialist Charles Brown both
20 concluded that “[i]t doesn’t make any sense . . . from a consumer protection or regulatory
21 standpoint to tell [BCBS] they cannot offer subscribers identity theft protection services” and
22 agreed that BCBS’s offering did not “raise[] the problem that the rebate and inducement statutes
23 were intended to prevent.” Zen. Exs. AM; AN. They reached this conclusion even though
24 BCBS—in stark contrast to Zenefits—offered free identity theft protection services *only to its*
25 *insureds* and only “*after insurance has been effected.*” *Id.* Hamje’s testimony speaks for itself:
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1 PETER WALSH: How do you reconcile, Mr. Hamje, a decision not to take action against
2 an entity that's providing free identity theft protection services only to its insureds with
3 the decision to find Zenefits in violation for providing free benefits to the general public
4 without condition?

5 JOHN HAMJE: I can't.

6 Hamje Tr. at 234: 14-22.

7 In sum, the statutory language, legislative history, prior agency precedent and
8 conclusions of every other state confirm that the anti-rebating statutes do not prohibit Zenefits or
9 other licensees from offering non-insurance benefits to the general public because there must be
10 a connection, or nexus, between an offered benefit and an insurance transaction.

11 **II. OIC's shifting, inconsistent interpretations and theories fall flat.**

12 OIC has offered a variety of different and inconsistent interpretations of the anti-rebating
13 laws unsupported by any legal authority whatsoever. At the hearing, Hamje posited that a
14 licensee violates the statute whenever it offers anything of value over the statutory maximum to
15 anyone. ("Hamje's *per se* test"). In other instances, OIC has taken the position that the
16 applicability of the anti-rebating statutes depends on whether a licensee is "primarily" an
17 insurance broker. OIC's counsel argued that the court should apply a "convenience test"—
18 contending that anything offered that enhances convenience for potential insurance customers
19 violates the anti-rebating statutes. And, OIC obliquely suggested at the hearing that the benefit
20 administration services that Zenefits provides insureds through its benefits apps to help manage
21 their benefit plans—the digital equivalent of what conventional brokers have always provided
22 their customers in paper form—might be an illegal rebate. Finally, OIC contended in its Hearing
23 Brief that the common interpretation of every other state and its own legal department would
24 render certain statutes and regulations "unnecessary and superfluous." These various theories—
25 many of which were offered up for the first time at the hearing by Hamje—not only lack any
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1 legal support, they also illustrate the complete failure of process and absence of a clear and
2 consistent application of the law that has characterized OIC's investigation of Zenefits since it
3 was removed from Legal Affairs and handed over to Hamje and underscore why OIC's Consent
4 Order is entitled to no deference.

5 **A. Hamje's *per se* test has no legal precedent or basis in text or policy.**

6 Hamje argued at the hearing that the anti-rebating statutes impose an objective *per se*
7 test—an entity is in violation of the statutes if it: (1) is a licensee; and (2) gives any free or
8 discounted goods or services to the general public, regardless of any relationship to a potential
9 insurance transaction. Hamje Tr. at 238: 8-25. Neither Hamje nor OIC, however, can point to
10 any legal authority for this expansive reading of the statute which, as discussed above, is
11 inconsistent with the statutory language, the legislative history, and OIC precedent, and, like the
12 other theories offered, has never been memorialized by the agency in any form. See Hamje Tr. at
13 95: 18-25, 96: 1-25, 97: 1-22, 99: 13-25, 106: 1-11, 109: 7-18. Hamje's formulation writes out
14 of the statute the key language "to insurance," "in connection with an insurance transaction" and
15 "or any other valuable consideration or inducement." If that is what the Washington legislature
16 intended, the statute would simply read "no insurance producer shall provide or offer anything of
17 value to anyone in excess of one hundred dollars."
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20 **B. OIC's "primarily an insurance broker" test fails.**

21 In attempting to distinguish Zenefits from other integrated companies like banks or
22 Expedia, OIC has also suggested that the anti-rebating statutes apply only to companies that are
23 "primarily" insurance brokers. When explaining why he believed Zenefits was in violation,
24 Hamje emphasized (without any factual basis for doing so) that Zenefits "makes no bones about
25 making money from selling insurance . . . they make their money from selling insurance."
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1 Hamje Tr. at 48: 4-9, 108: 1-5. OIC also offered this theory to State Senator Joe Fain, when
2 Senator Fain asked why OIC's Consent Order would not apply to other companies like Zenefits
3 such as banks or Expedia. In a February 10, 2017 email, OIC Legislative Director Lonnie Johns-
4 Brown, replying on information "provided by staff here at OIC," wrote:

5
6 It is important to understand that *online travel companies, such as Expedia, and*
7 *banks offer insurance as a sideline to their primary businesses* while Zenefits gets
8 at least 80% of its income from insurance sales. . . . *Zenefits, however, makes*
9 *clear in its advertising that it makes its money from selling insurance, not from*
10 *providing the free online services. It is in the insurance business not the payroll,*
11 *human resources etc. business. . . . Zenefits developed the platform and provides*
12 *the bulk of the services offered without charge, for the purpose of selling*
13 *insurance. . . ."*

14 Zen. Ex. CQ at 2 (emphasis added).

15 Putting aside the fact that many of the factual assertions in Johns-Brown's statement to
16 Senator Fain are contradicted by the undisputed evidence, the agency's suggestion that the anti-
17 rebating laws distinguish between licensees based on their source of revenue or the nature of
18 their business is untenable.⁶ The anti-rebating statutes apply to all licensees. Even if OIC did
19 have the authority to make this distinction and apply a revenue test, its application would be the
20 embodiment of arbitrary. At what point is a licensee no longer "primarily" an insurance broker?
21 When commissions constitute only 49% of its revenue? Does the law no longer apply to
22 Zenefits because, as Hazard testified and OIC does not contest, 79% of its 2017 new customer
23 revenue is derived from non-insurance services? In sum, this is an arbitrary distinction, justified
24 by no legal authority and seemingly applied for the first time in this case.

25
26 ⁶ Johns-Brown's email to Senator Fain was based entirely on information provided to her by
27 Hamje. See Zen. Ex. CQ.

1 **C. “Convenience” is not an inducement.**

2 In its closing argument, OIC suggested yet another test, arguing that a violation would
3 occur if the “convenience” of Zenefits’ platform had “the effect of” or “caused” customers to
4 designate Zenefits as their broker of record—in essence rendering anything a broker does to
5 make their customers lives more convenient a rebate. In doing so, OIC failed to acknowledge
6 the irony of a consumer protection agency asserting that consumer “convenience” cannot be
7 tolerated. Regardless, the convenience that results from offering quality products and services in
8 an easily accessible manner has no nexus to an insurance transaction and is not an “inducement
9 to insurance.” This standard ignores the rest of the language in Sections 140 and 150, including
10 the phrase “in connection with any insurance transaction” which would be rendered meaningless,
11 and results in interpretation so broad it would encompass virtually everything offered by
12 licensees. As with Hamje’s *per se* test, if this had been the legislature’s intent, it would have
13 drafted the statute to read “no insurance producer shall provide or offer anything in excess of
14 \$100 that might cause the purchase of insurance, including making the lives of its customers
15 more convenient through better service.”
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18 Notably, OIC’s legal department rejected the concept that the “convenience” of the
19 platform could constitute an inducement, labeling it instead a public good to be promoted. Zen.
20 Ex. T at 3 (“Public policy considerations should permit this activity as consumers are *benefited*
21 *by convenience and ease of use for employee benefit management* unrelated to the purchase or
22 solicitation of insurance.”). The Montana Department of Insurance similarly rejected this
23 “convenience” test, acknowledging that “[w]hile there may be some ease to using broker services
24 provided by Zenefits,” the critical question is whether using Zenefits for broker services “is
25 required” to access the free apps. Zen. Ex. AG at 2. Even if this were the appropriate legal
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1 standard, the factual predicate for OIC's causation theory is undermined by the fact that more
2 than two-thirds of Zenefits customers do not use Zenefits for insurance services.

3 **D. Benefits administration services are not an inducement or a rebate.**

4 OIC also appeared to suggest at the hearing, for the first time and without any detail or
5 explanation, that the benefits administration apps offered by Zenefits to help insurance customers
6 manage and administer their insurance policies somehow constitutes an illegal rebate.

7
8 It is beyond debate that a broker may offer without separate charge brokerage services
9 that are incidental to the administration of an insurance policy, such as helping explain and fill
10 out enrollment forms. The proposition that insurance brokers are allowed to provide benefits
11 support services to their insurance customers is so uncontroversial that many states, including
12 Washington, have not even addressed it. Every state that *has* issued guidance on this subject,
13 however, has confirmed the obvious—producers may provide benefits administration services
14 that are not specified in the insurance policy to their insureds. *See e.g.*, Iowa Comm'r of
15 Insurance, Bulletin No. 08-15 (2008) *as amended by* Bulletin No. 08-16 (2008) (“[V]alue-added
16 services if they are related to the type of insurance purchase or are intended to reduce claims are
17 not considered rebates”).⁷

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20 ⁷ *See also* Maine Dep't of Professional & Fin. Regulation, Bureau of Insurance, Bulletin No. 384
21 (2012) (observing that “it is not possible to list all possible variations,” but the following do not constitute
22 rebates: “[t]echnological enhancements such as computer programs that aid in the efficient administration
23 of the insurance program provided through the producer” and “[s]ystem improvements, which could
24 include software provided to employers, that make information about group benefits provided through the
25 producer more accessible...”); Louisiana Advisory Letter 2015-01, Zen. Ex. BX at 3 (“Any person
26 engaging in the business of insurance may offer certain services to insureds without charge and that do
27 not constitute rebating . . . when the services are incidental to the policy of insurance and are offered to all
28 insureds.”); New York Circular Letter No. 9 (2009) (“[I]nsurance producer[s] may provide a service not
specified in the insurance policy or contract to an insured or potential insured without violating the anti-
rebating and inducement [laws] if: (1) the service directly relates to the sale or servicing of the policy or
provides general information about insurance or risk reduction; and (2) the insurer or insurance producer
provides the service in a fair and nondiscriminatory manner to like insureds.”); Illinois Dep't of Ins.,

1 Washington brokers commonly offer a variety of benefits administration services for free
2 to their insurance customers, including online tools and reporting. For example, Sprague Israel
3 Giles Insurance offers “benefits helpline[s]”, “educational seminars” and a “complete benefits
4 website.” See <http://www.siginsures.com>. PSG Washington provides “updates on changing
5 government regulations,” “reviews programs for results and cost-effectiveness”, and makes
6 available “secure 24/7 online access to employee benefits information, claim forms and provider
7 services.” See <http://www.psgwa.com/>. Rice Insurance, LLC offers a “client portal” with an
8 “online service center” with “tools” for processing payments, claims, and insurance certificate
9 requests. See <https://www.riceinsurance.com/service/>. Brokerage firm MCM provides its
10 insurance customers with “complete, turnkey employee benefit consulting services” including:
11 “selection, design and planning for the full range of health & welfare benefit plans;”
12 “development of comprehensive RFPs that identify the best benefit vendor partners;” “vendor
13 negotiation to obtain the best possible pricing;” “implementation and ongoing plan
14 management;” “responsive communications support;” benefit “plan financial and compliance
15 oversight, including monitoring of vendor performance;” and “up-to-date legislative and
16 regulatory guidance [and] preparation of detailed and customized reporting packages.” See
17 <http://www.mcmnw.com/>.

20 Zenefits’ benefits management apps fall squarely into these permissible categories of
21 benefit administration services and are no different because they are offered online. As
22 established by the platform demonstration offered by Hazard and the screenshots set forth at Zen.
23 Ex. CU, the benefits apps made available to insurance customers provide the same benefit

25 Company Bulletin No. 2012-11 (2012); New Jersey Dep’t of Banking & Ins., Bulletin No. 11-22 (2011);
26 Idaho Dep’t of Ins., Bulletin No. 11-03 (2011); South Carolina Dep’t of Ins., Bulletin No. 2009-10
27 (2009).

1 management services provided by all brokers, including claims assistance, enrollment, insurance
2 forms, carrier contact information, plan details and coverage. These services, offered to all
3 insureds are designed to assist with the management of benefits, have no practical use or value
4 unless Zenefits is designated as broker of record so that it can access policy and coverage details
5 from insurance carriers. OIC has offered no evidence to the contrary.

6
7 RCW 48.30.157, which provides an exception to the anti-rebating statutes where service
8 discounts are provided in exchange for an insurance commission, also illustrates that services
9 designed to administer insureds' benefits plans do not constitute an illegal rebate. Section 157
10 notes that its exception applies to things "beyond the scope of services customarily provided in
11 connection with the solicitation and procurement of insurance." Thus, Sections 140 and 157,
12 read together, assume that brokers may perform—and not charge for—services that are
13 customarily provided to assist with the administration of benefits, such as enrollment assistance,
14 renewals, adding and dropping employees from plans, claims handling and similar services.

15
16 Finally, prohibiting brokers from offering benefits administration services for free would
17 have the perverse effect of outlawing efficient, modern, online administration of insurance
18 benefits and forcing insureds to depend once again on cumbersome and time consuming
19 paperwork in managing their benefit plans.

20 **E. The common interpretation would not render other statutes superfluous.**

21 OIC's argument that this common interpretation of the anti-rebating statutes would
22 somehow render other statutory and regulatory provisions "unnecessary and superfluous" is also
23 meritless. In fact, the provisions cited by OIC *support* the common interpretation.

24
25 Sections 140 and 150 prohibit illegal rebating and inducements to insurance. The four
26 related provisions cited by OIC, RCW 48.30.140(6)(a), RCW 48.30.150(3)(a), WAC 284-17-835
27

1 and RCW 48.30.157, create exceptions to Sections 140 and 150. These exceptions only come in
2 to play if, in the first instance, there is a violation of Sections 140 or 150. Concluding that a
3 benefit provided to the general public without condition does not constitute a violation of the
4 anti-rebating statute does not implicate, let alone undermine, these exceptions in any way.
5 Zenefits addresses each of these statutes and regulations in turn.

6
7 Sections 150(3)(a) and 140(6)(a) create exceptions for wellness programs offered by
8 insurance carriers. Without these exceptions, plans offering wellness programs only to insureds
9 in connection with an insurance transaction would run afoul of Sections 140 and 150. Plans,
10 however, will continue to be able to take advantage of these statutory exceptions regardless of
11 the outcome of this case.

12 WAC 284-17-835 creates an exception for promotional games of chance, or
13 "sweepstakes," a marketing tool used commonly by insurers. OIC issued this regulation in 2015
14 to clarify that sweepstakes may be permissible, and not run afoul of the anti-rebating statutes,
15 under certain circumstances. This regulation is notable because it reflects an acknowledgment
16 by the OIC, in 2015, that benefits provided to insureds do not violate the anti-rebating statutes if:
17 (1) the benefits are not connected to an insurance transaction ("no person eligible to receive the
18 prize is required to apply for insurance, purchase insurance, refer a person to the insurance
19 producer, or pay consideration"); and (2) the benefit is "open to the public." WAC 284-17-835.⁸
20
21 In other words, WAC 284-17-835 is not only consistent with Zenefits' interpretation of the anti-
22 rebating statutes, it reflects yet another acknowledgment by the agency that benefits offered to
23

24 ⁸ On the other hand, OIC notes that if "[a]n insurance producer conducts an annual drawing for all
25 of the individuals that made referrals . . . and gives away an all-expense paid trip for two to British
26 Columbia as the prize" this arrangement constitutes a violation of Sections 140 and 150 "as it requires the
27 persons being entered in to the drawing to make a referral to the producer," according to guidance issued
28 by OIC. See OFFICE OF INSURANCE COMMISSIONER, PROMOTIONAL GAMES OF CHANCE (2016),
<https://www.insurance.wa.gov/promotional-games-chance>.

1 the general public without a connection to an insurance transaction are not illegal. This is
2 consistent with prior OIC guidance provided by Marcia Stickler in 2008, in which she assessed
3 “the nexus” between a benefit and “a specific solicitation to insurance” and concluded that “OIC
4 will not consider [sweepstakes] a per se violation of 48.30.150(3) because the inducement to
5 insurance or the connection to an insurance transaction is tenuous in most cases.” Zen. Ex. D. at
6 1, 5.⁹

7
8 OIC’s suggestion that its theory of the case is supported by both Section 157 and OIC’s
9 1981 Bulletin No. 81-2, OIC Ex. 11, also fails. In Bulletin 81-2, OIC explained the purpose and
10 genesis of Section 157. At the outset, OIC noted that giving “*inducements to an insured . . . as a*
11 *result of an insurance purchase*” may constitute a violation of the anti-rebating statutes. OIC Ex.
12 11 at 3 (emphasis added). It then observed that the Attorney General in 1979 concluded that a
13 broker offering reduced fees for pension/profit sharing services to customers who purchased
14 insurance violated the anti-rebating statutes. The AG based its conclusion on the fact that half of
15 the usual fee for pension services “had been foregone by the licensee—that is, rebated—*in*
16 *exchange for the commission on insurance.*” *Id.* (emphasis added). OIC was concerned that this
17 result “could be *unfair to the consumer* in some cases.” *Id.* (emphasis added). For example,
18 “some of the things done by a pension or profit sharing advisor could also be done by an
19 insurance agent. . . . [T]o require a full fee for both aspects of the service received would result
20 in a client paying twice for the same service.” *Id.*

21
22
23 OIC requested that the legislature adopt Section 157 to address this situation—
24 specifically creating a carve-out to the statutes authorizing the Commissioner to approve

25
26 ⁹ Even if WAC 284-17-835 were rendered “meaningless” by Zenefits’ statutory interpretation—
27 which it is not – that consideration would be irrelevant as the intent of the legislature in enacting a statute
28 cannot be gleaned from a subsequently enacted regulation adopted by the implementing agency.

1 arrangements that could violate the statutes. That opportunity for a carve-out from what would
2 otherwise be a violation of the statutes does not, however, change what is required to constitute a
3 violation in the first instance—i.e., the discount, reduction in charges, or other benefit must be
4 “as a result of an insurance purchase” or “in exchange for the commission on insurance.” *Id.* In
5 other words, Section 157 simply creates an exception in certain instances where discounts are
6 provided in exchange for insurance. Here, there is no such exchange—Zenefits does not offer
7 free services “as a result of an insurance purchase” and revenues that otherwise would be
8 collected are not “foregone . . . in exchange for the commission on insurance.” In short, OIC’s
9 contention that other statutes and regulations support its Consent Order is baseless and the
10 statutory language requires a ruling in Zenefits’ favor.

12 **F. OIC’s statutory interpretation would have broad, unintended consequences**
13 **for the many innovative Washington licensees like Zenefits.**

14 There can be little doubt that Hamje’s *per se* test and OIC’s “convenience” test would
15 both snare all sorts of licensed entities offering non-insurance products and services—resulting
16 in the very “unintended consequences” that Hamje cautioned against. For example, Expedia is a
17 Washington licensed producer, offering travel insurance to its customers. Zen. Ex. BZ at 1. It
18 highlights its insurance line in its annual financial statements, noting that insurance sales are a
19 significant and growing part of its business. Zen. Ex. BZ at 62, 144. At the same time, Expedia
20 offers a variety of valuable discounts to its customers, including its insurance customers, such as:
21 a free hotel stay after 10 nights of bookings; the ability to earn “Orbucks” for discounts on future
22 bookings at hotels; a partnership with a bank to offer “rebates” to new bank cardholders and
23 “exclusive discounts” when cards are used at Expedia affiliate hotels.com; and a partnership with
24 Cabify for rideshare discounts. Zen. Ex. BZ at 55, 149. These benefits are valuable enough that
25 Expedia has to book a liability for the estimated future cost of redemptions in its financial
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1 statements. *Id.* at 55.

2 ADP is a payroll company that also provides time and attendance and human resources
3 technology to its consumers and is a direct competitor of Zenefits. Zen. Ex. BY; Haz. Tr. ADP
4 is also a Washington licensed producer offering property, casualty and health lines of insurance,
5 while promoting two free months of payroll service to new customers—on the same webpage it
6 advertises its insurance offerings. *See* Attachment 2.

7
8 USAA is a bank and licensed producer that offers free checking, no monthly service fee,
9 free ATM use, free direct deposits, free transfers and bill payment, free roadside assistance and
10 25% discounts at partner rental car companies Avis, Hertz, Budget and Enterprise. Zen. Ex. CB
11 at 12, 14, 15, 17. USAA sells its liability insurance on the same webpage it advertises car rental
12 discounts. Zen. Ex. CB at 13.

13
14 Overstock.com, an online retailer, offers vehicle, residential and business insurance, as
15 well as a variety of discounts to its “Club O” members, including dining rewards, free shipping
16 and up to 40% off certain purchases. Zen. Ex. CA at 3-5. It gives its Club O memberships away
17 for free to its credit card holders, veterans, teachers, students and first responders. Zen. Ex. CA
18 at 4. In promoting its insurance services, Overstock.com touts that shoppers can purchase
19 insurance “directly from its online shopping site” and that with its insurance offerings
20 “Overstock.com has joined the growing ranks of non-traditional insurance distribution channels.”
21 Zen. Ex. CA at 6. While OIC has downplayed the impact of its Consent Order on the likes of
22 Overstock.com, claiming that these companies are not really in the insurance business,
23 Overstock’s president and CEO disagrees, noting that its “own, private labeled, full-service
24 insurance aisle is “a game changer for the industry” and “a boon to the *millions* of consumers
25 who are looking for more affordable insurance.” *Id.*

1 In sum, the Consent Order's blanket prohibition on "licensees like Zenefits" offering free
2 or discounted services to the general public will require these and many other companies with
3 innovative business models that offer convenient and affordable access to a variety of products
4 and services, including insurance, to either cease offering insurance or stop providing discounts
5 on non-insurance services to their customers. Although Hamje discounted this risk, arguing that
6 the agency had not investigated these companies, his "objective" *per se* test would be satisfied
7 without the need for any investigation.
8

9 **III. Public policy weighs in favor of allowing companies like Zenefits to offer valuable**
10 **software for free or at less than fair market value.**

11 **A. This common interpretation is supported by public policy considerations.**

12 Public policy considerations also weigh in favor of allowing licensees like Zenefits to
13 offer free services with no connection to an insurance transaction to the general public.
14 Requiring Zenefits and other integrated companies to charge more to access historically free
15 services simply because they hold insurance producer licenses will hurt the very consumers the
16 anti-rebating statues were intended to protect. The testimony of Kalb and the affidavits
17 submitted by other Zenefits customers establish that the OIC's Consent Order is forcing
18 Washington small business owners and non-profits to incur significant costs.
19

20 The Consent Order's effect, however, will be felt far beyond the additional \$8 per
21 employee per month charge that Kalb and others have incurred. It will stifle innovation that
22 makes the lives of Washington residents easier, more convenient and more productive by
23 offering affordable, easily accessible integrated suites of services, and it will limit companies
24 like Expedia, Overstock.com, USAA and ADP from offering valuable discounts to their
25 customers. The net effect is that Washington businesses and consumers will pay more than their
26 out-of-state counterparts for a variety of goods and services, putting them at a competitive
27

1 disadvantage. Numerous regulators, as well as OIC's own Legal Affairs Division, have
2 acknowledged that allowing licensees like Zenefits to offer free services unrelated to insurance
3 transactions is good public policy. *See* Zen. Ex. AG (Montana concludes "[t]his interpretation is
4 also good public policy, as Zenefits may potentially provide Montana small businesses with
5 services they would otherwise not be able to afford"); Zen. Ex. T at 3 (Sticker concludes
6 "[p]ublic policy considerations should permit this activity as consumers are *benefited by*
7 *convenience and ease of use for employee benefit management* unrelated to the purchase or
8 solicitation of insurance"; Zen. Exs. AM, AN (Gellermann and Durphy conclude that "as a
9 matter of policy" BCBS should be allowed to offer free identity theft protection services to
10 insureds).
11

12 **B. Hamje's "policy considerations" and OIC's "public interest" arguments do**
13 **not apply here.**

14 The *only* legal authority cited by OIC in support of its contorted statutory interpretations
15 is a 1996 letter from an Alaska Assistant Attorney General ("AKAG") that Hamje claimed
16 provided public policy justifications for outlawing Zenefits' free software and apps.¹⁰ That
17 letter, however, does not purport to provide the legislative history of the anti-rebating statutes.
18 Nor does it address the reach of those statutes or apply the law to any factual scenario. Rather,
19 that letter responds to questions posed by a State Senator about whether Alaska's anti-rebating
20 statute violates Alaska's due process clause. Zen. Ex. B at 2. In an attempt to establish a
21 "rational basis" for that statute, the AKAG proposes a list of 13 "public policy" reasons "to
22

23
24 ¹⁰ Hamje testified that the Alaska AG letter was the "best" he found. Hamje Tr. P.69, 11. It was
25 also the "best" that another OIC staffer could come up with. *See* Zen. Ex. B at 1. And Washington
26 Assistant Attorney General Marta DeLeon could do no better, acknowledging to Hamje: "You also
mentioned some legislative history about one of the purposes of the rebating statutes being to maintain
fair competition between brokers. Do you have any notes or materials about that? The bill reports that I
reviewed don't mention competition as an issue." Zen. Ex. AT.

1 support these laws.” *Id.* at 10. This list is nothing more than a contemporary justification, by a
2 single state assistant attorney general, for finding Alaska’s statute constitutional. It certainly
3 cannot form the basis for an expanded, and unprecedented, interpretation of Washington’s
4 statutes.¹¹

5 Regardless of their merits generally, there is no evidence in the record to support a
6 finding that these public policy justifications apply here or that the Consent Order is otherwise
7 “in the public interest.” In his testimony, Hamje identified five policy justifications for the
8 Consent Order purportedly derived from the Alaska letter. Zenefits addresses each in turn.

9
10 i. *Hamje: “Nothing is free; someone has to pay; usually it is the consumer.”*

11 According to this theory, the “cost” of Zenefits free software and apps may be passed on
12 to and incurred by insureds in the form of increased premiums. This theory is bald speculation.
13 Indeed, Hamje acknowledged that “Zenefits may have a system that they don’t have to do that”
14 and that he doesn’t “know enough about how Zenefits business model works in terms of . . . how
15 they support their activities.” Hamje Tr. at 72: 20-25, 73: 1-6. While Hamje pointed to
16 authorities suggesting that the free software and apps are of significant *value to Zenefits*
17 *customers*, OIC offered no evidence of the *cost to Zenefits* of providing the free software and
18
19

20 ¹¹ None of the other materials provided to Hamje in Exhibit B support OIC’s legal interpretation or
21 that the Consent Order is in the public interest. The undated article entitled *Florida’s Anti-Rebating Law:*
22 *Background and Development*, is notable only for the fact that it quotes the Alaska AG’s laundry list of
23 public policy considerations. Notably, in 1996, the Florida Supreme Court held that Florida’s anti-
24 rebating statute violated the state’s due process clause by unnecessarily limiting the bargaining power of
25 consumers. *Dep’t of Ins. v. Date County Consumer Advocate’s Office*, 90 A.L.R. 4th 193 (Fl. 1986).
26 While the 2006 column published in the *Tarheel Financial Advisor* claims that one of the “important
27 public policy reasons” for the anti-rebating statutes is “to prevent the creation of a competitive
28 disadvantage or unlevel playing field for other agents, brokers and agencies in the market.” This theory
apparently didn’t carry water when North Carolina concluded in March 2015 that Zenefits “is not
engaging in rebating in violation” of its insurance laws because “Zenefits is not offering its free platform
in exchange for brokering insurance . . . [and, c]onsumers are not penalized for not using Zenefits as its
insurance broker.” *Compare Zen. Ex. B with Zen. Ex. Y.*

1 apps. Hamje also acknowledged that neither he nor OIC talked to insurers about the likelihood
2 they would pass on costs through premium increase; to Zenefits customers about their premiums;
3 or to regulators in other states about Zenefits' impact on premiums in those markets. Hamje Tr.
4 at 215: 4-7, 18-22.

5 ii. *Hamje: "Zenefits free offerings will result in price discrimination among*
6 *policyholders."*

7 There is no plausible basis to conclude that Zenefits free software and apps will result in
8 price discrimination. The anti-rebating statutes were adopted to address brokers' paying rebates
9 of their commissions, in cash or cash equivalent, to some insureds and not others. Here, on the
10 other hand, anyone can access Zenefits' free HR software and apps, including insureds using
11 different brokers. To the extent that the ability to access these free offerings reduces the
12 "effective" premium paid by insureds—as Hamje suggested—everyone in the marketplace can
13 take advantage of this offering, not just Zenefits' insurance customers. This is not discrimination
14 of any kind, much less the kind the laws were intended to address.

15 iii. *Hamje: The Consent Order is necessary to ensure a "level playing field" for*
16 *competing brokers.*

17 The anti-rebating statutes were adopted to protect *consumers*, not to protect local brokers
18 from competition at the expense of consumers. Indeed, as in any industry, competition among
19 brokers is good for consumers, resulting in innovation and better customer service.

20 Even if one were to assume an anti-competitive purpose to the anti-rebating statute,
21 Hamje's conclusory assertion that "no one can compete with the resources Zenefits has" has no
22 basis in fact. Indeed, Hamje admitted that he does not know Zenefits' annual revenue, its market
23 share, or even whether it is profitable; and his lack of familiarity with the facts of this case is
24 further underscored by his striking admission that he didn't even read all of Investigator Deb
25
26
27
28

1 Calhoun's interviews of Zenefits customers or any of OIC's Final Investigative Report. Hamje
2 Tr. at 159: 2-4, 227: 16-25. Tellingly, the only sources Hamje turned to for information about
3 Zenefits' potential impact on the market were Zenefits competitors, represented by the Big I. *Id.*
4 at 215: 4-14, 220: 16-25, 221: 7-15, 224: 18-22. Regardless, OIC offered no evidence for the
5 proposition that increased competition could have an adverse effect on consumers.

6
7 **iv. *Hamje: Zenefits' free offerings could create a risk of insurer insolvency.***

8 The anti-rebating statutes were prompted by, among other things, the concern that if
9 brokers rebated too much of their commissions to insureds they would demand bigger
10 commissions, potentially threatening insurers with insolvency. OIC admittedly did not speak to
11 any insurers to inquire about commission trends or whether brokers were seeking larger
12 commissions to compensate them for "free" services. Hamje didn't talk to OIC's Rates and
13 Forms department about premium and commission trends. Had he done so, he would have
14 discovered that commissions are in fact decreasing due to competition in the market place. It
15 also deserves note that this theory was considered and rejected by Stickler, who concluded that
16 there was no insolvency risk since "Zenefits apparently bears the cost of providing the
17 noninsurance services alone, so the insurer's revenue and ability to pay is unaffected." Zen. Ex.
18 T at 3.

19
20 **v. *Hamje: Zenefits' free offerings may result in insureds buying unsuitable***
21 ***policies.***

22 Again, OIC did nothing to investigate whether this in fact occurred. On the other hand,
23 Calhoun's interviews of 28 Zenefits' insurance customers, which Hamje did not read, revealed
24 that they were nearly uniformly pleased with their insurance policies and that many retained their
25 existing policies after designating Zenefits as their broker of record. Moreover, the suggestion
26 that a business might spend tens if not hundreds of thousands of dollars on an "unsuitable" policy
27

1 simply because it availed itself of Zenefits' free apps makes no sense.

2 In the end, all of these justifications suffer the same fatal flaw. There is no evidence to
3 suggest that they apply to Zenefits' free offerings or that OIC assessed their applicability at the
4 time it was investigating Zenefits.

5 **IV. OIC's Consent Order is entitled to no deference.**

6 As discussed above, because the standard of review here is *de novo*, OIC is not entitled to
7 deference. Further, deference to an agency is inappropriate where an agency's decision is—as
8 here—undocumented, post-hoc and unsupported by clear and consistent reasoning. *See*
9 *Chandler*, at *11.

10 As OIC's former Deputy Commissioner for Legal Affairs Carol Sureau testified,
11 Commissioner Kreidler, prompted by concerns that the agency was inconsistent in its application
12 of the law, adopted a detailed set of procedures for investigations and enforcement actions
13 designed to ensure consistency, transparency, and predictability. That process requires that: (1)
14 an enforcement action be referred to Legal Affairs; (2) the action then be assigned to a Legal
15 Affairs staff attorney to perform a legal analysis and then reduce it to writing; (3) Legal Affairs,
16 where appropriate, may also assign an investigator to investigate and report factual findings
17 which the assigned attorney considers in her legal analysis; (4) if, on the basis of that legal
18 analysis, the Deputy Commissioner for Legal Affairs determines that there was a violation, the
19 case is be referred to either the Compliance Committee ("CC") or the Producer Enforcement
20 Group ("PEG") along with a written legal analysis and recommendations; and (5) that the CC or
21 PEG meet and issue an Outcome Summary with a final recommendation as to the enforcement
22 action. This process (the "Kreidler Process") is reinforced by the February 23, 2015 Legal
23 Affairs Interoffice Memorandum launching a formal investigation into Zenefits. Zen. Ex. W
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1 (describing OIC's "standard investigative protocol" and "standard operating procedures"). As
2 that memorandum establishes, there must be detailed findings—in writing—reflecting whether
3 violations of the law occurred, summarizing all the evidence gathered and containing the
4 ultimate legal conclusions.

5 Hamje conceded that none of this was done here. Hamje Tr. at 173: 8-10. Instead, the
6 agency took the "unprecedented" step of transferring the case from Legal Affairs to Hamje.
7 Although Hamje testified that it is important in investigations to focus on the details, obtain staff
8 input, be consistent, consider unintended consequences and memorialize decisions, he and OIC
9 did none of these things after he took over the investigation. Hamje Tr. at 113: 21-23, 114: 1-2,
10 131: 21-25, 183: 12-15, 232: 1. Indeed, the paper trail went cold as soon as Hamje was assigned
11 the case, with one exception—Hamje continued to provide an audience to, and solicit the views
12 of, the local brokers' lobbying group, the Big I. As a result of these failures, Hamje was unable
13 to explain: why the case was transferred to him; why the September 14, 2015 draft Final
14 Investigative Report did not contain a finding; why he was purporting to assess the applicability
15 of statutory exceptions in the fall of 2015 if OIC had not yet decided to find Zenefits in violation
16 as he contends; what happened at and who attended the meeting in the spring of 2016 when
17 Hamje allegedly made his recommendation and transferred the case back to Legal; or why he
18 didn't bother to read the August 1, 2016, Final Investigative Report until preparing for this
19 hearing. These failures demonstrate the arbitrary nature of this enforcement action and the lack
20 of merit in OIC's post-hoc legal theories, to which no deference should be afforded. *See*
21 *Chandler*, at *11 (under *de novo* review, arbitrary agency procedures that "disregard the facts
22 and circumstances, and [that] are unreasoned and without consideration" should be rejected).
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1 CONCLUSION

2 Zenefits is revolutionizing the way small businesses and non-profits operate their
3 businesses, much in the same way the iPhone revolutionized how we live our day-to-day lives.
4 Zenefits' innovative integrated platform provides employers and their employees with all their
5 HR, payroll, and benefits information at their fingertips, both in the cloud and on their mobile
6 devices, eliminating the burden and cost of mountains of paperwork and time consuming tasks.
7 It provides small business owners like Stefan Kalb with access to a host of HR services that
8 were, until now, complicated and costly to administer, and frees them up to focus on building
9 their businesses, creating jobs and simplifying their employees' lives.
10

11 OIC's expansive and unprecedented interpretation of the anti-rebating statutes threatens
12 all of this, and more. Were there some compelling public interest in requiring licensees like
13 Zenefits to charge for services that enhance consumer convenience one might understand OIC's
14 approach. But there is not. To the contrary, the evidence established that this was an ends-
15 driven, politically motivated decision, with no consideration of agency precedent, or process, or
16 its impact on consumers that OIC even today cannot explain or justify. These significant failings
17 aside, the law is clear: the anti-rebating statutes do not prohibit Zenefits or other licensees like
18 Zenefits—including banks and online travel agencies—from offering free non-insurance benefits
19 on equal terms to the general public.
20

21 For these reasons and those set forth at the hearing and in Zenefits' Hearing Brief, the
22 Court should rule that RCW 48.30.140 and RCW 48.30.150 do not prohibit a licensee like
23 Zenefits, acting directly or through affiliates, from offering valuable software functions or other
24 valuable benefits for free or at less than fair market value to the public, and should reverse OIC's
25 conclusion to the contrary.
26

1 Dated this 27th day of July, 2017.

Respectfully submitted,

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*Counsel for Appellant YourPeople, Inc. dba
Zenefits FTW Insurance Services*

ATTACHMENT 1

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11 YourPeople, Inc. dba Zenefits FTW Insurance
12 Services, Appellant.

13

14 Docket No. 02-2017-INS-00009

15 Hearing Day 2

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1 completed concerning insurance companies,
2 potentially [UNINTEL] for insurance companies, if
3 there would be a discussion with our alum.

4 Not all the deputies, most of the
5 deputies were there. I think the only deputy that
6 did not attend was operations deputy, but it was
7 all of the regulatory--the big regulatory, we
8 used to call them the big three--Consumer
9 Protection, Rates and Forms, and Company
10 Supervision, and then also, Legal Affairs.

11 Legal affairs led that group. And also,
12 Policy that was there, as well as Public Affairs.
13 If I've missed one, I'm sure Mr. Colman will
14 remind me. And what we would do is the attorneys-
15 -and I'd give this to staff attorneys as well.

16 We would present with a memo, facts,
17 law, explain it, answer questions. My practice
18 had been, meet with the deputy for a particular
19 area that had referred the matter originally, and
20 to make sure that whatever recommendation I was
21 going to make would be something that a deputy
22 would--that [UNINTEL] on, but also [UNINTEL].
23 What we were doing, I wanted to try to get
24 [UNINTEL], if I could.

25 And so, I would go ahead and make the

1 presentation as the other one, staff attorneys
2 would, and the deputies would listen as questions
3 have been decided, what would be the [UNINTEL].
4 You know, the idea behind it, there are two
5 things that were really important about it. The
6 first was, is that there had been a time before
7 commissioner [UNINTEL] had come to the office,
8 that the decisions were made by the legal affairs
9 deputy, [UNINTEL].

10 And this was not something that was
11 deemed by the deputies, particularly the new
12 deputies that were coming in, something that was
13 appropriate. That particular deputy, and I'm not
14 talking about Ms. Cirillo, because she was
15 appointed [UNINTEL] tenure. It was a predecessor,
16 where there were--my understanding is, there were
17 objections about how they operated, where
18 decisions will be made about the input of the
19 staff, without the input of the deputies.

20 And there would be no consistency.
21 There would be no connection to policies
22 necessarily that the commissioner was wanting to
23 focus on these kinds of things. And so, that was
24 something that wanted to be cured, and it was
25 wanted that there would be a decision that people

1 would focus in trying to make sure that it would
2 be a consensus driven, and it would take into
3 consideration all of the various aspects of
4 [UNINTEL] what the agency was focusing on.

5 The other aspect of it, that I think
6 was extremely important is consistency,
7 precedent, trying to--there were a series of
8 principles that were laid out, when it was first
9 established. And it may have been modified from
10 time to time, but they were principles that
11 [UNINTEL], took things that determined that
12 fairness, how it would look to the public, you
13 know, just a whole [UNINTEL]. I don't remember
14 them all now, but we paid close attention to try
15 to be fair in how--but we do that, and
16 accomplished that.

17 So and another group that was also kind
18 of spawned from this group was after the
19 investigation's function was transferred into
20 Legal Affairs, and Ms. Cirillo began to deal with
21 the, you know, the investigation's union, and the
22 different, her concept, which is basically an
23 investigator's unit, purely, you know,
24 investigating matters, not trying to promote
25 compliance, you know, at least not directly, as

1 it had been before. That was really what my job
2 was supposed to be.

3 And what [UNINTEL] we set up and we
4 would call it the [UNINTEL] enforcement
5 [UNINTEL]. And it was to be made up of five
6 working members. And two deputies, Legal Affairs,
7 and Consumer Protection, Producer Licensing and
8 Enforcement program--I'm sorry, produce the
9 licensing [UNINTEL] a program manager was also a
10 [UNINTEL] member.

11 The manager investigations was a
12 [UNINTEL] member. And also, excuse me, the senior
13 staff attorney, who actually was designated to
14 facilitate the [UNINTEL]. And that--the original
15 one was a gentleman by the name of Chuck Brown,
16 who had been--actually started as a staff
17 attorney just a couple of months before I became
18 employed at the OIC.

19 So that meeting was basically, the
20 intention was to do the same thing. Memos had
21 been prepared and presented, and the idea would
22 be is that we would talk about them and trying to
23 be consistent and fair on how we would approach
24 the staff.

25 And so, that--now there were other

1 years, I've been with [UNINTEL] Affordable Care
2 Act groups served on for years. There were--most
3 recently, it's called an ACA Alignment Group, I
4 think is--that it's dealing with.

5 But the ones that I've described to
6 you, I think are ones that are the most--that I
7 can think of right now, they're the ones that
8 have continued for a long period of time and that
9 I've participated in in one way or the other.

10 DARRYL E. COLMAN: And you talked about
11 a number of groups that seemed to cross
12 divisional lines. Why is getting [UNINTEL]?

13 JOHN HAMJE: Well, you know, the thing
14 about bureaucracies, and I have to say, you know,
15 I've been involved in them both in the private
16 sector and in the public sector for 33 years,
17 with [UNINTEL]. I think it--one of the hugest
18 problems I think you deal with is people talking
19 to each other, and people sharing information.
20 Siloes, it's just terrible.

21 And I know that it's also an issue that
22 many private sector companies have to deal with
23 as well, but it's just--I just found it to be
24 something that's very characterization, of what
25 you find in bureaucracies.

1 And if you--you know, you may be taking
2 an action in one area, and you know, maybe
3 responding to a consumer request stay or a
4 consumer issue or a producer issue or a company
5 issue. And it may be for the first time, that's
6 the first time you've ever seen it.

7 Well, that may very well be the case
8 that maybe it's the case to [UNINTEL] for the
9 entire agency, but probably it isn't. Probably
10 somebody else in the agency has been working on
11 that and knows something about it.

12 And the problem is, there's a lot of
13 times that these kinds of things will come into
14 the agency, and something will be--a [UNINTEL]
15 will be written, a decision might be made, a memo
16 might be prepared, something would occur, and it
17 would state a position.

18 And then, it would turn out, well, wait
19 a minute. You didn't check with the people that
20 are actually involved in the day to day
21 regulation of that particular area, you know? And
22 no, we--here's memos we've had before. Here's
23 information we've had before. Here's things we've
24 done before.

25 You need to take that into

1 consideration. And so, this was what we were
2 trying to do. You know, we have a number of areas
3 and I think it's particularly with the deputies,
4 they can talk to each other about these things.
5 And they will try to share information. And
6 they're really the ultimate folks that are
7 responsible for the--how their groups operate.

8 But staff are the ones below the
9 deputies who are usually the ones who have the
10 great expertise. They're the ones that have been
11 on the front lines for years. And they're the
12 ones that you need--they are the [UNINTEL] that
13 you go to.

14 Now see, now sometimes they're wrong.
15 You discover they've made--you know, they're--
16 that they're doing something incorrectly and
17 you've changed. And that's important, too, by the
18 way.

19 But more often than not, they have
20 something really worthwhile to share, and that
21 you have to make sure that that is pulled in, and
22 you try to develop different mechanisms. And some
23 of these types of committees that we've pulled
24 together tended to do exactly that, and I think
25 that's what Carol Cirillo and the commissioner

1 and Mike Watson wanted to do, and the compliance
2 group.

3 And it's clearly one of the things we
4 wanted to do with the producer, enforcement as
5 well. But all these other groups, that is a
6 common denominator, I would--

7 DARRYL E. COLMAN: Thank you. Do you
8 believe these kind of processes help with
9 [UNINTEL] public?

10 JOHN HAMJE: Well, of course. You tend
11 to have, you know, I'm a little bit of a student
12 of [UNINTEL] history. You know, [UNINTEL], he
13 could make all of the decisions because he was a
14 genius. But not everybody is a genius. And the
15 best way to go ahead and try to come to a fair
16 and appropriate decision is to bring in smart
17 people, is to have the people, particularly the
18 people that have the expertise and have the
19 experience of having--working in these various
20 areas, to be at the table to talk about it.

21 And that was, I think, what really
22 helps the consumers, because then you try to come
23 to--with a--well, you try--you may not always get
24 wisdom, but you want to have something where you
25 display some good judgment and make good

1 2015. And because I don't know if there had been
2 an investigation before. I understood there was
3 some inquiries made or something, but in any
4 case, the decision, my recollection was, is it
5 was made at a deputy's meeting, and it should be
6 before. But that's my recollection.

7 DARRYL E. COLMAN: Okay. And is that
8 also the case with the decision to move forward
9 with the enforcement?

10 JOHN HAMJE: Yes, there's no question
11 about that because I remember making the
12 presentation at the deputy meeting because it was
13 mine. I was the one that carried the ball on the
14 compliance side to try to bring it through
15 compliance and trying to identify and make sure,
16 you know, we knew where the issues were, we knew
17 where the statutory framework was, and so that I,
18 the families, the [UNINTEL] that presentation and
19 that it was referred by the deputies and the
20 chief deputy in order to--for enforcement.

21 DARRYL E. COLMAN: Was the chief--was
22 the deputy for legal affairs part of those
23 decisions?

24 JOHN HAMJE: Absolutely.

25 DARRYL E. COLMAN: If it's all right,

1 Your Honor, we'll ask for a brief restroom break.

2 JUDGE LISA DUBLIN: Sure.

3 DARRYL E. COLMAN: Is that all right?

4 JUDGE LISA DUBLIN: Absolutely, and
5 [UNINTEL] when you're ready. We're off the
6 record.

7 (Recess)

8 JUDGE LISA DUBLIN: All right. We're
9 back on the record after a morning break in
10 testimony. During that break or any breaks
11 yesterday, did we talk about the case, Ms.
12 Colman?

13 DARRYL E. COLMAN: We did not, Your
14 Honor.

15 JUDGE LISA DUBLIN: Thank you. And
16 [UNINTEL]?

17 PETER WALSH: No, we did not, Your
18 Honor.

19 JUDGE LISA DUBLIN: All right, then,
20 thank you. All right, then.

21 DARRYL E. COLMAN: Thank you. Mr. Hamje,
22 is there anything else that you'd like to add
23 about the decision making process in this case?

24 JOHN HAMJE: I don't think so, no.

25 DARRYL E. COLMAN: No? Okay, thank you.

1 You testified earlier about how you were clear
2 that Zenefits' business model fed into 4831, 40,
3 and 150. Could you explain that, please?

4 JOHN HAMJE: Well, Zenefits is an
5 insurance produced--it makes no bones about the
6 fact that it makes its money from selling
7 insurance. And [UNINTEL] it's the way it pays for
8 providing all these free services [UNINTEL] to us
9 to employers.

10 I base that on materials that I had
11 reviewed that came out of the investigation of
12 the OIC. Time and again, it talks about those
13 materials, data timing and other materials, you
14 know, that have taken [UNINTEL] do this because
15 they make their money from selling insurance.

16 And so, you know, that is a problem
17 when you provide free anything or provide other
18 types of benefits that are not part of the policy
19 that is issued to the insured. And that is what's
20 prohibited by a base [UNINTEL] and a legal
21 [UNINTEL] statutes.

22 And if so, the agency's enforced it,
23 was [UNINTEL] at the agency. And staff, if
24 they're my staff, who I--who have been there
25 longer than I have, have confirmed that. So and

1 as I said, when I found that old AGO opinion, I
2 thought I found maybe at least a recognition back
3 then, or maybe even back further, who knows.

4 These are old laws, you know? They're--
5 these are from 1911, so they're based--at least
6 before all of the modifications were made,
7 they're from 1911, and that was a time when
8 you're really looking at things that were going
9 on in the late 19th century, early 20th century.

10 And so, but so I don't know how--I
11 can't reach back to 1911 when [UNINTEL] back
12 then, [UNINTEL]. But this seemed to be a real
13 problem. It's not permitted to go ahead and
14 provide those kinds of benefits, to [UNINTEL] and
15 selling them to insurance. You know, one of the
16 issues that has been raised is, there's no
17 requirement to [UNINTEL].

18 So you know, that's fine. If Zenefits'
19 were not in selling insurance, there'd be
20 absolutely no problem with the agency, a[UNINTEL]
21 I have any issue with Zenefits whatsoever, but
22 because they are selling insurance, then we
23 looked at their entire, you know, the way they
24 relate to their customers.

25 And clearly, when they offer as an

1 it.
 2 And so as we did--during that time, one
 3 of the things that I was interested in exploring
 4 is that all during this time, all we had really
 5 been doing is just saying, okay, here are the
 6 laws, and laid out and [UNINTEL] the legislature.
 7 We're not that concerned about the policy. We're
 8 just going to implement these laws as we
 9 understand.

10 Well, now for the first time we were
 11 going to be dealing--this is out there--with the
 12 policymakers. And of course their questions are
 13 going to be, why do we need these laws? What's
 14 this all about? This is counterintuitive.
 15 Consumers are not getting a good deal here.
 16 What's happening?

17 And so I asked that question, too. I
 18 said, do we really need these laws anymore? Why
 19 don't we go ahead and just dump them? And I
 20 talked to the chief deputy about it and he agreed
 21 that we needed to make a decision--put up or shut
 22 up.

23 So, I began some research mostly on the
 24 internet, looking, trying to get information
 25 about well, what's going...what do other states

1 do? What are the policies? What are the
 2 arguments--what are the reasons for these
 3 particular laws? Are they still valid today?

4 And I found a number of different
 5 things, and ultimately I came to the conclusion,
 6 yes, that they are, and I felt that they were.
 7 And I put together some materials and I shared
 8 them with the legislative director so that she
 9 could use them. Because these questions were
 10 going to come up before the legislature on these
 11 issues. And so we got that answered, so our
 12 proposal then--as we moved forward, all we did
 13 was we just worked on trying to refine the
 14 proposals that were before the legislature.

15 And so as we went through it, we did so
 16 and it was--we ended up with, I think the 133 and
 17 135, which are the ones I mentioned before--are
 18 the two that came out of it. We also ended up
 19 with the rulemaking. We went back, we had to go
 20 ahead and make changes in some of the rules that
 21 would've gone into effect in July so that we
 22 could go ahead and reflect the changes in the
 23 law. And so we did so, and we clarified some
 24 things in those rules as well.

25 And so that's really, I think, where I

1 got my education and I think that many staff that
 2 I shared all of this with at the agency had
 3 learned a lot about what was underlying--what the
 4 underlying policy was for these and more about
 5 how we enforce it.

6 Part of what also had come up too is
 7 there was an argument or an issue was raised that
 8 we were not enforcing these laws. It apparently
 9 came through our legislative director, hearing
 10 something like that. And so one of the things I
 11 also did is I went back at that time and had my
 12 staff working with the [UNINTEL] Affairs staff to
 13 put together and list the [UNINTEL] of the
 14 consent orders and other types of orders, and
 15 other actions, and letters of reprimand, and all
 16 that kind of stuff that were involved in--going
 17 back three-four years, I don't know how many
 18 years now it was, from the end of 2014, and with
 19 a little brief summary of each of these orders
 20 and what happened. And show that we actually were
 21 enforcing it. We were not ignoring it at all, and
 22 we were doing our job, so that she would have
 23 that as ammunition. So when she went before the
 24 legislature and had those questions raised, she
 25 would have something there you could talk about.

1 So that was another thing that we went
 2 through that I also had shared with the [UNINTEL
 3 PHRASE].

4 DARRYL E. COLMAN: Mr. Hamje, did you
 5 find any helpful materials that helped your
 6 understanding for the purpose of the rebating
 7 sessions?

8 MR. HAMJE: I did. I think the best one
 9 that I found--I liked it the best--was an old
 10 Alaska attorney general came in from 1995 or '6
 11 or something like that, and they just laid it out
 12 beautifully what they were. It was one of a
 13 number of different things. There were a number
 14 of articles that I felt were particularly useful
 15 that I shared. I read a lot more than just that,
 16 but these were things that I thought were most
 17 useful and could be easily understood and picked
 18 up by staff when they were reviewing them, and
 19 could be explained.

20 DARRYL E. COLMAN: I'm going to hand to
 21 you the Appellant's Exhibit [UNINTEL]. Could you
 22 take a look at Exhibit B, Page, I think, three?
 23 [UNINTEL] two and three. Do you recognize that
 24 document?

25 MR. HAMJE: Yes. Yes, this is the one

1 from--this is the AG opinion I was talking about.
2 It goes from Page 2...it goes from Page 2 to Page
3 14. What I plagiarize often from this particular
4 document were those items on Page 9. There's a
5 laundry list there--I think it's the one. It goes
6 on to Page 10 as well. And I changed it a little
7 bit to take the ones out that I didn't think
8 applied anymore. And I prepared kind of--just a
9 sheet that I would include in some of my emails
10 that were sent around to the liaison and to other
11 staff that were working on that legislation at
12 the agency.

13 DARRYL E. COLMAN: What did you take
14 away from this document?

15 MR. HAMJE: Well, that there was still
16 use for it. You know, the world was a lot
17 different in the late 19th century, early 20th
18 century in terms of insurance. But--and things
19 were just going crazy. We didn't have as good
20 financial regulation, there was... The one thing
21 that has not changed, there's tremendous
22 competition.

23 But back then, the competition--to such
24 an extent it was much less regulated. And so
25 there were folks promising all kinds of things to

1 their business model in this state, we're going
2 to be looking at others in other areas, not just
3 in health and disability, but others in all the
4 other lines of insurance will start looking at
5 the possibility of doing the same thing or
6 something similar because the concept could be
7 applicable all the way across the board.

8 You know, one of the things that's
9 different now is that we have a lot better
10 financial regulation of insurance. Much better.
11 And having been in an insurance department in the
12 '80s and worked in receiverships, I am very
13 grateful for all the work that was done for so
14 many years since that time in really tightening
15 down all of the financial regulations. So it's
16 much stronger now.

17 But what happens is this: Is that
18 anything that is given to a consumer that is free
19 is really not free. It's going to be paid for.
20 Somebody has to pay for it, and usually it's
21 going to be the consumer.

22 Now, Zenefits may have a system that
23 they don't have to do that to, but the concept
24 that's applied across the board, what's going to
25 happen is that everybody else is going to get

1 go ahead and sell insurance. And it just created
2 issues with how--with insurance--insolvencies,
3 with consumers being hurt, all kinds of issues.

4 And so these laws ultimately--and
5 essentially they're based on a model--were
6 enacted and we're talking about 140 and 150
7 basically. I think 140 is the broader statute;
8 150 is kind of a subset of that broader statute
9 but they're very closely related.

10 They were designed to stop these
11 practices and create a level playing field so
12 that there would not be these kinds of marketing
13 abuses that were creating all of the problems in
14 the marketplace. And so when you look at these
15 particular number of--113...I think they, to some
16 extent, can apply today but not all of them as
17 much as others and there are some changes, too.

18 Keep in mind that these rebating laws
19 [UNINTEL] all lines of insurance. And I think
20 that's very important to keep in mind when you're
21 talking about it. It's not just health or
22 disability insurance, which is what the benefits
23 are all about; it goes way beyond that.

24 And so, if there's a determination made
25 that Zenefits can go ahead and go forward and use

1 into that business and try to do the same thing.
2 They may not be able to--assuming, again, and I
3 don't know enough about how Zenefits' business
4 model works in terms of the inner activities of
5 how the funds--how they support their activities--
6 what will happen is that everybody will have to
7 go ahead and start providing freebies, free
8 services, to go ahead and compete in the
9 marketplace.

10 If you don't do that, then there's
11 going to be--then you're going to lose out to
12 other competition. And when that happens, these
13 kinds of expenses for these freebies can be built
14 into the race and they will be approved by
15 insurance companies--by the insurance departments
16 in their rate [UNINTEL]. And so, the rate premium
17 will be higher, and the freebies will actually be
18 reflected and it'll be paid in those rates.

19 And it particularly is going to be
20 significant because if some of the people do not
21 buy--or I'm sorry--do not buy insurance but
22 receive the services, well, they're not going to
23 contribute, and so the premiums are not going to
24 reflect--they're just going to reflect that--
25 there's a smaller group of people that's going to

1 JUDGE LISA DUBLIN: Thank you.
 2 [BREAK]
 3 JUDGE LISA DUBLIN: All right, we're
 4 back on the record after lunch. The time is about
 5 12:54. We'll resume with cross-examination, I
 6 believe of Mr. Hamje. Are you ready to proceed?
 7 PETER WALSH: I am, thank you, Your
 8 Honor.
 9 JUDGE LISA DUBLIN: All right, thank
 10 you.
 11 PETER WALSH: Good afternoon, Mr. Hamje.
 12 JOHN HAMJE: Good afternoon.
 13 PETER WALSH: I have a number of things
 14 I want to cover. But I want to go back to one of
 15 the things you mentioned in your direct
 16 examination. You offered a pretty detailed
 17 narrative in defense of OIC's consent order in
 18 the course of your testimony. And I want to break
 19 it out a little bit.
 20 One of the things I understand you did
 21 is you reviewed and you analyzed Section 4830 140
 22 and 150. Is that correct? And it's not a guess,
 23 meaning those are the--I'll represent the anti-
 24 rebating and anti-inducement statutes?
 25 JOHN HAMJE: Well, I guess "reviewed and

1 analyzed" is accurate.
 2 PETER WALSH: Okay. And where is that
 3 review and analysis memorialized?
 4 JOHN HAMJE: It's not.
 5 PETER WALSH: It's not in the final--the
 6 agency's final investigative report?
 7 JOHN HAMJE: No, it would not be there.
 8 PETER WALSH: It's not in the consent
 9 order?
 10 JOHN HAMJE: No, it's not.
 11 PETER WALSH: Is it in any legal affairs
 12 department memo?
 13 JOHN HAMJE: Not that I'm aware of.
 14 PETER WALSH: Okay, or a written
 15 recommendation to the producer enforcement group?
 16 JOHN HAMJE: No.
 17 PETER WALSH: And it's not in OIC's
 18 prehearing brief in this case?
 19 JOHN HAMJE: Well, may I ask you a
 20 question? Are you referring to a document?
 21 PETER WALSH: I should back up. I
 22 apologize. Have you had an opportunity to review
 23 the brief that has been filed by the Office of
 24 Insurance Commissioner in this case, in advance
 25 of this hearing?

1 JOHN HAMJE: No, I have not.
 2 PETER WALSH: Okay.
 3 JOHN HAMJE: [UNINTEL] the review and
 4 analysis that you mentioned, there was never a
 5 document [UNINTEL] result of my review and
 6 analysis.
 7 PETER WALSH: You also, I understand,
 8 reviewed and analyzed Section 157, so that's 4830
 9 157?
 10 JOHN HAMJE: That's correct.
 11 PETER WALSH: And you talked a little
 12 bit about the purpose of that statute today.
 13 JOHN HAMJE: Mm hmm. That's correct.
 14 PETER WALSH: And likewise that analysis
 15 is not documented anywhere?
 16 JOHN HAMJE: It's not documented. Well,
 17 if it is, it would be in notes here and there. I
 18 don't recall actually putting together a document
 19 of analysis. I took notes. I may have--I reviewed
 20 materials. I may have made notations. Those are
 21 the kinds of things that I did.
 22 PETER WALSH: It's not memorialized in
 23 any formal report or memos [UNINTEL] OIC?
 24 JOHN HAMJE: It is not.
 25 PETER WALSH: Okay. Did anybody else

1 memorialize to writing your analysis or any
 2 similar analysis of Section 157?
 3 JOHN HAMJE: [UNINTEL] I'm not aware of
 4 any [UNINTEL].
 5 PETER WALSH: You also considered the
 6 legislative history, I understand?
 7 JOHN HAMJE: Yes.
 8 PETER WALSH: And was that memorialized
 9 to writing?
 10 JOHN HAMJE: There is a document, but--
 11 that's all that matters.
 12 PETER WALSH: What document is that?
 13 JOHN HAMJE: It's a document that was
 14 prepared by [UNINTEL] of our policy and
 15 legislative affairs division that was shared
 16 internally.
 17 PETER WALSH: Okay. Do you remember
 18 about when that was?
 19 JOHN HAMJE: It was between [UNINTEL]
 20 say November of 2014 and February of 2016,
 21 somewhere in that [UNINTEL].
 22 PETER WALSH: And tell me a little bit
 23 about the document [UNINTEL] we issued a public
 24 records request to the agency, and it's possible
 25 I missed it. But we asked for anything related to

1 this investigation and I don't recall seeing
2 that. Can you tell me a little bit more about
3 that document?

4 JOHN HAMJE: Yes. It was--Mr. Tompkins
5 apparently--I'm going from memory now. He took
6 various--he went back and cut-and-pasted the
7 various changes in the statute from one year to
8 the next, from one [STATUTE?] as there were
9 amendments, and showing where the differences
10 were from year--from session to session, where
11 there was a change.

12 And so, they were all lined up
13 chronologically on the page. And they had, you
14 know, taken them out of each--copied the
15 documents and just pasted in, and made copies of
16 that, and then shared that with me, obviously.

17 PETER WALSH: Was there any analysis of
18 Zenefits or application of that legislative
19 history to Zenefits in that memo?

20 JOHN HAMJE: I don't recall anything
21 other than just laying out how the statute
22 evolved.

23 PETER WALSH: Otherwise, no
24 memorialization by the agency of how the
25 legislative history of--or how 157 might apply to

1 Zenefits?

2 JOHN HAMJE: I don't think so.

3 PETER WALSH: Okay. [UNINTEL]
4 legislative history? No memorialization by the
5 agency of how the legislative history of the
6 anti-rebating statutes might apply to Zenefits?

7 JOHN HAMJE: Not that I'm aware of.

8 PETER WALSH: Okay. Or support some of
9 the public policy purposes that you described
10 today?

11 JOHN HAMJE: Well, again, not that I'm
12 aware of.

13 PETER WALSH: You also--I understand you
14 testified that you had given some thought to
15 whether Zenefits's online integrated platform was
16 a good or service. Is that correct?

17 JOHN HAMJE: Yes. Uh huh.

18 PETER WALSH: And is that--was that
19 analysis memorialized in writing by you or
20 anybody else at the agency?

21 JOHN HAMJE: Not that I'm aware of.

22 PETER WALSH: And you discussed numerous
23 meetings with Zenefits over the course of 18
24 months; is that correct?

25 JOHN HAMJE: No, just two meetings.

1 PETER WALSH: Two meetings with
2 Zenefits? And were those meetings with Zenefits
3 memorialized by you or the agency?

4 JOHN HAMJE: I took notes on some
5 occasions, or prepared notes afterwards. I don't
6 recall if I did it on both occasions, maybe just
7 one of them.

8 PETER WALSH: Besides your handwritten
9 notes, are you aware of any memorialization or
10 analysis of the information that was obtained in
11 those meetings by the agency?

12 JOHN HAMJE: I--no.

13 PETER WALSH: And you also--we talked
14 about Exhibit 11 in the Office of Insurance
15 Commissioner's Exhibits, the 1981 advisory. And
16 you provided a sort of explanation and narrative
17 around that. Is that memorialized in writing?

18 JOHN HAMJE: What, the [UNINTEL]
19 writings?

20 PETER WALSH: You gave a--okay, yes.
21 There's a '78 attorney general opinion. Is that
22 correct?

23 JOHN HAMJE: That is correct.

24 PETER WALSH: And there's an '81 OIC
25 advisory. And I think you gave a summary and a

1 bit of an interpretation of both. Is that a fair
2 characterization?

3 JOHN HAMJE: Yes, I summarized them.

4 PETER WALSH: And as--was your summary
5 or characterization of both of those documents,
6 or either of those documents, memorialized in
7 writing?

8 JOHN HAMJE: I don't think so.

9 PETER WALSH: Okay. And you talked a
10 little bit about--I think you were--in your
11 opinion, there were a series of purposes to the
12 statute that you identified, which included
13 passing on--avoiding--making sure that costs
14 weren't passed on to consumers and consumers were
15 making the right decisions about policies, the
16 need for a level playing field. Do you recall
17 what I'm talking about?

18 JOHN HAMJE: Yes, I do.

19 PETER WALSH: And any of those public
20 policy purposes of the statutes that you offered
21 up, were those memorialized in any written
22 document by the agency?

23 JOHN HAMJE: Well, I think there have
24 been some documents that I have put together that
25 I've shared with staff that are based upon that

1 AGO opinion from the Alaska Attorney General's
2 Office. I cut and pasted some items for that. But
3 I don't think that there would be an analysis. I
4 might've just provided those--that information as
5 a--to give people an understanding of what the
6 policy, a policy--underlying policy is for, [ON
7 41?].

8 PETER WALSH: So, none of the analysis,
9 statutory legislative history or otherwise, that
10 you offered today, Mr. Hamje, is reflected,
11 certainly in -- it is not reflected in any formal
12 OIC report or analysis, correct?

13 JOHN HAMJE: I'm not aware of any report
14 that would include that information.

15 PETER WALSH: And are you aware of
16 anything produced by the legal affairs division
17 that reflects your views?

18 JOHN HAMJE: I'm not aware of anything
19 along those lines, no.

20 PETER WALSH: Mr. Hamje, the
21 interpretation you offered today, do those
22 represent your opinion or the opinion of the
23 Office of Insurance Commissioner?

24 JOHN HAMJE: Well, now you've put me in
25 a difficult spot. I am no longer associated with

1 the Office of Insurance Commissioner. So, I do
2 not speak for it. I can only say that, at the
3 time that I was an employee of the OIC, they
4 ultimately were adopted by the Office of
5 Insurance Commissioner.

6 PETER WALSH: When you say ultimately
7 they were adopted, do you mean that the Office of
8 Insurance Commissioner determined that Zenefits
9 was in violation and entered into the consent
10 order to address it?

11 JOHN HAMJE: Yes, I think that that was--
12 well, you could say it was shown by the OIC's
13 actions.

14 PETER WALSH: And I understand that. But
15 I want to talk specifically about some of the,
16 you know, legislative--the purposes, statutory
17 purposes that you identified. To the extent that,
18 for example, you represented that one of the
19 purposes of the statute purportedly is to ensure
20 a level playing field, does that represent the
21 view of the Office of the Insurance Commissioner
22 or your personal opinion?

23 JOHN HAMJE: Well, again, I--at the
24 time--let's go to June 30th of this year, it was
25 my date of retirement, when we're talking about

1 that. I was--it represents my view, but it also
2 was my understanding of the OIC's view, as of
3 June 30th.

4 PETER WALSH: And what was that based
5 on?

6 JOHN HAMJE: Based upon the work that
7 I've done with the deputies and the chief deputy.

8 PETER WALSH: Have you been authorized
9 to speak on behalf of the agency here today?

10 JOHN HAMJE: No.

11 PETER WALSH: So, I guess you just
12 mentioned you're not--you're no longer with the
13 agency, correct?

14 JOHN HAMJE: That's correct.

15 PETER WALSH: And you haven't been in a
16 legal role since 2005?

17 JOHN HAMJE: That's correct.

18 PETER WALSH: Is--Annalisa Gellermann is
19 the deputy for legal affairs, correct?

20 JOHN HAMJE: That's correct.

21 PETER WALSH: And is that--that's the
22 functional equivalent of a general counsel?

23 JOHN HAMJE: She would--it could be.

24 PETER WALSH: She's the--

25 JOHN HAMJE: Some of the duties.

1 PETER WALSH: She's the top legal
2 officer of the agency.

3 JOHN HAMJE: That's correct.

4 PETER WALSH: Okay. And she's still with
5 the Office of Insurance Commissioner?

6 JOHN HAMJE: That's--to the best of my
7 knowledge.

8 PETER WALSH: Okay. Do you know why OIC
9 sent you instead of Ms. Gellermann here to
10 explain the agency's statutory interpretation?

11 JOHN HAMJE: No, I don't have any idea.

12 PETER WALSH: Did you speak with Ms.
13 Gellermann in advance of your testimony today
14 about your testimony and OIC's statutory
15 interpretation as it relates to the Zenefits
16 case?

17 JOHN HAMJE: I've not spoken to Ms.
18 Gellermann at all about my testimony.

19 PETER WALSH: When was the last time you
20 spoke with Ms. Gellermann?

21 JOHN HAMJE: It may have been... it
22 would have been sometime perhaps in the last week
23 of my employment at the Office of Insurance
24 Commissioner, perhaps at the deputy meeting on
25 Monday of that week.

1 PETER WALSH: Okay. And when was that?
2 JOHN HAMJE: I don't remember the dates,
3 but it would have been the Monday of--June 30th
4 was the Friday, so I'm looking--my eyes are not
5 that good.

6 JUDGE LISA DUBLIN: The calendar?

7 JOHN HAMJE: Yes.

8 PETER WALSH: I don't need an exact
9 date. So, it was sometime in June of--late June
10 of 2017?

11 JOHN HAMJE: I might have spoken to her
12 another time. We did have discussions from time
13 to time. You know, [UNINTEL PHRASE] can be
14 certain--I'm assuming that she attended the
15 meeting. [UNINTEL PHRASE] whether she did or not.
16 But.

17 PETER WALSH: All right, and it doesn't
18 matter. But I--but, just to be clear, you have
19 not spoken to her at all at any point in time
20 about your testimony today.

21 JOHN HAMJE: That's correct.

22 PETER WALSH: Or the positions that you
23 would take.

24 JOHN HAMJE: Well, now--

25 PETER WALSH: In this proceeding.

1 JOHN HAMJE: Well, I've talked about the
2 positions that--my positions during the
3 development of this--the matters that resulted in
4 the order we're here to talk about. But I haven't
5 discussed with her the testimony or what I would
6 say at this hearing, at all.

7 PETER WALSH: Mr. Hamje, going back to
8 another piece of your testimony, you were asked
9 why Zenefits falls into the ambit of Section 140
10 and 150. Do you recall that question?

11 JOHN HAMJE: I do.

12 PETER WALSH: And you responded, in
13 essence, three things. One, it's a producer.
14 Correct? That was one of the bases for your
15 conclusion?

16 JOHN HAMJE: Well, I don't recall my
17 specific testimony right now, but that would be
18 an important criterion.

19 PETER WALSH: In assessing whether or
20 not they were violating the statutes, in your
21 opinion, obviously, number one is they're a
22 producer.

23 JOHN HAMJE: They're a licensee.

24 PETER WALSH: Right. And the second
25 reason you cited for concluding that they were in

1 violation of these statutes is that--I think you
2 said they made no bones about making money from
3 insurance. So, that was another factor that
4 weighed into your analysis?

5 JOHN HAMJE: Well, I think that's fair
6 to say, yes.

7 PETER WALSH: And then the third that
8 you mentioned was: and that's how they pay for
9 the human resources services that they offer.

10 JOHN HAMJE: Well, now, I want--I
11 probably said that, yes, but that was certainly
12 not--does not follow the statutory language.

13 PETER WALSH: That's okay. I just
14 wanted--you mentioned those three things as the
15 factors that led you to conclude that Zenefits
16 was in violation of 140 and 150. Is there
17 anything else you'd like to add to that list?

18 JOHN HAMJE: Well, the--clearly, the
19 most important thing is that they provide free
20 services to insureds, prospective insureds, that
21 are not part of the policy they're issued. And
22 that's the most important thing.

23 PETER WALSH: All right, so that's
24 fourth. Anything else?

25 JOHN HAMJE: I'd have to look at the

1 statute to be able to review all of the
2 [UNINTEL].

3 PETER WALSH: Well--

4 JOHN HAMJE: But the statute is very
5 broad, and it provides for any type of a benefit
6 that is provided that's outside of the contract,
7 either directly or indirectly.

8 PETER WALSH: I understand your view,
9 Mr. Hamje. What I'm actually--just want to focus
10 now on the facts, if you will, the facts and
11 circumstances surrounding Zenefits [UNINTEL] in
12 violation of the statutes.

13 JOHN HAMJE: [UNINTEL] I understand
14 where you're going. So.

15 PETER WALSH: So, my question is, in
16 addition to those four things we just discussed,
17 is there any other thing that weighed in your
18 [DECISION?]?

19 JOHN HAMJE: Not that I can think of
20 right now.

21 PETER WALSH: Okay. You, in your role as
22 the deputy for consumer protection, you had no
23 responsibility for statutory interpretation,
24 correct?

25 JOHN HAMJE: I did have responsibility

1 to talk about statutes and statutory [UNINTEL],
 2 yes.
 3 PETER WALSH: Wasn't that the purview of
 4 the legal affairs division?
 5 JOHN HAMJE: Well, that was also--legal
 6 affairs also that [UNINTEL] responsibility, too.
 7 PETER WALSH: Certainly legal
 8 interpretation of the insurance code is not one
 9 of the stated and accepted responsibilities of
 10 the consumer protection [UNINTEL], is it?
 11 JOHN HAMJE: Well, that's correct.
 12 PETER WALSH: And it is clearly the
 13 responsibility of the legal affairs division.
 14 JOHN HAMJE: It can be, yes.
 15 PETER WALSH: If I may have a moment,
 16 Your Honor, just to mark something?
 17 JUDGE LISA DUBLIN: Sure.
 18 PETER WALSH: Thank you, Mr. Hamje, I
 19 apologize. I just wanted to mark a document that
 20 I'm going to hand to you here. I'll give you an
 21 opportunity to take a look at it. May I approach
 22 the witness, Your Honor?
 23 JUDGE LISA DUBLIN: Sure.
 24 MAN: [UNINTEL - OFF-MIC]
 25 PETER WALSH: Do you recognize this

1 document?
 2 JOHN HAMJE: Yes, I do. This is an
 3 organizational chart for the Office of Insurance
 4 Commissioner, dated approximately April 24, 2017.
 5 Or that's what it appears to me.
 6 PETER WALSH: And I just want to draw
 7 your attention to the beginning there. Legal
 8 affairs, this first page sets out the major
 9 departments or lead departments of the OIC,
 10 correct?
 11 JOHN HAMJE: It is.
 12 PETER WALSH: Okay. And I won't belabor
 13 this. Under legal affairs, it sets forth four
 14 responsibilities, correct?
 15 JOHN HAMJE: It does.
 16 PETER WALSH: One of which is "legal
 17 interpretation of the Insurance Code"?
 18 JOHN HAMJE: Yes.
 19 PETER WALSH: Okay. The consumer
 20 protection section, laying out its
 21 responsibilities, there's no reference to legal
 22 interpretation of the Code, is there?
 23 JOHN HAMJE: That's correct.
 24 PETER WALSH: Your Honor, I move for the
 25 admission of Exhibit CT.

1 DARRYL COLMAN: No objection.
 2 JUDGE LISA DUBLIN: All right, CT is
 3 admitted, then. Thank you.
 4 PETER WALSH: Mr. Hamje, nor does
 5 consumer protection have responsibility, at least
 6 anymore, and for some time, for conducting
 7 investigations, right?
 8 JOHN HAMJE: That's correct.
 9 PETER WALSH: Okay. And it does not have
 10 responsibility for enforcement actions either?
 11 JOHN HAMJE: That's correct.
 12 PETER WALSH: It doesn't have
 13 responsibility for antitrust?
 14 JOHN HAMJE: Antitrust?
 15 PETER WALSH: Antitrust issues? Does
 16 your unit handle antitrust issues as it relates
 17 to producers or insurers?
 18 JOHN HAMJE: No.
 19 PETER WALSH: And rate review is also a
 20 topic that's handled by other--another department
 21 of the agency? Rate review?
 22 JOHN HAMJE: Rates and forms. Rates and
 23 forms handles review of rates, yes.
 24 PETER WALSH: And that would be the
 25 department of the agency, for example, that would

1 review and approve rates and their impact on the
 2 marketplace?
 3 JOHN HAMJE: That's right.
 4 PETER WALSH: I want to turn back a
 5 little bit now, Mr. Hamje, to 2014. I think you
 6 mentioned that you--the first you recalled of the
 7 Zenefits matter was about that period of time,
 8 summer of 2014. Is that correct?
 9 JOHN HAMJE: I thought it was later
 10 [UNINTEL]. I thought it was the fall.
 11 PETER WALSH: Fall of 2014? Okay. So,
 12 let's turn back there. If you would turn, please,
 13 in your exhibit took to Exhibit F? And before we
 14 dive into that document, I just--are you aware
 15 that, in the summer of 2014, Mark Durfee
 16 responded to a complaint from a producer about
 17 Zenefits and whether or not it may be violating
 18 [UNINTEL] statutes?
 19 JOHN HAMJE: I was not aware of it
 20 until, I think, I reviewed this document.
 21 PETER WALSH: Okay. Mr. Durfee is the
 22 investigation manager at OIC?
 23 JOHN HAMJE: That's correct.
 24 PETER WALSH: And he oversees
 25 investigators, including Deb Calhoun?

1 JOHN HAMJE: When Deb Calhoun was
2 employed, yes.
3 PETER WALSH: I apologize. Deb Calhoun
4 has left the agency?
5 JOHN HAMJE: Yes.
6 PETER WALSH: And the--Durfee and the
7 investigations manager--and investigations unit,
8 they are in the legal affairs division, correct?
9 JOHN HAMJE: That's right.
10 PETER WALSH: Not your division.
11 JOHN HAMJE: That's right.
12 PETER WALSH: And, well, let me ask you,
13 at any point in time during--over the course of
14 the past several years, did you become aware that
15 Mr. Durfee had conducted a review of Zenefits in
16 connection with a complaint received by a
17 producer in the summer of 2014?
18 JOHN HAMJE: Well, I was made aware of
19 some type of a review by the manager of [UNINTEL]
20 oversight that it was conducted by
21 investigations. And perhaps this is what he was
22 referencing. I did not know the specifics of it.
23 PETER WALSH: Turn your attention,
24 please, to Page 2 of that.
25 JOHN HAMJE: Of the exhibit?

1 seen this document before your preparation for
2 this testimony today, Mr. Hamje?
3 JOHN HAMJE: I have not.
4 PETER WALSH: Sorry?
5 JOHN HAMJE: I have not.
6 PETER WALSH: You did not? You hadn't
7 seen this? Okay. Were you aware that Mr. Durfee
8 had gathered these facts and concluded that
9 Zenefits was not in violation of the statutes?
10 JOHN HAMJE: I don't think I was, no. I
11 know that there had been an investigation that I
12 understood had been closed without
13 recommendations, something like that. And I
14 assumed that perhaps this was it.
15 PETER WALSH: Okay. Let me ask you: he
16 reports there that clients are not required to
17 use Zenefits as their insurance broker to receive
18 their other services. Do you have any reason to
19 dispute that conclusion?
20 JOHN HAMJE: No.
21 PETER WALSH: And he also concludes, "A
22 client may purchase their HR and payroll services
23 a la carte, and there is no mandatory linkage of
24 non-insurance functions to the insurance-related
25 functions." Same question: any reason to dispute

1 PETER WALSH: Yes.
2 JOHN HAMJE: Exhibit F?
3 PETER WALSH: Exhibit F, Page 2. And I'm
4 looking at the email from Mark Durfee to Jeff
5 Lidstrom, which includes--Jeff Baughman is the
6 individual you discussed today. He's copied on
7 this email?
8 JOHN HAMJE: Yes, he is.
9 PETER WALSH: Okay. And I'm just going
10 to read this to you and then ask a question. So,
11 he writes to Mr. Lidstrom, who I'll purport to
12 you that the email represents is a producer, "We
13 received information from Zenefits that clients
14 are not required to use Zenefits as their
15 insurance broker to receive their other services.
16 A client may purchase their HR and payroll
17 services a la carte, and there is no mandatory
18 linkage of non-insurance functions to the
19 insurance-related functions. Further, Zenefits
20 does not provide any free, downloadable software
21 to accountholders."
22 And then the second paragraph ends, "At
23 this point, we have no information that Zenefits
24 is offering rebates or illegal inducements
25 regarding the sale of insurance." Have you ever

1 that?
2 JOHN HAMJE: No.
3 PETER WALSH: And finally, Zenefits does
4 not provide any free, downloadable software. Do
5 you have any reason to dispute that?
6 JOHN HAMJE: No.
7 PETER WALSH: I think you referenced
8 this. You're aware that Ms. Gellermann,
9 Commissioner Kreidler, and Jim Odeon met with
10 Zenefits in the fall of 2014?
11 JOHN HAMJE: That's my understanding.
12 PETER WALSH: And they were given a
13 demonstration of the platform?
14 JOHN HAMJE: I don't know exactly what
15 the nature of the meeting was about, other than a
16 meet-and-greet.
17 PETER WALSH: You weren't there? And is
18 that the meeting you expressed disappointment
19 that you hadn't been invited to?
20 JOHN HAMJE: Yes.
21 PETER WALSH: Okay. Why did you expect
22 to be invited to that meeting?
23 JOHN HAMJE: Well, I--my area is the
24 area that's responsible for compliance with
25 producers. And I would have thought that I should

1 several other colleagues, not you?
 2 JOHN HAMJE: Well, I did have input when
 3 I was a staff attorney in making changes to the
 4 forms and some of its processes. [UNINTEL PHRASE]
 5 because I was very much involved in the process.
 6 But I was not an originator of it. It was when I
 7 became staff attorney, this was something I
 8 participated in.
 9 PETER WALSH: Okay. Please turn to
 10 Exhibit J next in your book. Take a look at the
 11 second email saying, and you wrote to Ms.
 12 Gellermann on October--on December 2, and Mr.
 13 Odiorne. Based on what I understand from a
 14 business [UNINTEL], it looks like it violates
 15 140, 150 or both. So you, I think you've said--
 16 pretty much [UNINTEL] what [UNINTEL] just said.
 17 You had already, based on what you knew, drew a
 18 conclusion that it was likely a violation?
 19 JOHN HAMJE: I said it looks like it. I
 20 didn't say it was definitive.
 21 PETER WALSH: True. But based on the two
 22 things you mentioned, they give something away
 23 for free and they're a producer, that was the
 24 basis for your observation here.
 25 JOHN HAMJE: Well, producer in that they

1 were selling insurance, I mean, insurance. I
 2 mean, [UNINTEL].
 3 PETER WALSH: Those three elements were
 4 sufficient.
 5 JOHN HAMJE: Well, it was based upon
 6 what I knew at the time, [UNINTEL].
 7 PETER WALSH: And you felt pretty
 8 strongly about--that you know, you should go back
 9 and reassess Zenefits, correct?
 10 JOHN HAMJE: Well, yes. I didn't want
 11 the agency to make a mistake. I wanted to make
 12 sure it was considered before any final decision
 13 was made. I didn't think it'd been considered.
 14 PETER WALSH: So turn now, if you would,
 15 to Exhibit K, please. And here, you get another
 16 email from Dan Holst, Big I, correct, on December
 17 5, 2014?
 18 JOHN HAMJE: That's correct.
 19 PETER WALSH: And he references a
 20 meeting with Bill and me about the rebate--I
 21 assume that's Bill Stauffacher?
 22 JOHN HAMJE: Stauffacher.
 23 PETER WALSH: Stauffacher, all right.
 24 JOHN HAMJE: I'm [UNINTEL] again,
 25 Stauffacher.

1 PETER WALSH: [UNINTEL PHRASE] risk, And
 2 who is Mr. Stauffacher?
 3 JOHN HAMJE: He is the lobbyist for--and
 4 has been for some years, for the the Big I in
 5 Washington.
 6 PETER WALSH: Okay, in Washington D.C.,
 7 in Washington or Washington D.C.?
 8 JOHN HAMJE: Washington State, not D.C.
 9 PETER WALSH: Okay. And the Big I has a
 10 national affiliate, too, the IIABA?
 11 JOHN HAMJE: Yes.
 12 PETER WALSH: Okay. All right. And some
 13 of their folks have been communicating with you
 14 from time to time as well?
 15 JOHN HAMJE: Just one.
 16 PETER WALSH: Who is that?
 17 JOHN HAMJE: Wes Bissett.
 18 PETER WALSH: Wes Bissett, and he's in
 19 Washington D.C.?
 20 JOHN HAMJE: I think so.
 21 PETER WALSH: Okay. So this reflects
 22 that you had met with both Stauffacher and Holst
 23 to discuss the rebate inducement issue. When was
 24 that meeting?
 25 JOHN HAMJE: You know, I don't know what

1 meeting this is referring to. I don't think it
 2 refers to Zenefits whatsoever. I think it refers
 3 to the meet--let's see, what we were doing in
 4 2014. This was before the 2015 legislative
 5 session. So they were--and they had made
 6 proposals to make changes to our rebating
 7 inducement levels in the 2015 session.
 8 So that meeting took place concerning
 9 those proposals, when they first sat them down
 10 with me, I think [UNINTEL], our legislative rep
 11 was there. And there may have been others. So I
 12 do not recall the date of that meeting. It
 13 must've been in--within a few weeks, maybe
 14 November or October, but probably November of
 15 2014.
 16 PETER WALSH: Well, if you look at this
 17 exhibit, Mr. Hamje, the IIABW, the Big I is
 18 actually forwarding you articles about Zenefits,
 19 and in particular, Zenefits, the Utah
 20 investigation, correct? So is it fair to say that
 21 this likely meeting did involve Zenefits?
 22 JOHN HAMJE: I don't think it ever came
 23 up.
 24 PETER WALSH: At that meeting?
 25 JOHN HAMJE: At the meeting we were

1 company and concludes that they are not in
2 violation?

3 JOHN HAMJE: I am.

4 PETER WALSH: And she concludes that
5 they're not in violation because the insurance
6 and non-insurances products and services offered
7 by Zenefits are available to the general public
8 without cost, and thus concluded there is
9 inducement or relation to the insurance products
10 it offers, correct?

11 JOHN HAMJE: Would you show me where
12 you're reading--

13 PETER WALSH: Sure. The last--if you
14 look at Page 1, the second to the last line, it
15 reads, "Since the insurance and non-insurance
16 products and services offered by Zenefits are
17 available to the general public without cost and
18 there is no inducement or relation to the
19 insurance products it offers, Zenefits has not
20 violated the illegal inducement statute." Did I
21 read that correctly?

22 JOHN HAMJE: You did.

23 PETER WALSH: Will you go, please, to
24 Page 3 and I just want you to take a look at the
25 third from the last paragraph, starting from the

1 second line, "Zenefits offers a free online human
2 resources platform." Actually, skip down,
3 please. "Insurance customers get no discount on
4 premium or other special consideration." You have
5 no reason to dispute that finding, do you?

6 JOHN HAMJE: My understanding is there
7 is--I'm not aware that Zenefits can give
8 discounts on premiums.

9 PETER WALSH: And she says the user may
10 avail himself or herself of all the services
11 except insurance and the non-insurance services
12 will still be free. You have no reason to dispute
13 that either, right?

14 JOHN HAMJE: Yes, I do not dispute.

15 PETER WALSH: And at the bottom of the
16 document, the last sentence reveals that Ms.
17 Stickler also gave consideration to public policy
18 considerations?

19 JOHN HAMJE: Yes.

20 PETER WALSH: And she noted that
21 consumers would be benefited by the convenience
22 and ease of use for employee benefit management
23 unrelated to the purchase or solicitation of
24 insurance?

25 Your Honor, would it be possible to

1 take a two-minute break?

2 JUDGE LISA DUBLIN: Sure.

3 PETER WALSH: Thank you.

4 JUDGE LISA DUBLIN: We'll go off the
5 record.
6 (Break)

7 All right, we're back on the record
8 after a brief break. Before we begin, reconvene
9 cross-examination, do you want [UNINTEL PHRASE]?

10 PETER WALSH: Yes, Your Honor. Mr.
11 Hamje, in his direct testimony, offered a lot of
12 what I'd characterize as legal argument. In lieu
13 of sort of walking through and trying to address
14 it all in the course of cross-examination, what I
15 would propose and ask the Court and Mr. Colman is
16 whether the parties would be entitled to or
17 allowed to submit a post-hearing brief in which
18 we could address some of the legal issues, which
19 I think from our perspective would be more
20 efficient and hopefully more helpful for you a
21 way to address things like what does Section 157
22 mean, and the like. But I wanted to raise that
23 issue now, Your Honor, because if we don't have
24 the opportunity, then I would need to spend time
25 with him on statutory interpretation.

1 MR. COLMAN: As long as we have the same
2 opportunity, Your Honor, we're totally fine with
3 that. I think it might be better to have a
4 written opportunity so we can check the citations
5 and potentially--

6 JUDGE LISA DUBLIN: Sure.

7 MR. COLMAN:--[UNINTEL PHRASE].

8 JUDGE LISA DUBLIN: Sure, we will forego
9 oral opposing arguments and we will have written
10 closings, and we can set a deadline for that
11 after we conclude.

12 PETER WALSH: Actually, Your Honor, with
13 all due respect, I wasn't proposing it as an
14 alternative to closing. We would like an
15 opportunity to close.

16 JUDGE LISA DUBLIN: Oh.

17 PETER WALSH: Because I think it will be
18 a helpful way to pull the evidence together.

19 JUDGE LISA DUBLIN: Oh.

20 MR. COLMAN: We will--we're fine with
21 that. Our closing will be certainly short under
22 that circumstance because we would rely on our
23 brief, particularly on these essential legal
24 arguments, so...

25 JUDGE LISA DUBLIN: Sure, we can do that

1 too. [UNINTEL PHRASE] administrative [UNINTEL
2 PHRASE].

3 MR. COLMAN: I promise, Your Honor, we
4 won't flood you, but I think the thought was
5 that, you know, closing is mostly to tie it all
6 together. A post-hearing brief would give us an
7 opportunity to sort of drill into some of the
8 nuances that we've heard today that may not quite
9 be as--some of these arguments are legal, so it
10 might make sense to have a legal brief to address
11 them.

12 JUDGE LISA DUBLIN: All right, we'll
13 pick a date then tomorrow.

14 MR. COLMAN: Thank you.

15 PETER WALSH: Thank you.

16 JUDGE LISA DUBLIN: Sure.

17 MAN: Should we let Mr. Hamje back in?

18 JUDGE LISA DUBLIN: Yes, please do.

19 PETER WALSH: May I proceed, Your Honor?

20 JUDGE LISA DUBLIN: Absolutely.

21 PETER WALSH: Thank you. Before the
22 break, Mr. Hamje, we were talking, I believe,
23 about what I referred to as the Stickler memo,
24 the January 9 memo we just reviewed. You did not
25 take the Stickler memo into account in your

1 analysis of Zenefits and whether it was violating
2 the statutes, did you?

3 JOHN HAMJE: I believe that at one point
4 time in time, I did see it and I disregarded it.

5 PETER WALSH: And you are also aware
6 that a number of other states have considered
7 Zenefits' business model as well as Washington,
8 correct?

9 JOHN HAMJE: Yes.

10 PETER WALSH: Okay. And you saw copies
11 of those decisions, advisories or opinions?

12 JOHN HAMJE: I can't say I saw all of
13 them. I've seen some of them.

14 PETER WALSH: Sure. And you're aware,
15 for example, that Maryland, the state of
16 Maryland, took a look at Zenefits and concluded
17 that it was not in violation of the anti-rebating
18 statutes?

19 JOHN HAMJE: It's possible. I don't
20 recall which states have done it. I know several
21 states did it, such as Louisiana. Tennessee, I
22 think, did it, maybe a few others.

23 PETER WALSH: So, you didn't take into
24 account Louisiana or Tennessee's conclusions, was
25 that this was not violating the statute in your

1 assessment?

2 JOHN HAMJE: Well, I can't say I didn't
3 take them into account, but I think they don't
4 have applicability [UNINTEL PHRASE].

5 PETER WALSH: You rejected them?

6 JOHN HAMJE: Yes.

7 PETER WALSH: And that's because they
8 don't apply to Washington law?

9 JOHN HAMJE: They have an entirely
10 different regulatory structure in those states.

11 PETER WALSH: Have you reviewed the
12 statutes from those states, the anti-rebating and
13 inducement statutes?

14 JOHN HAMJE: I have not.

15 PETER WALSH: So, you have no reason to
16 dispute that those statutes are in material
17 respects the same as Washington's?

18 JOHN HAMJE: They may be.

19 PETER WALSH: You're aware the
20 Washington statutes is based on the NAIC Model
21 rule for anti-inducement?

22 JOHN HAMJE: I think it is, but there
23 are unique statutes in Washington that apply as
24 well that are not in any other states.

25 PETER WALSH: So, you're referring to

1 statutes other than 150 and 140?

2 JOHN HAMJE: Well, and I also gather
3 that there have been amendments to our statutes
4 that are unlike amended in other states as well,
5 and I would suspect that there have been other
6 amendments in other states that also are not in
7 our law, as well as different policies of
8 enforcement in other states. So, I'm not aware of
9 any of those kinds of things, and I was not in a
10 position to do the kind of research which was
11 appropriate for me to go ahead and do that kind
12 of research.

13 PETER WALSH: Why is not appropriate for
14 you to go ahead and do that kind of research? It
15 looks like you had already been doing plenty of
16 it.

17 JOHN HAMJE: I had been doing some
18 overall general information gathering to try to
19 get some ideas about policy for the purpose of
20 helping our legislative liaison or legislative
21 director to go ahead and present [UNINTEL] to our
22 legislature.

23 PETER WALSH: You thought it too much to
24 pull the anti-inducement and anti-rebating
25 statutes from Tennessee, from Montana, Maryland,

1 Michigan, North Carolina, Arizona, or any one of
2 those states to see if they were similar to
3 Washington's?

4 JOHN HAMJE: I did not do so.

5 PETER WALSH: You did go so far as to
6 find a 1996 Alaska Attorney General opinion to
7 consider for the public policy position you were
8 taking?

9 JOHN HAMJE: I found that, yes.

10 PETER WALSH: So, you didn't consider
11 any of the seven states and their opinions,
12 findings, Zenefits not in violation of the
13 statute?

14 JOHN HAMJE: Well, again, I considered
15 them, but I rejected them.

16 PETER WALSH: You're aware that there
17 are a number of other states that have considered
18 very similar analogous situations to Zenefits and
19 have also all concluded that there is no
20 violation when a producer is providing a benefit
21 to the--that is available to the general public?

22 JOHN HAMJE: You'll have to please be
23 more be specific. I don't know generally what
24 you're speaking about.

25 PETER WALSH: Have you ever read New

1 York State's advisory concluding that benefits
2 that a producer provides to the general public
3 does not constitute a violation of the inducement
4 statute?

5 JOHN HAMJE: Is that in one of your
6 exhibits?

7 PETER WALSH: It is.

8 JOHN HAMJE: I think I read it.

9 PETER WALSH: Okay. Did you read it back
10 in June 2015?

11 JOHN HAMJE: You know, I don't recall if
12 I did, but it made no sense for us because we had
13 gone ahead and amended our statutes specifically,
14 because our statutes are so broad so to exclude
15 wellness benefits such as were being discussed by
16 New York [UNINTEL PHRASE].

17 PETER WALSH: So, you rejected it
18 because that had to do with wellness?

19 JOHN HAMJE: Well--

20 PETER WALSH: You had a statutory
21 exception for wellness in--

22 JOHN HAMJE: It didn't apply to
23 Washington State.

24 PETER WALSH: Yeah. And you rejected
25 Louisiana's opinion as well?

1 JOHN HAMJE: Yes, I did, yeah.

2 PETER WALSH: You didn't pull the
3 statutes to review to see whether there was
4 [UNINTEL] there?

5 JOHN HAMJE: I didn't look at it.

6 PETER WALSH: And Kansas, Rhode Island
7 and Tennessee, did you review and consider their
8 opinions finding that Zenefits was not in
9 violation because--

10 JOHN HAMJE: I did not.

11 PETER WALSH: You rejected those as
12 well.

13 JUDGE LISA DUBLIN: Was that a question?

14 PETER WALSH: No, I withdraw it. Sorry,
15 Your Honor.

16 At some point in time between January 9
17 and the middle of February, do you recall that a
18 decision was made to conduct an investigation of
19 Zenefits, Ms. Stickler's memo notwithstanding?

20 JOHN HAMJE: Yes. Well, would you repeat
21 the question?

22 PETER WALSH: Sure.

23 JOHN HAMJE: I was trying to read what--

24 PETER WALSH: Sure. We don't have to
25 stay right to that. So, do you recall seeing Ms.

1 Stickler's memo in January of 2015?

2 JOHN HAMJE: I don't remember when I
3 first saw it.

4 PETER WALSH: Do you remember that
5 within the next month or six weeks an
6 investigation was opened into Zenefits?

7 JOHN HAMJE: Well, I remember that
8 sometime in January or February, an investigation
9 was begun in legal affairs of Zenefits--

10 PETER WALSH: Did you--

11 JOHN HAMJE: --as of 2015.

12 PETER WALSH: Did you have any
13 involvement in the decision to conduct an
14 investigation?

15 JOHN HAMJE: I believe I was a part of
16 the deputy team, or the executive management
17 team, or whatever decision was made [UNINTEL
18 PHRASE].

19 PETER WALSH: Who was at that meeting?

20 JOHN HAMJE: Well, you know, this was
21 several years ago. I attended so many of those
22 meetings, I don't recall. If it was a deputy
23 meeting, it would've been the deputies and the
24 chief deputy for each of their areas. If it were
25 the executive management team, it would have been

1 a commissioner and, as I said, the assistants and
 2 all of the deputies.
 3 PETER WALSH: Who made the decision to
 4 reject the Stickler memo and launch a formal
 5 investigation?
 6 JOHN HAMJE: I don't know they made a
 7 decision to reject the memo. I just knew that
 8 that that at the time, disregarded.
 9 PETER WALSH: What was your position at
 10 that executive management team meeting in
 11 January-February where the investigation was
 12 launched?
 13 PETER WALSH: I believe we needed to do
 14 an investigation of Zenefits to figure out fully
 15 and finally whether or not it was in violation
 16 and what action we should take, if there is a
 17 violation.
 18 PETER WALSH: But you had already
 19 concluded, based on what you knew at the time,
 20 you thought they were in violation--
 21 JOHN HAMJE: I said that it looked like
 22 there was a violation, and so that supported an
 23 investigation.
 24 PETER WALSH: What else do you remember
 25 about this meeting at which Ms. Stickler's memo

1 was rejected at a formal investigation?
 2 JOHN HAMJE: Well, again, I don't
 3 remember a meeting where there was a rejection of
 4 her memo.
 5 PETER WALSH: Okay, I won't characterize
 6 it that way. There was a meeting sometime between
 7 January 9th and--let me--[UNINTEL PHRASE] go to
 8 Exhibit W, please. And this is an interoffice
 9 memo from AnnaLisa Gellermann to Mark Durfee, and
 10 [UNINTEL PHRASE]--
 11 JOHN HAMJE: [UNINTEL PHRASE]
 12 PETER WALSH: From?
 13 JOHN HAMJE: Mark Durfee.
 14 PETER WALSH: From Mark Durfee to
 15 AnnaLisa Gellermann. Thank you. And dated
 16 February 23. And if you go to the bottom of that,
 17 it indicates that--basically, this is launching
 18 an investigation, correct? Is this a memo
 19 commencing investigation?
 20 JOHN HAMJE: Well, I'm not familiar with
 21 these forms. This is not a form that I'm familiar
 22 with. Let me read the whole thing and then I can--
 23
 24 PETER WALSH: I'm sorry. I don't need
 25 that answer, but you're not familiar with it

1 because that's a function of legal, correct?
 2 JOHN HAMJE: Yes, it is a function of
 3 legal affairs to engage in investigations.
 4 PETER WALSH: Okay. Well, I just direct
 5 your attention down to the bottom of Page 1, if
 6 you will. And it says, second to last line of
 7 paragraph, "Information about Zenefits'
 8 operations was subsequently discussed by the
 9 OIC's Executive Management Team and it was
 10 determined that further inquiry into Zenefits'
 11 operations was needed."
 12 Now, that does refresh your
 13 recollection at all about a meeting of the
 14 Executive Management Team?
 15 JOHN HAMJE: Well, I'm assuming if Mr.
 16 Durfee were correct that there had been an
 17 Executive Management Team meeting where this was
 18 discussed, I would agree with it. But I'm not
 19 absolutely sure that that would necessarily be
 20 the case. Mr. Durfee was not necessarily present
 21 at it. He may have gotten confused between a
 22 deputy meeting and an executive management team
 23 meeting. I can't be certain of that. I do not
 24 recall which it was. It could have been either
 25 one.

1 PETER WALSH: Well, whether it was an
 2 EMT meeting, a deputies meeting or otherwise, you
 3 do recall there was a meeting of the senior
 4 deputies to discuss benefits, around this time
 5 period in particular, whether or not to conduct
 6 an investigation?
 7 JOHN HAMJE: I do.
 8 PETER WALSH: And tell me what you
 9 recall about that meeting.
 10 JOHN HAMJE: Well, I don't recall
 11 specifics about it. I just recall that it
 12 occurred and a decision was made to go forward
 13 with an investigation.
 14 PETER WALSH: Was the Commissioner
 15 there?
 16 JOHN HAMJE: Well, if it was an
 17 executive management team meeting, yes, he would
 18 have been there.
 19 PETER WALSH: What was the--whether
 20 reflected at that meeting or otherwise, what was
 21 the Commissioner's position in January-February
 22 of 2015 about Zenefits?
 23 JOHN HAMJE: I don't know what his
 24 position was.
 25 PETER WALSH: He had received a

1 [UNINTEL] and AnnaLisa Gellman in the fall,
2 correct?

3 JOHN HAMJE: That's what I--that's what
4 you've represented to me. I don't know what
5 occurred at that meeting.

6 PETER WALSH: Did you ever speak to the
7 Commissioner about Zenefits directly?

8 JOHN HAMJE: I did not.

9 PETER WALSH: You don't recall who was
10 at this meeting and you recall no other specifics
11 besides what you've described?

12 JOHN HAMJE: That's correct.

13 PETER WALSH: And you don't know the
14 basis for the decision to launch an
15 investigation?

16 JOHN HAMJE: Well, I think that what
17 I've articulated, that there was essentially
18 violations that needed further investigation.

19 PETER WALSH: That's what you thought?

20 JOHN HAMJE: That's my understanding,
21 right.

22 PETER WALSH: You don't know why this
23 group--you don't what the decision--why the
24 decision was made at that meeting?

25 JOHN HAMJE: I don't recall any

1 statement being made, nor do I know what each of
2 the other deputies or the Commissioner [UNINTEL
3 PHRASE] present were thinking.

4 PETER WALSH: Do you have any other
5 circumstance where the EMT or the senior deputies
6 rejected the advice of the legal department?

7 JOHN HAMJE: Not off hand.

8 PETER WALSH: Staying on this document
9 for a moment, if you would, and if you'd flip to
10 the second page, please. This document, a variety
11 of its actions, legal authorities, and prosed
12 investigative authority, I don't want to spend a
13 ton of time on this, Mr. Hamje, but in the
14 section entitled Proposed Investigative Activity,
15 the beginning says, "In accordance with OIC
16 standard investigative protocol", did you
17 understand that there was a standard
18 investigative protocol in investigations and
19 legal affairs?

20 JOHN HAMJE: I think Mr. Durfee had gone
21 ahead an implemented [UNINTEL] protocol.

22 PETER WALSH: And if you look down to
23 the bottom of that section, the recommendation
24 here from Ms. Gellman is that, "After completing
25 all of the investigative steps necessary, derive

1 logical conclusions based on the evidence of
2 obtained, a final investigative report is
3 prepared. The report includes findings as to
4 whether a violation of laws occurred and all of
5 the evidence gathered to support the
6 investigative finding."

7 Is it your understanding that that was
8 standard investigative protocol?

9 JOHN HAMJE: No, I'm not familiar with
10 that part, so I can't answer.

11 PETER WALSH: And then, down in the
12 recommendations section, it says, again, "In
13 accordance with standard operating procedures, it
14 is recommended that the final investigative
15 report before from the Investigations Unit to the
16 Legal Affairs Program Manager for review and the
17 findings--that the findings indicate that a
18 possible violation of the insurance code has
19 occurred. It is further recommended that the case
20 be assigned to an OIC staff attorney for possible
21 enforcement action." Do you see that?

22 JOHN HAMJE: Yes. And you did skip a
23 word--

24 PETER WALSH: Oh.

25 JOHN HAMJE: --and I think it's

1 important. It's the Legal Affairs Litigation
2 Program Manager.

3 PETER WALSH: Okay.

4 JOHN HAMJE: That's a--

5 PETER WALSH: I apologize.

6 JOHN HAMJE: That's a separate position.
7 Yes, I do see all that.

8 PETER WALSH: That process was not
9 followed in this case, was it?

10 JOHN HAMJE: No, it was not.

11 PETER WALSH: And there's no reference
12 to a role for you or Consumer Protection in this
13 memo?

14 JOHN HAMJE: Not that I'm aware of.

15 PETER WALSH: You have no reason to
16 believe that AnnaLisa Gellermann did not accept
17 Mark Durfee's recommendation for how to proceed
18 with this investigation?

19 JOHN HAMJE: That's correct.

20 PETER WALSH: Do you know what Ms.
21 Gellerman thought about the rejection of Ms.
22 Stickler's memo and the launching of an
23 investigation to support it?

24 JOHN HAMJE: Would you repeat that?

25 PETER WALSH: I'm sorry, that was a bad

1 whatsoever.

2 PETER WALSH: The investigation was

3 being led by Legal Affairs, correct?

4 JOHN HAMJE: Correct.

5 PETER WALSH: And by the investigations

6 under the auspice of Ms. Gellerman?

7 JOHN HAMJE: Yes.

8 PETER WALSH: And you didn't, for

9 example, speak to anybody during the-- I'm going

10 to focus now on the time period of February 2015

11 to September 2015. During that time did you speak

12 to anybody at Zenefits?

13 JOHN HAMJE: I don't think so.

14 PETER WALSH: Okay. You didn't conduct

15 any interviews with his Zenefits' customers?

16 JOHN HAMJE: I did not.

17 PETER WALSH: Okay. Did you have any

18 involvement with Ms. Calhoun's investigation?

19 JOHN HAMJE: It's possible that Ms.

20 Calhoun may have called me to ask me a question

21 or two, but I don't recall if she did.

22 PETER WALSH: Why would she call you?

23 JOHN HAMJE: She may have wanted some

24 information about producers or how producers

25 operate, or something like that. But I don't

1 what I needed to understand what the facts were.

2 PETER WALSH: From a couple of them?

3 JOHN HAMJE: Well, there was a lot more

4 in the investigative [UNINTEL PHRASE].

5 PETER WALSH: Would you skip ahead,

6 please, to Exhibit AH? And this, we're into July

7 2015 now, and here's Dan Holst again, "Out of

8 curiosity, have you heard anything on your

9 department's response to Zenefits?" And above,

10 again, you informed him that the investigation is

11 continuing? Is that a fair characterization?

12 JOHN HAMJE: Yes.

13 PETER WALSH: Okay. So, here, you

14 inquire--you ask him to share with you what other

15 state departments are looking at, under state

16 department's insurance, correct?

17 JOHN HAMJE: Yeah, in response to a

18 statement he makes in his email to me.

19 PETER WALSH: Yeah. So, you are

20 interested in any information that the Big I

21 might provide about what other states were doing,

22 but you disregarded the other state advisories

23 finding that Zenefits was in violation?

24 JOHN HAMJE: Well, I disregarded them

25 after reviewing them, but if there was any

1 recall a specific one. But I don't want to in any

2 way mislead. So, it's possible that she may have.

3 She probably would have a better recollection

4 [UNINTEL PHRASE].

5 PETER WALSH: And you don't have any

6 yourself, so you don't the questions you asked.

7 You don't know the questions she asked Zenefits'

8 customers?

9 JOHN HAMJE: No, I do not. Not until I

10 saw the report.

11 PETER WALSH: Okay. Referring to the

12 final investigative report?

13 JOHN HAMJE: Yes.

14 PETER WALSH: Okay. Did you read her

15 investigation memoranda, her witness interviews?

16 JOHN HAMJE: I read some of them. I

17 don't know if I read every single one of them.

18 PETER WALSH: You didn't read all of

19 them?

20 JOHN HAMJE: No.

21 PETER WALSH: You didn't think it was

22 important to read all of them and find out what

23 Zenefits' customers thought about Zenefits, the

24 products, the free services?

25 JOHN HAMJE: I thought I got the gist of

1 information that other state departments were

2 taking action on, I wanted to hear about it and

3 share it with people internally.

4 PETER WALSH: Skip ahead, please to

5 Exhibit AJ. This is an email chain, August 20th

6 to 21st, and it looks--again, here's Dan Holst

7 reaching out to you. Oh, Bill Stauffacher as

8 well. They'd like to meet with you to discuss the

9 Zenefits rebating issue, and you passed it on to

10 AnnaLisa Gellermann. And it appears around this

11 time there's a draft final investigative report

12 close to complete?

13 JOHN HAMJE: There was.

14 PETER WALSH: Okay. And if you flip the

15 page to AK, it looks like Ms. Gellerman is saying

16 she's hoping that final investigative report

17 might be done in time for a deputies meeting, and

18 she suggests she might promise to the Big I an

19 imminent decision. Is that fair?

20 JOHN HAMJE: If--what did it say? Yes, I

21 think that's fair.

22 PETER WALSH: Did you let--did you

23 promise Big I an imminent decision?

24 JOHN HAMJE: I do not believe I did.

25 PETER WALSH: Okay. Following on Exhibit

1 AL, so continuing in a chain here, Ms. Gellerman
2 says, "It would be interesting to have a
3 conversation with them"--I think that's with Big
4 I, [UNINTEL] to characterize this--"after we
5 received a report before they announced our
6 decision. What do you think of that?" What do you
7 think of that? Do you think it's appropriate to
8 share with the Big I preliminary findings before
9 they have been announced?

10 JOHN HAMJE: No, I thought it was close
11 call.

12 PETER WALSH: In any event, you do meet
13 with the Big I in early September. Do you have a
14 recollection of that?

15 JOHN HAMJE: [UNINTEL] what would this
16 meeting be about?

17 PETER WALSH: Well, I think I can help
18 you refresh your recollection. If you move up to
19 Exhibit AO, please, which is an email dated
20 September 10th. And you wrote to Ms. Gellerman,
21 that "Holst and Big I wanted to--again asked to
22 visit by conference call concerning Zenefits as
23 well as rule making." And then in the second
24 paragraph, "Of course, all they wanted to talk
25 about was Zenefits." Then you report to her

1 you're concerned the investigation's taking way
2 too long and our inaction is having an adverse
3 effect on Washington producers. Why are you so
4 concerned? Isn't it more important to have a
5 thorough and complete investigation?

6 JOHN HAMJE: Well, I have to say that I
7 think I was being unreasonable in saying that at
8 that point in time. Normally, the investigation
9 target is 120 days to complete an investigation.
10 This was taking much longer. I guess I think it
11 shows some frustration on my part for not having
12 any determination [UNINTEL]. But I agree that it
13 is absolutely critical to have due diligence and
14 have a good and full complete investigation of
15 the facts, which is what I think occurred.

16 PETER WALSH: Yeah, and I think you
17 actually testified to that on direct that it's
18 important to have all the facts, to have an
19 established process.

20 JOHN HAMJE: An established process for
21 what?

22 PETER WALSH: For reviewing a matter,
23 conducting an investigation, considering the
24 legal implications of it in the course of the
25 matter.

1 JOHN HAMJE: Well, I think so, yeah.

2 PETER WALSH: And it's important to
3 understand, I think you said, not only the
4 consequences but the unintended consequences of
5 agency action?

6 JOHN HAMJE: [UNINTEL PHRASE]

7 PETER WALSH: So, anyway, it looks like
8 you met again with them on the 10th of September.
9 And if you flip ahead to AQ, just quickly,
10 there's another--you're reporting to a larger
11 group of executives about the meeting with the
12 Big I. Obviously, no surprise, the Big I believes
13 it violates the [UNINTEL] violation. And it looks
14 like at that point, the Big I was threatening to
15 obtain--they wanted to--they said if no action
16 was taken, they wanted permission to adopt
17 Zenefits' business model?

18 JOHN HAMJE: Would you help me speed
19 things--

20 PETER WALSH: Sure.

21 JOHN HAMJE: --up by pointing that out?

22 PETER WALSH: First paragraph, third-
23 fourth line.

24 JOHN HAMJE: I guess, yeah, that's
25 something--in fact that I heard that on a number

1 of instances from [UNINTEL] that had asked
2 questions or commented--

3 PETER WALSH: And did that sort of
4 factor into the agency's decision?

5 JOHN HAMJE: Well, it's what I would
6 expect. You know, if you're--I don't know exactly
7 how to answer the question, but factoring is--it
8 didn't accelerate our efforts or cause us to
9 accelerate our efforts, but it is something that
10 if you're going to have a level playing field,
11 you should make a decision to go one way or the
12 other way. So, if we're going to go and bless the
13 Zenefits' model, then everybody should be able to
14 use it. Otherwise, it's not fair.

15 PETER WALSH: I'm going to skip out of
16 order here because there are some docs that
17 didn't have a date on them. So, we're in early
18 September, and at this point I think the
19 documents show us that at least Gellermann and
20 Durfee thought that that final investigative
21 report was imminent, correct?

22 JOHN HAMJE: I think it was finally
23 rendered in October.

24 PETER WALSH: Okay. But the emails we
25 were looking at in August, there was some

1 department is response for enforcement actions,
2 correct?

3 JOHN HAMJE: Yes.

4 PETER WALSH: And so it is -- the
5 process dictates that once a final investigated
6 report is done, it's referred over to a staff
7 member to pursue an enforcement action if it
8 turns out that the recommendation to finding a .
9 violation has occurred.

10 JOHN HAMJE: I think the ordinary case
11 [UNINTEL PHRASE].

12 PETER WALSH: And this was not an
13 ordinary case?

14 JOHN HAMJE: I do not believe it was.

15 PETER WALSH: Why did you depart from
16 the standard procedure here?

17 JOHN HAMJE: This was the case where we
18 were still wrestling with the situation [UNINTEL
19 PHRASE].

20 PETER WALSH: And you were more capable
21 than Ms. Gellermann of understanding it?

22 JOHN HAMJE: Well, I don't know if I can
23 say that I'm more capable of understanding it. I
24 think that because of my background and
25 expertise, it was thought that I would be the

1 best person to lead the effort.

2 PETER WALSH: No, Ms. Stickler handled
3 the audit and a rebating and anti-inducement
4 investigations over her 10 years with the agency,
5 didn't she?

6 JOHN HAMJE: I do not know.

7 PETER WALSH: You don't know the degree
8 of her--the depth of her experience in that area?

9 JOHN HAMJE: I do not.

10 PETER WALSH: Mr. Hamje, if a decision
11 is made that they're in violation, which has not
12 been memorialized, which we don't have, why then
13 are you sometime after October 5 engaging in a
14 pro-and-con analysis of the implications of
15 finding Zenefits in violation?

16 JOHN HAMJE: Well, we're trying to
17 determine what the impact of any decision that
18 were made could be.

19 PETER WALSH: Go back to your previous
20 comment and the decision to allow you to continue
21 this inquiry. Talk about your background and your
22 expertise. What background and expertise in the
23 previous 10, 12 years at the agency have you had
24 in legal analysis?

25 JOHN HAMJE: Your question [UNINTEL

1 PHRASE] of my experience just to the last 10 or
2 15 years.

3 PETER WALSH: You're not in the legal
4 [UNINTEL].

5 JOHN HAMJE: Well, I'm not, not as a
6 deputy for consumer protection.

7 PETER WALSH: But you were more
8 qualified to conduct the remaining investigation
9 and analysis.

10 JOHN HAMJE: Well, it wasn't necessarily
11 a legally-based based investigation. It was more
12 of time to understand what the OIC's position
13 should be and what the impact of its decision,
14 what it might be.

15 PETER WALSH: That may explain why
16 there's no legal analysis in any of the OIC's
17 record on this case.

18 JOHN HAMJE: Pardon me?

19 PETER WALSH: That may explain why
20 there's no legal analysis in any of OIC's record
21 in this case.

22 JOHN HAMJE: I can't answer that.

23 PETER WALSH: You acknowledged that
24 there were some problems with finding Zenefits in
25 violation of the statutes, right? This wasn't

1 clean cut.

2 JOHN HAMJE: I'm not sure what you mean
3 by problems about finding--

4 PETER WALSH: Well, ruling in against
5 Zenefits could be viewed as counterintuitive, at
6 least as far as consumers are concerned.

7 JOHN HAMJE: Well, I think that's an
8 important thing to consider when talking about
9 the [UNINTEL PHRASE] is if they are on the
10 surface counterintuitive, because they don't seem
11 to be directly [UNINTEL PHRASE] to help the
12 consumers. They seem to be denying consumers the
13 ability to get free benefits.

14 PETER WALSH: You concluded that it
15 could be counterintuitive to find Zenefits in
16 violation, because they were providing benefits
17 to consumers that you would take away.

18 JOHN HAMJE: Yes, and that may have been
19 one of the columns that I put together in my
20 notes.

21 PETER WALSH: And you also realized that
22 Washington IOC [UNINTEL PHRASE] taking
23 enforcement action.

24 JOHN HAMJE: Well, I think at that time
25 that may have been the case.

1 PETER WALSH: And is it not the case
2 today?
3 JOHN HAMJE: I don't know.
4 PETER WALSH: You don't know. You also
5 knew that--you thought that OIC would be accused
6 of standing in the way of progress?
7 JOHN HAMJE: I think that was one of the
8 columns, yes.
9 PETER WALSH: [UNINTEL] consumer?
10 JOHN HAMJE: Excuse me?
11 PETER WALSH: [UNINTEL PHRASE] consumer?
12 JOHN HAMJE: I think that was one of the
13 columns.
14 PETER WALSH: And [UNINTEL PHRASE]?
15 JOHN HAMJE: [UNINTEL PHRASE].
16 PETER WALSH: [UNINTEL].
17 JOHN HAMJE: Yes, [UNINTEL] competitive
18 protector of producers.
19 PETER WALSH: Yep, it would be viewed as
20 protective of producers.
21 JOHN HAMJE: That's correct.
22 PETER WALSH: And bad publicity. Did you
23 do any investigation or talk to anybody about
24 whether in fact the action might be anti-
25 consumer?

1 expected, by the producer community?
2 JOHN HAMJE: That's correct.
3 PETER WALSH: And you factored that
4 expectation into your decision?
5 JOHN HAMJE: Their understanding of the
6 law is the [UNINTEL].
7 PETER WALSH: [UNINTEL]. And you also
8 claimed that taking action would be consistent
9 with the policy purpose of the statute--any
10 policy purpose to the statute advanced by taking
11 action against Zenefits, besides the ones you've
12 mentioned today?
13 JOHN HAMJE: Well, those are the main
14 ones that are mentioned.
15 PETER WALSH: And then you've got your
16 level playing field here too, correct? That was
17 another consideration?
18 JOHN HAMJE: And you're responding to
19 Page 3 now of [UNINTEL]?
20 PETER WALSH: I am.
21 JOHN HAMJE: Yes.
22 PETER WALSH: Mr. Hamje, you're weighing
23 the pros and cons of the enforcement action
24 against Zenefits, are you not?
25 JOHN HAMJE: Well, no, I was not

1 JOHN HAMJE: No, I did not. That was
2 just on my list of pros and cons. That was one of
3 the comments.
4 PETER WALSH: And did you talk to any of
5 Zenefits' customers to find out how they may be
6 impacted by the decision?
7 JOHN HAMJE: No.
8 PETER WALSH: Small businesses that
9 would have to pay more for services they received
10 for free?
11 JOHN HAMJE: No.
12 PETER WALSH: You didn't talk to them?
13 JOHN HAMJE: I didn't talk--considered
14 the impact of it.
15 PETER WALSH: You knew there was
16 possible--not only there was--it would be viewed
17 as taking counterintuitive statutes standing in
18 the way of progress, but in fact it would be
19 viewed and the fact could be very well be
20 reasonably considered to be standing in the way
21 of progress.
22 JOHN HAMJE: I think that is inaccurate.
23 PETER WALSH: On the other hand, Mr.
24 Hamje, you knew in the pro column that taking
25 action against Zenefits would support, if not

1 actually. The deputies were. What I did was lay
2 this all out for the deputies [UNINTEL PHRASE].
3 PETER WALSH: In the spring of 2016?
4 JOHN HAMJE: Yes.
5 PETER WALSH: So the deputs are still
6 trying to decide whether an enforcement action
7 against Zenefits is appropriate.
8 JOHN HAMJE: Well, what opposition to--
9 well, well, at that point in time they'd been
10 pretty well excited that we were going to
11 [UNINTEL]. I wanted to make sure and I was--I
12 felt like it was important to go through and talk
13 about the pros and cons before we take any steps.
14 PETER WALSH: But you had been tasked in
15 October to decide how to move forward.
16 JOHN HAMJE: No, not to decide. I was
17 tasked to make--developing recommendations to
18 bring to the [UNINTEL].
19 PETER WALSH: And did you bring
20 recommendations?
21 JOHN HAMJE: I did.
22 PETER WALSH: What was that
23 recommendation?
24 JOHN HAMJE: It was to move forward.
25 PETER WALSH: Did you put that in

1 writing?
 2 JOHN HAMJE: I don't believe I did,
 3 other than these notes.
 4 PETER WALSH: Did you--
 5 JOHN HAMJE: These are not submitted.
 6 These are just [UNINTEL PHRASE].
 7 PETER WALSH: You didn't provide these
 8 notes to the deputies?
 9 JOHN HAMJE: No.
 10 PETER WALSH: You didn't put the pros
 11 and consider in any--you didn't memorialize them
 12 and share them with your colleagues?
 13 JOHN HAMJE: I did not.
 14 PETER WALSH: Did you--
 15 JOHN HAMJE: I shared them orally.
 16 PETER WALSH: And you also, I believe,
 17 during this time period, you testified in direct
 18 you were looking into Section 157, whether that
 19 might apply.
 20 JOHN HAMJE: Well, see, that--
 21 PETER WALSH: It's just yes or no. You
 22 were looking at 157?
 23 JOHN HAMJE: Before I made these
 24 recommendations.
 25 PETER WALSH: Right, between October

1 2015 and this meeting in the spring of 2016.
 2 JOHN HAMJE: [UNINTEL].
 3 PETER WALSH: You did some research into
 4 Section 157?
 5 JOHN HAMJE: I looked at 157 to make
 6 sure, to determine whether or not that was--
 7 whether that applied to this.
 8 PETER WALSH: And you assessed whether
 9 or not there would be other statutory exceptions
 10 to 140 and 150?
 11 JOHN HAMJE: [UNINTEL PHRASE] any place
 12 where I wanted to look.
 13 PETER WALSH: Where's that [UNINTEL]??
 14 JOHN HAMJE: It's not, that I know of.
 15 PETER WALSH: And did you present the
 16 results of that research to the deputies meeting?
 17 JOHN HAMJE: Yes. We shared with the
 18 deputies what we found out. [UNINTEL PHRASE].
 19 PETER WALSH: We were doing the legal
 20 research, not the legal [UNINTEL].
 21 JOHN HAMJE: Wasn't legal research. It
 22 was just talking about what we found, what we
 23 hadn't found.
 24 PETER WALSH: What else did you do
 25 during that six-month period between October and

1 the spring of 2016 [UNINTEL PHRASE]??
 2 JOHN HAMJE: Well, one of the [UNINTEL
 3 PHRASE] we worked--well, first of all, we met
 4 with Zenefits on two occasions. And I think I've
 5 already testified about that. And during that
 6 process, we determined that our 483157 was
 7 probably the [UNINTEL PHRASE] potential for
 8 compliance for taking any action [UNINTEL PHRASE]
 9 compliant with Section 483157.
 10 So one of the concerns that was raised
 11 was what would be the impact on the marketplace
 12 if we were to go in and enforce this law, because
 13 we had not dealt in a controversy before, at
 14 least in my experience at the agency, of using
 15 this particular statute.
 16 So we had concerns about what the
 17 market impact may be and what would happen out
 18 there. We were not sure if it was something that
 19 was already being used by producers, which was
 20 something that was commonly [UNINTEL] and known.
 21 So I was asked--and I think I mentioned this
 22 before--I was asked to talk to the two producers
 23 about the market. And this was a meeting that
 24 would have with our group of AnnaLisa Gellermann,
 25 Leslie Krier, and Doug Hartz.

1 PETER WALSH: I'm going to ask you to go
 2 through [UNINTEL PHRASE] why don't we close the
 3 group. I don't want to [UNINTEL] refreshing your
 4 recollections of the documents in front of you.
 5 You did meet--
 6 JOHN HAMJE: I've already testified--
 7 PETER WALSH: Right, and I appreciate
 8 that. To be clear, during the course of the six
 9 months between the assigning of this case to you
 10 and the spring of 2016, you met on a number of
 11 occasions with the Big I--Dan Holst, Chris Free,
 12 other producers as well as the Big I.
 13 JOHN HAMJE: Well, just those are the
 14 ones for the purpose of accounting were trying to
 15 determine what the impact might be on the market
 16 [UNINTEL PHRASE].
 17 PETER WALSH: And you had a call with
 18 Dan Holst and Wes Bissett in February 2016. Do
 19 you recall that?
 20 JOHN HAMJE: I do.
 21 PETER WALSH: And Dan Holst said don't--
 22 let's take a look at that. Go back to BJ, please.
 23 Take a look at Page 10.
 24 JOHN HAMJE: You looking at Page 8?
 25 PETER WALSH: I am, yeah. And so at the

1 very top, this, I believe, reflects the
2 conversation you had with Dan Holst and the Big
3 I. He says, "Don't open a can of worms"--157. So
4 I assume you're talking with Dan about the
5 interpretation of Section 157.

6 JOHN HAMJE: Where is that? I'm not
7 seeing that.

8 PETER WALSH: Very top of Page 10 of
9 Exhibit BJ.

10 JOHN HAMJE: Oh, Page 10. Yes, I don't
11 recall the content [UNINTEL PHRASE].

12 PETER WALSH: So you're still doing
13 statutory analysis here and trying to determine
14 whether or not there's a 157 exception [UNINTEL]
15 on this.

16 JOHN HAMJE: Well, no, I'm trying to
17 determine whether or not--what the impact on the
18 market would be if we used 157 and--or not or
19 used some other approach. The questions--the
20 discussion that I had with Mr. Holst and Mr.
21 Bissett was not very useful. What I have tried to
22 do is ask open-ended questions. I mostly got
23 rhetoric back, is what I received. And so it was
24 not very [UNINTEL]. So this is not something that
25 I would say would rise to the level of a

1 statutory interpretation.

2 PETER WALSH: No surprise, it's Dan
3 Holst and Wes Bissett who are responsible for
4 being Big I's government affairs across the
5 country in a nationwide basis, right? That's
6 their job.

7 JOHN HAMJE: Mr. Bissett is.

8 PETER WALSH: Bissett.

9 JOHN HAMJE: And has some
10 responsibility. Mr. Holst is from the [UNINTEL
11 PHRASE].

12 PETER WALSH: And fair to assume that
13 Mr. Bissett was engaged with other state
14 [UNINTEL] about Zenefits, right?

15 JOHN HAMJE: I would not be surprised.

16 PETER WALSH: Law [UNINTEL] defined
17 Zenefits in violation in those standards.

18 JOHN HAMJE: Like I said, I would not be
19 surprised. I don't have personal knowledge of it,
20 but I would not be surprised.

21 PETER WALSH: And he was undoubtedly
22 aware of Montana's decision, Maryland's decision,
23 North Carolina's decision Zenefits was not in
24 violation of [UNINTEL PHRASE]?

25 JOHN HAMJE: No. I cannot speak to what

1 he was aware of or what he was not aware of.

2 PETER WALSH: Did you ask him were you
3 aware of those decisions?

4 JOHN HAMJE: I don't recall.

5 PETER WALSH: You don't recall. [UNINTEL
6 PHRASE]. Did you ask Mr. Bissett whether those
7 decisions, those other states that would open the
8 can of worms in those states?

9 JOHN HAMJE: I don't know. I don't
10 recall.

11 PETER WALSH: What the impact on the
12 market was in the other states, the other 49
13 states where Zenefits was legal?

14 JOHN HAMJE: Again, neither of these
15 gentlemen were producers. I really did not think
16 asking those kinds of market [UNINTEL] questions
17 was going to be useful to me.

18 PETER WALSH: Did you call any of your
19 colleagues in other DOIs across the country to
20 get their views on the impact that Zenefits might
21 have on the marketplace?

22 JOHN HAMJE: I did not.

23 PETER WALSH: Your Honor, would we be
24 able to take a break for a few minutes?

25 JUDGE LISA DUBLIN: Yeah.

1 PETER WALSH: Thank you.

2 JUDGE LISA DUBLIN: We'll go off the
3 record for 10 minutes.

4 (OFF THE RECORD)

5 JUDGE LISA DUBLIN: All right, we're
6 back on the record after a break.

7 PETER WALSH: Your Honor, we'd like to
8 do this earlier. I'd like to move for admission
9 of Exhibit AT.

10 DARRYL E. COLMAN: [UNINTEL] overruled
11 my objection.

12 JUDGE LISA DUBLIN: Oh, [UNINTEL] that I
13 flip to it is that the [UNINTEL PHRASE].

14 DARRYL E. COLMAN: It is.

15 JUDGE LISA DUBLIN: All right, other
16 than--anything else to add?

17 PETER WALSH: No.

18 DARRYL E. COLMAN: My only concern was
19 the attorney [CLIENT?].

20 JUDGE LISA DUBLIN: All right, AT is
21 admitted, thank you.

22 PETER WALSH: Mr. Hamje, I just got two
23 topics to run by you and then we'll be closed at
24 the finish here--we'll be at the finish line
25 here. I want to turn ahead now in time. I want to

1 turn ahead to the summer of 2016.
2 And first of all, you said there was a
3 time in--let me [UNINTEL PHRASE] first of all, I
4 want to talk about the final investigative
5 report. And then we're going to turn for a moment
6 just to wrap up on the value of consistency and I
7 want to talk about how this case compares to some
8 other similar cases.

9 But it's really up to the final
10 investigative report. I just want to make sure I
11 understand your testimony. You had testified, I
12 believe, on direct when you regrouped the
13 deputies sometime in the spring of 2016 to
14 address once again what to do with Zenefits?

15 JOHN HAMJE: I don't think it was 2016.
16 I thought it was--I know--yes, you're right. It
17 was in 2016, sometime in the spring of 2016.
18 There was a deputy aware--I presented the
19 recommendations and determined [UNINTEL PHRASE]
20 to look over the legal, to go ahead and move
21 forward with [UNINTEL].

22 PETER WALSH: Yeah, that was the meeting
23 we talked about a few minutes ago on the break,
24 where there were--there's no documentation of
25 that meeting, correct?

1 JOHN HAMJE: Well, documentation on
2 order.

3 PETER WALSH: Okay. And a decision was
4 made to transition it back to legal at that point
5 in time? Okay. And what exactly occurred between
6 October and--had you done anything during that
7 period of time, such as you described?

8 JOHN HAMJE: Well, no, we did actually
9 look up all those things we talked about all of
10 this morning and this afternoon.

11 PETER WALSH: So it goes back to legal
12 and you have little to no involvement following
13 that point in time?

14 JOHN HAMJE: I'm pretty much off the
15 case.

16 PETER WALSH: Okay. Can you turn to
17 Exhibit AZ, please? So this appears to be the
18 final investigate report--another final
19 investigative report, dated August 1, 2016. Have
20 you ever seen this before?

21 JOHN HAMJE: No, I haven't. And now what
22 I was referring to then must have been a draft in
23 my office. It probably had a blank just like the
24 one [UNINTEL PHRASE]. So I want to make it
25 [UNINTEL PHRASE] that what I have probably is

1 what would [UNINTEL PHRASE] was the final
2 investigative report.

3 PETER WALSH: So it's not accurate to
4 say that a decision had been made and a finding--
5 there had been a legal analysis and a finding
6 that Zenefits was in violation in 2015?

7 JOHN HAMJE: I think that's right. I
8 [UNINTEL PHRASE].

9 PETER WALSH: So why was the case
10 assigned to you?

11 JOHN HAMJE: To go ahead and try to
12 develop a position and to try to bring--find an
13 exception that Zene fits was [UNINTEL].

14 PETER WALSH: There's no legal analysis
15 in this report.

16 JOHN HAMJE: Without reading the entire
17 thing, I can't say that definitively, but I would
18 not be surprised. I think it's just a fact--
19 series of facts.

20 PETER WALSH: There's no finding of
21 fact, is there?

22 JOHN HAMJE: I don't see findings
23 labeled as such. I have to agree with the--

24 PETER WALSH: The recitation of a bunch
25 of different facts gathered in the course of the

1 investigation, isn't it?

2 JOHN HAMJE: It appears to be an
3 executive summary.

4 PETER WALSH: No application of the
5 facts of the law?

6 JOHN HAMJE: Well, again, without me
7 going through it word for word, I think [UNINTEL
8 PHRASE].

9 PETER WALSH: Well, I represent to you
10 there's not--or discussion of policy purposes in
11 here?

12 JOHN HAMJE: No, again, as I told you, I
13 don't think I ever saw this, saw the exhibit.

14 PETER WALSH: So there's no reference in
15 here to policy concerns like level playing field,
16 co-petition? There's no documents for any of
17 those?

18 JOHN HAMJE: I don't know about that,
19 but as far as I know, I'm not aware of anything
20 other than what I have generated we just talked
21 about.

22 PETER WALSH: Is there any document at
23 OIC explaining why it rejected the analysis of
24 Stickler, Gellermann, and Durfee?

25 JOHN HAMJE: I don't know what you mean.

1 I don't know what analysis you're talking about
 2 in terms of Ms. Gellermann.
 3 PETER WALSH: There's nothing in this
 4 finding, in this final investigative report,
 5 about the potential impact on consumers?
 6 JOHN HAMJE: Are you talking about
 7 Exhibit [UNINTEL PHRASE]?
 8 PETER WALSH: The final investigative
 9 report, yeah.
 10 JOHN HAMJE: Again, I'm not familiar
 11 with it.
 12 PETER WALSH: You've never seen this
 13 one, this version?
 14 JOHN HAMJE: I don't think so. I don't
 15 think so.
 16 PETER WALSH: Do you think that's
 17 strange, having led the investigation--strike the
 18 investigation--having led the matter for six or
 19 eight months?
 20 JOHN HAMJE: The portion that I led did
 21 not involve the investigation. The investigation
 22 was handled by [UNINTEL].
 23 PETER WALSH: Your job is to develop
 24 OIC's position with respect to Zenefits and you
 25 never read the final investigative report?

1 JOHN HAMJE: I think that is so.
 2 PETER WALSH: Okay. Are you aware at the
 3 same time that around the same time that things
 4 were coming to a head in September 2015 in the
 5 case [UNINTEL] assigned to you in October 2015? A
 6 very similar set of circumstances were being
 7 considered by the agency in connection with Blue
 8 Cross Blue Shield?
 9 JOHN HAMJE: No.
 10 PETER WALSH: You weren't aware that
 11 Blue Cross Blue Shield was offering and identify
 12 protections--wanted to offer an identity
 13 protection service to its insured?
 14 JOHN HAMJE: Oh, I do think I do
 15 remember that. They were some discussion about
 16 that, yes.
 17 PETER WALSH: And in fact, what they
 18 were proposing to do was to offer free identity
 19 protection services to only their insureds.
 20 JOHN HAMJE: Now, wasn't that in
 21 connection with the statutory proposal or
 22 [UNINTEL PHRASE]? I'm trying to remember. I think
 23 I may have seen or been asked for my opinion
 24 later on at one point in time during the
 25 legislation. And I remember going ahead [UNINTEL

1 JOHN HAMJE: I did not. This came after
 2 my work was completed.
 3 PETER WALSH: There's no analysis in
 4 here on the impact on Zenefits' consumers either,
 5 is there? And you never considered the impact on
 6 Zenefits' consumers?
 7 JOHN HAMJE: Well, that's not correct. I
 8 did consider it.
 9 PETER WALSH: I'd like to turn now to
 10 the impact of this consent order. You read the
 11 consent, I presume?
 12 JOHN HAMJE: It's been quite a while.
 13 PETER WALSH: Are you familiar with it?
 14 JOHN HAMJE: I'm not familiar with it.
 15 PETER WALSH: Did you read it when it
 16 was issued?
 17 JOHN HAMJE: I think I did, yeah.
 18 PETER WALSH: You didn't read the
 19 investigative report. You read the consent order.
 20 JOHN HAMJE: I think I did.
 21 PETER WALSH: You testified earlier
 22 about the importance about consistency and
 23 transparency in enforcement actions and
 24 regulation. Do you agree those are important
 25 factors?

1 PHRASE].
 2 PETER WALSH: What was your view on Blue
 3 Cross Blue Shield's ability to offer free
 4 identity theft protection services?
 5 JOHN HAMJE: Well, I wanted to make sure
 6 that--if I recall correctly, I wanted to make
 7 sure that the legislative director was aware that
 8 there could be a potential problem with respect
 9 to rebate inspections. And that would have to be
 10 something that would have to be [UNINTEL].
 11 PETER WALSH: That's not where AnnaLisa
 12 Gellermann and Charles Brown came down, is it?
 13 JOHN HAMJE: I don't know [UNINTEL
 14 PHRASE].
 15 PETER WALSH: If you turn to Exhibit AN,
 16 and if you look at the last paragraph of that
 17 email on Page 1, Chuck Brown--Chuck Brown is a
 18 lawyer, right?
 19 JOHN HAMJE: He was.
 20 PETER WALSH: I'm sorry, he passed,
 21 correct?
 22 JOHN HAMJE: Yeah.
 23 PETER WALSH: Mr. Brown, he was widely
 24 regarded as somebody with significant expertise
 25 in the anti-rebating and inducement statutes, was

1 he not?

2 JOHN HAMJE: Well, I think he was well
3 respected as a fine attorney.

4 PETER WALSH: Okay. And he concludes
5 here, "I tend to agree with the carriers that
6 this offering does not pose the kind of threat or
7 problem inducement and rebate statutes were
8 intended to address. My instinct would be to tell
9 them that while we are not in a position to agree
10 with the legal analyses of 140, we don't intend
11 to [UNINTEL] any regulatory action to block this
12 program." And Ms. Gellermann says, "Thank you, I
13 agree."

14 How do you reconcile, Mr. Hamje, a
15 decision not to take action against an entity
16 that's providing free identity theft protection
17 services only to its insureds with the decision
18 to find Zenefits in violation for providing free
19 benefits to the general public without condition?

20 JOHN HAMJE: I can't.

21 PETER WALSH: Isn't this why the agency
22 adopted the Producer Enforcement Group and
23 compliance committee structure to ensure this
24 kind of thing didn't happen, to make sure the
25 decisions were being made consistently across

1 industries?

2 JOHN HAMJE: No, that's not the case.
3 This is something entirely separate. And in fact
4 this is a legal--something that was in legal
5 affairs. And apparently it was--not only was it
6 submitted to AnnaLisa Gellermann [UNINTEL
7 PHRASE], it was not provided apparently to any
8 other staff. It does not represent necessarily
9 the position of the agency. I don't know what it
10 is.

11 PETER WALSH: The viewpoint of the
12 general counsel and Lisa Gellermann doesn't
13 represent the viewpoint of the agency?

14 JOHN HAMJE: It depends. It depends on
15 how it's publicized, but I don't know.

16 PETER WALSH: [UNINTEL PHRASE] rebate
17 statutes done distinguish a carrier like Blue
18 Cross Blue Shield and a producer in terms of
19 their application?

20 JOHN HAMJE: It applies to all [UNINTEL
21 PHRASE] insurance and producers and insurance
22 companies [UNINTEL PHRASE] service contractors.
23 I'll have to go back and look to be sure about
24 how the service contractor--it may not apply to
25 the service contracts. I'd have to go take a look

1 at that. Because I [UNINTEL PHRASE]. I'd have to
2 see that. Because Blue Cross Blue Shield [UNINTEL
3 PHRASE] service contractor. That may be the
4 reason why [UNINTEL] came up with this decision
5 and this [UNINTEL]. I don't know, without looking
6 at the statute.

7 PETER WALSH: You read the consent
8 order--I'm going to shift to a different example.
9 You read the consent order and it concludes that
10 140, 150 prohibit a licensee like Zenefits from
11 offering valuable software functions or other
12 valuable benefits for free or less than fair
13 market value to the public. Is that true?
14 Consistent with your recollection?

15 JOHN HAMJE: Would you read that again?

16 PETER WALSH: Sure. And actually, yeah--

17 JOHN HAMJE: Is there something that I
18 can look at?

19 PETER WALSH: Sure, Exhibit CR--C as in
20 Charlie, R as in Ralph [UNINTEL PHRASE].

21 JOHN HAMJE: Okay, I guess [UNINTEL
22 PHRASE].

23 PETER WALSH: Well, while we're looking
24 at--just want to confirm, you never saw the Blue
25 Cross Blue Shield decision memorialized anywhere

1 besides that email we just saw?

2 JOHN HAMJE: I don't know what happened.

3 PETER WALSH: And don't you think it
4 would be important to memorialize that decision?

5 JOHN HAMJE: Well, just because I
6 haven't seen it does not mean it hasn't been
7 memorialized.

8 PETER WALSH: Okay, now, please take a
9 look at Page number 6 of CR--consent order and--
10 I'm sorry, I made a lot of page [UNINTEL].

11 JOHN HAMJE: What's the page?

12 PETER WALSH: Page 3 of 6--Paragraph 6.

13 JOHN HAMJE: Okay.

14 PETER WALSH: And this was ultimately
15 the conclusion of you and your colleagues,
16 correct?

17 JOHN HAMJE: I think so, I think so. But
18 I understand this is negotiating, because this
19 language is all negotiating of the benefits. So
20 I'm not sure what it's saying and what it's not
21 and it should be included. So all I can say is
22 that seems to be accurate.

23 PETER WALSH: It's a pretty broad
24 conclusion, wouldn't you say?

25 JOHN HAMJE: It is, yes.

1 PETER WALSH: Likely to impact a variety
2 of other companies doing business in Washington?

3 JOHN HAMJE: Pardon me?

4 PETER WALSH: Likely to impact a variety
5 of other companies doing business in Washington?

6 JOHN HAMJE: I'm not sure if this
7 applies to other countries--other companies doing
8 business in Washington.

9 PETER WALSH: Well, any licensees like
10 Zenefits.

11 JOHN HAMJE: Okay, again, if it's--it
12 could very well affect--it would apply across the
13 board to all companies and licensees in
14 Washington.

15 PETER WALSH: You testified earlier that
16 you believe any producer who offers both discount
17 or pre services and sells insurance is in
18 violation of any rebating and inducement
19 statutes, correct? That's your view?

20 JOHN HAMJE: No, would you start--repeat
21 that?

22 PETER WALSH: Sure. It's your view that
23 license producers who offer free or discounted
24 services and also sell insurance--

25 JOHN HAMJE: That's what 157 prohibits.

1 PETER WALSH: But if they are entitled
2 to 157 exception, but that's what I was talking
3 about. That is a violation of the anti-inducement
4 statutes, anti-inducement statutes according to
5 you?

6 JOHN HAMJE: Okay, I'm sorry, if you
7 would start over again. I'm getting confused.

8 PETER WALSH: Licensed producer offers
9 discounts or benefits for free, sells insurance.

10 JOHN HAMJE: That's a violation of the
11 rebate statutes.

12 PETER WALSH: So why isn't the agency
13 pursuing Expedia?

14 DARRYL E. COLMAN: Objection. Expedia is
15 not at relevance [UNINTEL PHRASE] action.

16 PETER WALSH: Your Honor, it's highly
17 release. The Witness has testified that one of
18 the fundamental purposes of the regulatory
19 enforcement office's consistency--it's a large
20 part of our case. In fact, this proceeding was
21 anything but consistent. It was inconsistent with
22 how they handled BCBS. It is inconsistent with
23 their knowing decision not to pursue other
24 licensed Washington producers who are offering
25 significant discounts and also selling insurance.

1 And I well establish in evidence are some
2 documents.

3 And I plan to move into evidence
4 additional documents demonstrating that in fact
5 it depicts companies like [AVP?], Overstock.com,
6 USAA, and Expedia, just to name a few, derive
7 significant revenues from insurance premiums.
8 They offer benefit--they offer discounts on
9 [UNINTEL] from hotels and cars, cash back, and
10 refunds. So I think it's highly release, Your
11 Honor.

12 JUDGE LISA DUBLIN: I don't know how it
13 helps me answer the question that we amended the
14 [UNINTEL] conference order to determine whether
15 RCW 40.30, 31.40, and 150 prohibits benefits from
16 offering [UNINTEL] offer functions and benefits
17 for free. I think that's in the consent order.

18 So I understand you have a [UNINTEL
19 PHRASE] argument or that kind of thing. I'm not
20 here [UNINTEL PHRASE] determine that. I
21 understand that [UNINTEL PHRASE] evidence. That
22 really doesn't help me. It's outside the scope of
23 what I have jurisdiction to determine.

24 PETER WALSH: Your Honor, if I may
25 respond?

1 JUDGE LISA DUBLIN: You may [UNINTEL
2 PHRASE].

3 PETER WALSH: Okay, for the record, I
4 just want to be clear, I think that not only--
5 it's not just for the purposes in demonstrating
6 arbitration capricious, which I understand is one
7 thing. But it's in the purpose of demonstrating
8 that the decision of the agency here is baseless.
9 And we've heard evidence to that effect. And it's
10 one more example of the fair--the ends-driven--
11 and we argue politically-driven--decision that
12 has no support in legal analysis, legal
13 authority, has not been documented in any way,
14 shape, or form.

15 And we think that's all evidence to
16 show that the agency's rationalization of it now
17 is after-the-fact justification that had no basis
18 in the time. And therefore they should be given
19 no deference. The only thing that should be given
20 deference is the opinions and conclusions of the
21 legal department in 2014/2015.

22 JUDGE LISA DUBLIN: I don't want to turn
23 this [UNINTEL] into a place where we're going to
24 discuss investigation against [UNINTEL PHRASE].
25 So I'll let you put it in your argument in your

ATTACHMENT 2



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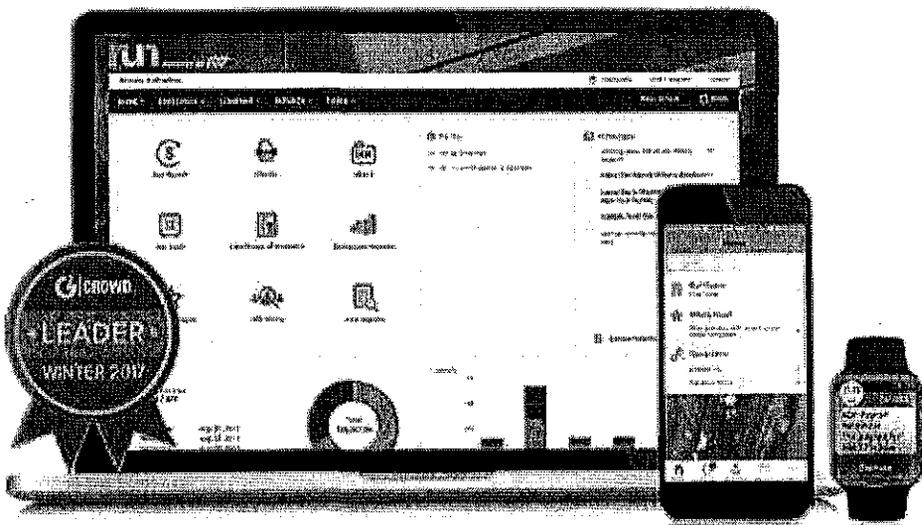
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Exhibit C



Paul R. LePage
GOVERNOR

STATE OF MAINE
DEPARTMENT OF PROFESSIONAL
AND FINANCIAL REGULATION
BUREAU OF INSURANCE
34 STATE HOUSE STATION
AUGUSTA, MAINE
04333-0034

Eric A. Cioppa
Superintendent

Bulletin 426
Rebates – Guidance for Producers
(Replaces Bulletin 384)

This Bulletin replaces Bulletin 384 and provides additional guidance for producers regarding what activities may be conducted under Maine's amended rebating statutes.

The purpose of Maine's anti-rebating laws is to protect both insurance consumers and the insurance industry. A consumer's choice to purchase insurance should not be influenced by inducements that could result in an unsuitable policy choice, and insurance must be provided in a nondiscriminatory manner to like insureds or potential insureds. Anti-rebating statutes are designed to protect insurer solvency and prevent predatory pricing, both of which can hurt market participants and consumers.

The general rule under Maine's rebating¹ laws is that no person may offer a discount or other inducement to a purchaser or prospective purchaser of insurance unless it is specified in the policy or the insurer's filings.² A determination whether a given arrangement violates Maine's rebating statutes is fact-specific and will depend upon the circumstances of the interaction between the parties. Some of the factors that the Bureau will evaluate in determining whether an arrangement violates the general prohibition on rebating will be the timing of the alleged inducement, the prior relationship between the parties, the type of benefit, and the recipient of the benefit. Section 2163-A of the Insurance Code establishes the permitted statutory exceptions to the general prohibition on rebating. Recent changes to this section have expanded the statutory exceptions by increasing the dollar thresholds and addressing the circumstances under which value-added services may be provided for free or at a reduced fee. These changes will go into effect on November 1, 2017.³ The purpose of this Bulletin is to give insurance professionals an overview of the statutory changes and provide guidance regarding how these new exceptions are interpreted by the Bureau.

¹ The subject of this Bulletin is compliance with laws prohibiting improper sales inducements. It does not relate in any way to the health insurance premium rebates that are required by state and federal law when insurers fail to meet minimum medical loss ratio standards.

² The rebate provision concerning life and health insurance is found in the Maine Insurance Code at 24-A M.R.S. § 2160. The corresponding provision for property and casualty insurance is located at 24-A M.R.S. § 2162. The provisions are not identical, but set forth the same basic principles for purposes of this Bulletin.

³ See P.L. 2017, ch. 84 (L.D. 1161).



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Gifts and Prizes

As of November 1, 2017, a producer may offer gifts valued up to \$100 per year per person in connection with the marketing of insurance, and conduct raffles or drawings with prizes valued at no more than \$500⁴, so long as there is no participation costs to entrants. These gifts may not be in the form of cash; however, cash equivalents (e.g., pre-paid MasterCard or VISA gift card) are no longer prohibited. For group coverage, the \$100 limit applies on a per-applicant-or-policyholder basis; *i.e.*, \$100 per group, not \$100 per covered life.

“Value-added” services

Maine’s recent statutory changes clarify that in certain circumstances, value-added services may be provided to a customer or potential customer, for free or at a reduced fee, without violating the general prohibition on rebating. Those services or discounts that can be valued at \$100 or less per policy per year are clearly acceptable under 24-A M.R.S. § 2163-A(1). If the services are worth more than \$100, the limitation will depend upon whether the value-added service is offered selectively or to all existing customers or potential customers.

If services valued in excess of \$100 are offered to specific customers, the services must be either included within the insurance policy or “directly related to the firm’s servicing of the insurance contract or offered or undertaken to provide risk control for the benefit of a client.”⁵

In evaluating whether a value-added service is directly related to the servicing of the insurance contract, licensees should look at the type of insurance involved and the nature of the services to be offered. The Bureau appreciates that the marketplace has become more complicated, especially for employers in the group health insurance market, and producers want to be able to use their expertise to provide customer assistance in a number of new areas.

The following examples are not intended as a complete list of acceptable services, but are offered to illustrate the range of services that would **generally** not be considered prohibited rebates:

- Risk management assistance provided by the producer;
- Regulatory and/or legislative updates;
- Enhancements that operate to make the producer’s own services and office operations more efficient and convenient for the insured;
- System improvements, which could include software provided to employers, which make information about group benefits provided through the producer more accessible to employers and employees;
- Services provided for COBRA or HIPAA administration for group health insurance customers;
- Administration of employer-sponsored Section 125 plans, flexible spending accounts (FSAs), and health reimbursement accounts (HRAs) for group health insurance customers.

⁴ The dollar limits for gifts and raffles were formerly \$20 and \$100, respectively.

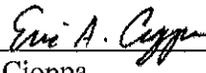
⁵ 24-A M.R.S. § 2163-A(2).

Producers and insurers should be cautious of providing services for free or at reduced cost for enhancements that provide significant value to the customer but have a relatively limited connection to the customer's insurance program. This is an important factor in determining whether the service has been offered primarily as a gift or inducement.

For example, the connection between the insurance coverage and the provision of assistance with payroll or human resource management is likely to be too attenuated to qualify for the "value-added" exemption. Additionally, services that are purchased by the producer from a third party (as opposed to being provided "in house") may be too far removed from the underlying insurance relationship.

Producers and insurers may offer value-added services for free or at a discount without regard to the underlying insurance relationship only when the receipt of services is not contingent upon the purchase of insurance and when the services are offered on the same terms to all potential insurance customers.⁶

October 25, 2017



Eric A. Cioppa
Superintendent of Insurance

NOTE: This Bulletin is intended solely for informational purposes. It is not intended to set forth legal rights, duties, or privileges, nor is it intended to provide legal advice. Readers should consult applicable statutes and rules and contact the Bureau of Insurance if additional information is needed.

⁶ 24-A M.R.S. § 2163-A(3).

Exhibit D

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WASHINGTON STATE
OFFICE OF ADMINISTRATIVE HEARINGS

In the matter of:) Docket No. 02-2017-INS-00009
YourPeople, Inc. Dba Zenefits) Agency: Office of the
FTW Insurance Services,) Insurance Commissioner
Appellant.) Agency No: 16-0219

APPEAL HEARING, DAY 1

TESTIMONY OF JEFF HAZARD

Administrative Law Judge Lisa N.W. Dublin Presiding

July 11, 2017

TRANSCRIBED BY: Marjorie Jackson, CET
Reed Jackson Watkins, LLC
Court-Certified Transcription
206.624.3005

A P P E A R A N C E S

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On Behalf of the Washington State OIC:

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ROSS D. VALORE

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2

3 JENNIFER A. FLEURY

4 Hogan Lovells US LLP

5 Columbia Square

6 555 Thirteenth Street, NW

7 Washington, D.C. 20004

8

9

10 Also Present:

11 Administrative Law Judge Dawn Bettinger (observing)

12 Beth Berendt, consultant for Zenefits

13

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July 11, 2017

(Time Stamp: 39 minutes, 50 seconds into the recording)

ALJ DUBLIN: All right. Then go ahead with your first witness.

MR. WALSH: Great. Thank you, Your Honor. Zenefits calls Jeff Hazard to the stand.

ALJ DUBLIN: Good morning, Mr. Hazard.

MR. HAZARD: Hi. How are you doing?

ALJ DUBLIN: Good. How are you?

MR. HAZARD: Good.

ALJ DUBLIN: Could you please raise your right hand. Do you swear or affirm the testimony you will give today will be the truth, the whole truth and nothing but the truth?

MR. HAZARD: Yes.

ALJ DUBLIN: Thank you.

JEFF HAZARD: Witness herein, having been first duly sworn on oath, was examined and testified as follows:

MR. WALSH: May it please the Court.

///

///

1 DIRECT EXAMINATION

2 BY MR. WALSH:

3 Q. Good morning, Mr. Hazard. Can you please state your full
4 name for the record?

5 A. Sure. Jeff Hazard.

6 Q. Can you spell it?

7 A. J-E-F-F, H-A-Z-A-R-D.

8 Q. Where do you work, Mr. Hazard?

9 A. I work at Zenefits.

10 Q. What's your job title?

11 A. VP of Sales (inaudible).

12 Q. How long have you been at Zenefits?

13 A. A little over two and a half years.

14 Q. Tell us a little bit about your responsibilities as Vice
15 President of Sales.

16 A. Sure, sure. So --

17 Q. I'm sorry. Before you start, this is being recorded at the
18 other end of the table --

19 A. Okay.

20 Q. -- so we have been asked to project, if you will.

21 A. Usually I don't need a projector. I will make sure I --

22 ALJ DUBLIN: You were doing fine.

23 THE WITNESS: Okay, good.

24 A. I can be overbearing that way.

25 Q. Sorry. So I will ask the question. Tell us a little bit

1 about your responsibilities.

2 A. Sure. So it's my job to make sure that the sales team is
3 performing their duties properly. It's everything from
4 SDRs, which are sales development reps. They make outbound
5 calls, inbound calls, basically calling out to prospective
6 customers, and also taking inbound calls.

7 From there, I need to make sure that our account
8 executives are doing everything properly, from selling to
9 understanding customers needs, to helping out with clients.
10 Basically, it's my job to make sure that the team is well
11 prepared, trained, compliant, and I'm driving growth for the
12 company.

13 ALJ DUBLIN: Before you ask your next question. I
14 apologize for interrupting. Is somebody on the phone with
15 us listening?

16 MS. FLEURY: Yes.

17 ALJ DUBLIN: And who is that person.

18 MS. FLEURY: Beth Berendt, B-E-R-E-N-D-T. Beth Berendt,
19 Your Honor, is listening on the phone.

20 ALJ DUBLIN: All right. Good morning. Ms. Berendt, this
21 is Judge Dublin. Can you hear me?

22 MS. FLEURY: I think she's probably muted, but...

23 ALJ DUBLIN: Okay. What is her job title?

24 MS. FLEURY: She is -- owns her own consulting business
25 and she is a consultant for Zenefits.

1 ALJ DUBLIN: All right. All right.

2 MS. FLEURY: We filed a motion specific to allowing
3 Ms. Berendt to participate.

4 ALJ DUBLIN: And I think we have already agreed that
5 there is no objection to her.

6 MS. FLEURY: Thank you, Your Honor.

7 ALJ DUBLIN: Thank you.

8 MR. WALSH: May I proceed, Your Honor?

9 ALJ DUBLIN: Yes, thank you.

10 MR. WALSH: Thank you.

11 Q. (By Mr. Walsh) Who do you report to at Zenefits?

12 A. To the COO, Chief Operating Officer, Jeff Carr.

13 Q. And are you an executive with the company?

14 A. Yes, I am.

15 Q. Where did you work before Zenefits?

16 A. I was at ADP for 16 years.

17 Q. What is ADP?

18 A. It's an HR and payroll company.

19 Q. And why did you you leave ADP to join Zenefits?

20 A. Sure. Two major reasons:

21 One, they wanted me to do more. That, and I hadn't moved
22 to New Jersey. I did not want to move to New Jersey; nor
23 did my wife. We love the Bay area.

24 The second reason was I was very excited about what
25 Zenefits was doing. The HR space is very complicated.

1 Businesses, when they use a lot of the current HR
2 applications, they're clunky, they're difficult to use,
3 they're not mobile-first. I was very excited about what
4 Zenefits was doing, to have a very simple, mobile-first, and
5 also building a platform connecting to all the different
6 systems. So I really felt like Zenefits was taking the next
7 step in the area of HR software.

8 Q. Well, that's a perfect segue to my next question, which was,
9 please tell us a little bit about what Zenefits does.

10 A. Sure, sure. So think of small business. You're trying
11 to -- you might be 50 employees. To manage your employees,
12 to hire them, to maintain everything about them, to pay
13 them, to do even performance management, like, who are my
14 rising stars, generally a lot of times that's done manually
15 with a lot of paperwork. That slows them down.

16 So Zenefits basically takes care of all that. We put all
17 of that software in one spot where we can manage all of that
18 for you. Whatever we don't manage, we actually have a
19 platform where we can connect into other systems. Because,
20 today, a lot of companies might have 8, 10, 12 systems to
21 manage their employees. If those are not interconnected one
22 way, you can imagine how many different things you're
23 logging into and trying to manage. That gets very complex.

24 So what we do is, we have a platform where we can connect
25 into those systems so you just put the information into

1 Zenefits and it populates those systems. So it really
2 eliminates a lot of the time that an owner or an HR person
3 would have to do to manage their people so they can focus on
4 their business.

5 Q. Mr. Hazard, you mentioned a few moments ago you worked
6 previously for ADP. How is -- how is -- is ADP a competitor
7 of Zenefits? How is it the same or different? How do the
8 two compare?

9 A. Certainly, they're a competitor. I believe our technology
10 is better and more up-to-date with what employees are
11 looking for, but, quite frankly, it's very similar and
12 they're a major competitor to us.

13 Q. Does ADP -- excuse me, does ADP also offer insurance
14 benefits?

15 A. Yes, they do.

16 Q. As a broker?

17 A. Yes, they do.

18 Q. Where is Zenefits headquartered?

19 A. San Francisco.

20 Q. When was it founded?

21 A. 2013.

22 Q. And how many states do you operate in?

23 A. All 50.

24 Q. How many employees do you have?

25 A. Approximately 500.

1 Q. And tell us a little bit about Zenefits' customers? I
2 understand -- well, you tell us: What kind of customers do
3 you have?

4 A. Sure. So, generally, they're anywhere from one employee to
5 a thousand employees. Most of them are small businesses;
6 10, 20, 30, 50 employees. We do almost any industry, but
7 certainly technology companies, healthcare companies, retail
8 companies, nonprofits, private schools. You know, almost
9 any company you can think out there leverages the Zenefits
10 platform.

11 Q. What's the average size of your Washington customer?

12 A. I think it's around 12 employees.

13 Q. I think you started to touch on this, Mr. Hazard, but tell
14 us about what is unique about Zenefits in the marketplace?

15 A. Sure. I would say three things, and I will probably repeat
16 myself a little bit so I apologize, but mobile-first. And
17 so that means is -- my guess is many of you have a
18 smartphone. We are seeing every day more and more people
19 have smartphones. And I think within two to three years,
20 there will be more smartphones or people using smartphones
21 instead of their computers.

22 So it's really important that the newest technology is
23 used on a mobile phone. And mobile-first means that it's
24 actually built for the mobile first, meaning, like, make it
25 best on mobile before you even build it for the computer.

1 So Zenefits is doing that.

2 Second, it's really simple. It's good looking software.
3 It may sound superficial but it's not, because being good
4 looking and easy to use means that people will use it. And
5 it's not complicated and so they don't need training. They
6 can just start using it because it's so intuitive.

7 And then the third reason is the platform. By us
8 connecting into all these different systems, you really make
9 it much more simple to manage your employees because you
10 don't have to go into 12 systems. We basically connect into
11 those systems.

12 And when I do a demo, I will try to, like, give a little
13 more of an example of that.

14 Q. Thank you.

15 In your job, you interact with customers?

16 A. Yes.

17 Q. Regularly?

18 A. Yes.

19 Q. And can you just, in summary, what do customers say about
20 Zenefits and its business?

21 A. "It's just so easy to use. You've really made my life a lot
22 easier. I'm spending a lot less time on our paperwork.
23 Thank you for making this so simple. Thank you for making
24 it so easy to manage my employees. This software is a lot
25 better than what I have used in the past." Or, "You have

1 automated things that are now manual. Thanks for giving me
2 time back so I can run my business."

3 Q. Among Zenefits' suite of offerings are insurance services?

4 A. Yes.

5 Q. And Zenefits is also a licensed broker, which is often
6 commonly referred to as a "producer"?

7 A. Yes.

8 Q. For the Court, just tell us simply and quickly: What is the
9 role of a broker in the insurance process?

10 A. Sure. The role of a broker is to work with the client to
11 help them see all of the different options out there for
12 them at their disposal for healthcare. It's complicated for
13 businesses.

14 Every state is different. There's different carriers.
15 And it's the job of the broker to kind of help educate them
16 on what is out there, potentially even go through a renewal,
17 so go through negotiation for pricing. Help them get that
18 up and running. Maybe help through open enrollment. That's
19 when all the employees are signing up for benefits.

20 And then just maintenance, customer service, when there's
21 questions about billing or maybe an issue, you know, with an
22 employee, to help navigate through that.

23 Q. And I apologize for the simplistic and possibly obvious
24 question. Can you tell us for the record how a broker
25 differs from an insurer?

1 A. Sure. An insurer is like a health carrier, so like Kaiser
2 or Premera. They offer the insurance. The broker is just
3 the go-between, between the client and the insurer.

4 Q. What kind of insurance does Zenefits offer as a broker?

5 A. Sure. Both health care, so medical, but also ancillary
6 plans, which is like dental, life insurance, disability,
7 those type of insurance options.

8 Q. What's a "broker of record"?

9 A. Broker of record basically means that you can work on behalf
10 of the client to help them negotiate the pricing and to work
11 with their sensitive documentation with the carrier.

12 Q. And in your space, is broker of record, is that a term of
13 art?

14 A. It's throughout the business, throughout the -- you know,
15 all companies, all insurance companies.

16 Q. So how does Zenefits get compensated for the insurance
17 products that it sells and oversees, manages as a broker?

18 A. We receive commissions through the carriers.

19 Q. Do you collect premiums from the insureds?

20 A. No. That is something directly with the company and the
21 carrier.

22 Q. Your customer --

23 A. Yes, we don't get in between them.

24 Q. Tell us a little bit about how the company -- the business
25 has evolved since its founding in 2013?

1 A. Sure. So it was always an HR software platform, but
2 certainly early on it was very basic. Over time, we built
3 out our platform and we added more and more priced options.
4 So, for example, time and attendance. That's a way to track
5 your hourly employees, you know, what hours they work, what
6 they worked on, and maybe taking PTO, time off. And then
7 over time we added payroll, HR services; premium services we
8 have added and will continue to add.

9 Q. Has there been significant change in the business's
10 operations in the past four years?

11 A. Dramatic.

12 Q. How has the role of Zenefits Insurance Services, brokerage
13 business evolved over time?

14 A. Sure. Certainly we have gained more experience. That has
15 been very helpful. We have built up our internal tools to
16 be better, to help manage our clients and to provide better
17 service. And, of course, we have made our tools that our
18 companies use for benefit administration better.

19 Q. And in terms of how the insurance services its brokerage
20 part, it's in a larger -- it's strategic plan of the
21 company, has that evolved or changed over time?

22 A. Sure.

23 Q. How so?

24 A. It's -- you know, over time we have consolidated some
25 carriers and made it more simple for us. And, certainly,

1 we're looking into outside avenues on the products.

2 Q. The Office of the Insurance Commissioner, OIC, has alleged
3 that Zenefits is primarily an insurance broker. Do you
4 agree?

5 A. No.

6 Q. Why not?

7 A. Because so many of our products that we offer are not around
8 insurance. Time and attendance, our premium HR services.
9 You know, can help companies build their handbooks. We can
10 help them with: What are the different laws in Washington
11 versus California? When I hire someone, what do I need to
12 do paperwork in Washington versus California?

13 We do payroll, so we can handle everything from paying
14 the employee to handling all the taxes for the company. So
15 quite frankly, yes, benefits is a part of what we do, but
16 we're a full-blown HR provider.

17 Q. And both in terms of the short-term and long-term vision of
18 the company, is that the case, and how does insurance fit
19 in?

20 A. Sure. So insurance will be part of what we do, but we're
21 going to go expanding our paid products. For example,
22 Talent is coming out soon. That's the ability to perform
23 like performance reviews: How did you you do this last
24 quarter, what are you working on, where are your talents and
25 where are your strengths and where are your weakness, what

1 do we need to work on to get you ready for your next
2 promotion.

3 So that's a new piece of software that will be coming out
4 relatively soon.

5 Q. Are you familiar, Mr. Hazard, with Zenefits revenue stream?

6 A. Yes.

7 Q. What percentage of new customer revenue from, let's say,
8 quarter 1, 2017, came from commissions on insurance?

9 A. I think it was around 25 percent.

10 Q. 25 percent of the company's revenue from new customers in
11 the first quarter of 2017 was insurance commissions?

12 A. Yes.

13 Q. And the remaining 75 percent?

14 A. Would be paid products.

15 Q. Your human resources?

16 A. Human resource premium, payroll, time and attendance.

17 Q. Do you know what those figures are for the second quarter of
18 2017?

19 A. It was actually lower.

20 Q. And so tell us what percentage of new customer revenue in
21 quarter 2 for 2017 came from commissions on insurance?

22 A. It was 16 percent.

23 Q. And when you you combine quarter 1 and quarter 2 and you
24 look at the first half of 2017, what percentage of the
25 customer revenue came from insurance commissions?

1 A. I think it's around 21 percent.

2 Q. And the remaining 79 percent comes from purely human
3 resources products?

4 A. Our paid products.

5 Q. Your paid products. Is that an aberration or a trend?

6 A. It's certainly a trend.

7 Q. Part of the long-term business strategy?

8 A. Yes, we're expanding into more paid products, more HR
9 products. That will continue for sure.

10 Q. Has that been part of the company's strategy for some time?

11 A. It has, yes. It just takes time to evolve and build
12 software.

13 Q. I would like to turn now to the topic of pricing. And you
14 mentioned before that you charge for certain apps and
15 software. And here I'm going to ask you to turn in your
16 exhibit book to Exhibit B-P (inaudible) pull out their big
17 binders?

18 A. What am I doing?

19 Q. B, as in boy, and P --

20 A. P.

21 MR. WALSH: Actually, what I am going to do is to make
22 this easier on everybody, because the print is a little bit
23 small (inaudible). All right. There we go.

24 THE WITNESS: Thank you.

25 Q. (By Mr. Walsh) What I put on the board, Mr. Hazard, is a

1 large blow-up, demonstrative version of Exhibit BP, which is
2 in evidence. And do you recognize this? Do you know what
3 it is?

4 A. Yes, this is our pricing page.

5 Q. Okay. And however you feel comfortable.

6 A. Okay.

7 Q. If you want to sit or stand, you can do either one. You may
8 be too close to read it.

9 And is this -- where would I find this? Where is this?

10 A. You can go to www.zenefits.com, pricing, and then this is
11 right there.

12 Q. It's posted on your website?

13 A. Yes, it is.

14 Q. And this sort of lays out the pricing for the various tiers,
15 the four tiers of software service that you provide?

16 A. Yes.

17 Q. Okay. Just -- I want to quickly - tell us what those tiers
18 are.

19 A. Sure. We basically put it to four metal particular tiers:
20 Bronze, Silver, Gold and Platinum. What you're seeing up
21 there is Bronze. It's free. Our Silver is 5 dollars per
22 month. This is the annual pricing. So 5 dollars per
23 employee per month, paid up front annually. 8 dollars for
24 Gold, and then 12 dollars for Platinum.

25 Q. And just so we understand and follow the page, this

1 demonstration here, it looks like every column contains the
2 same information but certain information in each column is
3 bolded; other is in light gray.

4 A. Yes.

5 Q. What is the distinction there?

6 A. Sure. So in the free package, you will see in bold what you
7 receive. So you will receive --

8 Q. And you don't have to go through the individual ones yet,
9 but --

10 A. Sure --

11 Q. -- just explain --

12 A. What you see in bold is what you receive. What is in gray
13 is what you don't have. And then you will see as you go up
14 in the modules that it opens up more things for you to use
15 if you pay for more.

16 Q. And if you're over there in the Platinum column, you get
17 everything in the Platinum --

18 A. Yes, you get everything (inaudible) column.

19 Q. Okay, great. Let's talk about and turn to some of these
20 metallic tiers, starting with Bronze. Tell us what comes
21 with the Bronze.

22 A. Sure. So that's employee management. That's everything
23 from hiring. So you can actually hire someone online -- and
24 I will show it during the demo, but what's great about that
25 is that it's all done through the online system. You don't

1 have to send emails or faxes. It's all done electronically.
2 Basic onboarding. Offboarding, so if you need to let
3 somebody go. Employee directory. Org chart. Basically all
4 basic employee management and then all benefit
5 administration is included in the Bronze package.

6 Q. And are these sort of the core apps?

7 A. Those are the core apps, yes.

8 Q. Tools to manage hiring and onboarding, terminating and the
9 like?

10 A. Yes. Day-to-day management?

11 Q. Generates some limited employee reports, org charts and the
12 like?

13 A. Definitely an org chart and then basic reporting. And I
14 will try to show that in the demo so you guys can see it.

15 Q. Bronze is free?

16 A. Bronze is free.

17 Q. Except...

18 A. Except for Washington.

19 Q. Why is it not free in Washington?

20 A. Due to the DOI's ruling in November.

21 Q. Turning now to the Silver.

22 A. Yes.

23 Q. Next in line there. So tell us what the Silver comes with?

24 A. Sure. So it's basically everything that Bronze came with.

25 And then we add premium HR, so that's some custom fields

1 around onboarding.

2 PTO, so that's your paid time off. Vacation, sick
3 tracking, liability. All that is done for the company.

4 Compliance assistant, how to make sure that you're
5 federally compliant. Formal Care Act reporting. Some
6 advanced reporting.

7 Our documents app, and then also our HR library, which
8 that helps you with maybe the different laws between the
9 states. It might be helping you build a handbook, basic HR
10 questions, salary benchmarking. It's all part of that HR
11 library.

12 Q. Okay. And you mentioned that costs 5 dollars per month?

13 A. 5 dollars per employee per month.

14 Q. Per employee per month?

15 A. Yes.

16 Q. You mentioned that's on an annual basis. If I don't want to
17 pay up in advance on an annual basis, what's the price?

18 A. I believe it's 8 dollars.

19 Q. All right.

20 Let's move next to the Gold. The Gold is 8 dollars per
21 month per employee. And what additional services do you get
22 if you purchase it?

23 A. Sure. So you basically get everything from the free package
24 to the premium HR, and now we're doing your payroll.

25 Q. Okay.

1 A. So everything from paying your employees to tax filing, that
2 is all included in the Gold package.

3 Q. And moving over to the Platinum, what do you get extra with
4 the Platinum?

5 A. So you receive everything that you did in Gold, but you also
6 get a certified HR specialist, so you can actually call our
7 HR specialist and they can help you through certain HR
8 items. Maybe you're trying to let someone go and you need
9 to know what the rules are in the state, like, "Do I have to
10 have two written warnings? Do I have to have a verbal?
11 What does that look like? What do I need do to make sure I
12 stay in compliance?"

13 And that certified specialist can walk through the client
14 what they need to do.

15 Q. Why is the company offering the free tier?

16 A. I think it's -- one, we have a lot of nonprofits that use
17 our software, and so we know that they don't have a lot of
18 money or budget.

19 Secondly, it helps us have a premium service, which is
20 pretty well known in the technology industry. It's a way
21 for people to test and use your software. Many times they
22 don't know if it will work for them. And this touches all
23 their employees. So they really want to make sure that this
24 is good software for them before they maybe want to purchase
25 or use us for more -- for more items.

1 Q. And is Zenefits prohibited from offering the free services,
2 the Bronze, anywhere else in the country besides Washington?

3 A. No.

4 Q. And if I'm a Washington small business and I want to sign up
5 for Zenefits, I can't get the Bronze? What happens if I --
6 what happens if I log in (inaudible), as you described, and
7 create an account and I want to try to get the Bronze?

8 A. So we'll know by your zip code. So once you put in a
9 Washington zip code, it takes you automatically -- instead
10 of giving it a free account and being able to start using
11 the account, it takes you automatically to this page, to the
12 pricing page, and Bronze is not an option. Silver is your
13 first option.

14 Q. So Washington customers that previously were Bronze, if they
15 stayed with Zenefits, are now obliged, if they want to
16 continue to Zenefits, to purchase at least the Silver?

17 A. They have to, yes.

18 Q. At 5 dollars per employee per month if they purchase a full
19 year in advance?

20 A. Yes.

21 Q. And 8 if they don't and go on a month-to-month basis?

22 A. Yes.

23 Q. Does Zenefits also offer services on an a la carte basis?

24 A. Yes.

25 Q. What kind of a la carte services does Zenefits offer?

1 A. Maybe one option is our time and attendance to track
2 employees' hours. Another option can be commuter benefits.
3 Certain states allow tax-free commuter benefits, so that's
4 another option that we can offer.

5 Q. Are savings accounts and flexible spending accounts also a
6 la carte options?

7 A. Yes, they are.

8 Q. Background checks? I forgot if you mentioned that.

9 A. Sure. (Inaudible) So this will give you an idea: Commuter
10 benefits, flexible spending, health savings accounts, time
11 and attendance, background checks, and then contractor
12 payments.

13 Q. And the prices are set forth on that, but there is an
14 additional -- what we mean by a la carte, is there is an
15 additional cost per employee or per user per month?

16 A. That's correct.

17 Q. It's (inaudible). You can choose any or none of these?

18 A. Yes.

19 ALJ DUBLIN: You have to watch leading questions because
20 you're not under oath.

21 MR. WALSH: Sorry, Your Honor.

22 Q. (By Mr. Walsh) Who decides -- so you also offer third-party
23 apps, apps developed by third parties?

24 A. We do, and that is via the platform.

25 Q. And what kind of third-party apps does Zenefits offer?

1 A. Sure. Maybe to get something that we would all know.

2 Google. Google gmail is a partner of ours.

3 Microsoft email is a partner of ours.

4 You might be familiar with this, Slack. It's a

5 communication tool. It's a partner of ours.

6 UBER. So if you use UBER for commuter benefits, that's
7 also a partner of ours. That's maybe some basic examples of
8 companies that we partner with.

9 There's also others: Expensify for expense reporting.

10 EShare is to manage your stock administration.

11 Principal to manage your 401(k). Those are just some
12 basic partners that we have on our platform.

13 Q. Do customers have to pay for access to these third-party
14 apps?

15 A. Generally, yes.

16 Q. And who decides the pricing and who do they pay?

17 A. That third-party does.

18 Q. And does Zenefits get compensated at all for your customers'
19 use of these third-party services?

20 A. We do get referral agreements.

21 Q. So in other words, the vendor, a third-party vendor may pay
22 a portion of what they receive to you?

23 A. Yes, they might.

24 Q. When -- you testified before that the company has evolved
25 over time. When did you launch the metallic-tier structure

1 we talked about here?

2 A. It was in October of 2016 when we added the tiers.

3 Q. And prior to launching this specific set of tiers, did the
4 company also have sort of the three categories that you
5 described: Free services, paid services, and then
6 third-party services?

7 A. Yes.

8 MR. WALSH: And if I could just have a second, Your
9 Honor.

10 ALJ DUBLIN: Mm-hmm.

11 MR. WALSH: Your Honor, I think this is probably a time
12 at which would begin the demonstration. May we take a two-
13 or three-minute break to get the technology set up?

14 ALJ DUBLIN: Sure, we're off the record.

15 MR. WALSH: Thank you.

16 (Recess)

17 ALJ DUBLIN: All right. We're back on the record after a
18 break, ready to proceed with the demonstration portion of
19 the direct. However, that obviously will not translate into
20 (inaudible).

21 MR. WALSH: Understood. Thank you, Your Honor.

22 Q. (By Mr. Walsh) So we have up on the screen a projection of
23 an online demonstration. Before we dive into this,
24 Mr. Hazard, tell us how Zenefits identifies potential
25 customers.

1 A. Sure. So we basically look for -- we build a database of
2 companies from 1 to 1,000 employees. We look for companies
3 that are in certain industries that I mentioned before, like
4 technology, healthcare, nonprofits, retail companies. We
5 basically have a database of those in our sales force, our
6 CRM, our customer relationship management software, and then
7 market to them.

8 That can mean everything from emails to webinars to phone
9 calls to events that we might do, locally in different
10 cities, and that's basically how we market to those
11 companies.

12 Q. How do you introduce potential customers to the platform?

13 A. If they have -- first, we usually give them a demo.

14 Q. Is a demo required to become a customer?

15 A. It's not.

16 Q. Is it possible for somebody to sign up for Zenefits without
17 ever speaking to somebody as Zenefits?

18 A. They could sign up for the software, yes.

19 Q. And when a demo is given to a customer, a potential
20 customer, how is it -- who provides it?

21 A. Usually the account executive.

22 Q. And how is it given?

23 A. Online. So there are services like Zoom or Join Me that a
24 client can go on from their site and then basically see the
25 demo.

1 Q. You don't have to be in the same room?

2 A. Oh, no.

3 Q. Is the demonstration of the Zenefits platform, is that,
4 again, similar to what a prospective customer would get?

5 A. Yes. My (inaudible) would probably say it better that I am
6 now, but yes.

7 Q. Okay. Let's (inaudible).

8 MR. WALSH: And what I'm going to do is, there is -- some
9 of this, Your Honor, is reflected in our exhibit book. We
10 have done our best. It's impossible to replicate an online
11 platform in paper form, but we have done a number of
12 screenshots to try and assist the court if you want to refer
13 back to it later in our exhibit book. Those are in evidence
14 as Exhibit B, as in boy, O, as in Oscar. And we do -- there
15 is one page (inaudible). It's page 38 of Exhibit B-O. I
16 find it helpful because it will be sort of the menu that we
17 will be working off of, but in any event...

18 Q. (By Mr. Walsh) Why don't you, Mr. Hazard, log in and take
19 us to the dashboard, if you would.

20 A. So a couple of things. Any web browser basically works, so
21 there is no software that you have to load on your computer.
22 You basically just go in as your web browser with your user
23 name and password.

24 I'm going in as an administrator, so think of maybe
25 someone in HR that is using the system, and that's how I

1 will demo today.

2 So first off, here is our task bar, so if there is
3 anything I need to do that is immediate, this basically
4 tells me, if you need to work on the work email (inaudible),
5 so it's basically prompting me there.

6 Quickly you will see that we have a lot of apps on our
7 platform, on our software, and you will notice it's kind of
8 like an iPhone, just like you have maybe on your iPhone, you
9 might have an app for UBER or for Starbucks or for your
10 banking app. We laid it out very similar. So, what's your
11 company profile, employees, basically how I manage our
12 employees. Documents, to manage documents. Payroll to
13 manage payroll.

14 Very simple. This kind of goes back to what I stated
15 earlier about a very simple user interface, very easy to
16 use.

17 Q. And just for the record, this page is screen-shot'd at
18 Exhibit B-O, page 38, and we will turn back to this. But
19 this is what you would call the dashboard page?

20 A. Yeah, this is the main dashboard. This is kind of where you
21 you go when you start. And then when you're done using an
22 application you go back to the dashboard.

23 Q. Show us, Mr. Hazard, which of these apps here are free -- at
24 least outside the state of Washington would you offer as
25 part of the Bronze package?

1 A. Sure. So to manage my company profile is free. Employees.
2 So this is basically to manage your employees, to maybe edit
3 their pay, see where they are in the org chart. Some custom
4 fields, that would be included here.

5 Payroll integration. So potentially integrating with
6 some of -- maybe a payroll provider that you have, so some
7 reports there. Hiring.

8 If we're your broker, the medical/dental/vision. And
9 then some basic reporting is also free.

10 Q. This is -- scroll down, is help center and community --

11 A. Yes, they are, yes. That -- yes.

12 Q. Why don't you walk us through a few of these, perhaps
13 starting, Mr. Hazard, if you want to start with the
14 employees app.

15 A. Yes. So I am now going to the employee app. And this is
16 where not only can you manage your individual employees, as
17 you can see them right here with their pictures, but I also
18 have the ability to see them in an org chart format. So
19 again, this is part of our free software outside of
20 Washington.

21 And so as you load your employees, we actually can build
22 on organizational chart for you. Generally, companies, you
23 know, they're either building their own PowerPoints to do
24 this or they're buying individual software that can be
25 costly. When you build just a PowerPoint, it's not always

1 up to date so that could be a problem.

2 What's great about Zenefits is that this is always up to
3 date. These are managing your employees in a system, so the
4 minute you hire someone, they actually show up in the org
5 chart. So it's really great for new employees or people
6 that see you, people coming into the business.

7 So Elizabeth here is the VP of HR. And Rachel reports in
8 to Elizabeth. If I want to look into Rachel, I now can
9 click onto Rachel and now I can see all her basic
10 information. And so, again, you can see how easy this is.
11 It's real simple.

12 So here's all her personal information, so I could edit
13 this information if I needed to. Employment. So is she
14 salary? How much money does she make? Who does she report
15 to? All that information is here.

16 If we wanted to see her tax information, you know, what
17 is she filing for? And also with her signature. Bank and
18 paycheck information, if she had any. Even documents. So
19 if there's documents that we need to upload, maybe the
20 federal W-4. It looks like Rachel is a California employee,
21 so the California state W-4 would be uploaded and we're able
22 to keep it here so you don't have to have a filing cabinet
23 with manual documents. It's all done online.

24 We also have the ability to track custom information. So
25 it could be anything from T-shirt size to what's your

1 insurance license number. You can basically build this for
2 your own company, what type of custom things they need to
3 track.

4 And then integrated apps, so you remember I mentioned
5 this earlier. Here are some of the apps that we could
6 actually link up for Rachel. So when we change information,
7 it then puts that information into those apps.

8 So that's some of the basic information that we can track
9 on the employees app.

10 I was going to go to hiring next --

11 Q. Sure. That would be great. I was going to ask you, please
12 take us --

13 A. Great.

14 Q. -- give us a tour of the hiring app.

15 A. So in the traditional role, to hire someone takes a lot of
16 work. You're trying to figure out, like, all right, what
17 form do I need to use, what offer letter? You might be
18 editing or sending this to different people in the company.
19 They're there looking at it, to sort of preview it. And
20 then you're emailing it off to the candidate. The candidate
21 has to print it. They have to sign it. Maybe they're
22 faxing it to you. It takes hours.

23 And then on the first day of work, they have to come and,
24 like, fill all this paperwork out. Especially for trying to
25 be a technology company, that is not a way to onboard an

1 associate. Plus it just takes a lot of time.

2 So to hire an employee, I can just basically go in there.
3 I'm going to pull someone that's already been done just for
4 the sake of time. But this is basically Kat. She's a new
5 employee. Here, I'm putting information like her first
6 name, her last name, what her email will be. And basically
7 on to the left here is a workload that I need to go through
8 to basically hire Kat. And it basically walks me through
9 the proper steps of everything I need to do to properly hire
10 Kat into the Zenefits system. So what is her title? Where
11 will they work? Their start date. What type of employee
12 they are. What department will they work in. What type of
13 worker they will be. If they have any track reports. Real
14 basic information, but everything that basically draws or
15 loads the Zenefits system for that.

16 Any custom fields, so laptop model, maybe. These are
17 things that you can add for your business, maybe you give
18 them a mobile phone. What mobile phone did you give to
19 them, so you can track that.

20 Payroll settings. What benefits they will be eligible
21 for. Any additional options. What apps do we want to
22 integrate them with.

23 And then once I have filled all this information out, I
24 can see her offer letter. It builds out all the information
25 I just put in there. It's that simple. And then if I want

1 to send this out, I just hit "next" and then we send out the
2 offer.

3 I'm not going to show the demo, but just to give you an
4 idea, Kat then gets the email with her offer. She can sign
5 it online. And then once she signs the offer letter, she
6 actually onboards herself and adds any more particular
7 information. So when she comes to the first day at work,
8 there is no paperwork here to fill out. They're ready to do
9 the job.

10 And what's really neat is everyone can see that employee
11 on the org chart, so they can start getting to know that
12 person.

13 Q. Thanks, Mr. Hazard. Why don't you you you take us back to
14 the dashboard and let's take a look at the business
15 intelligence app.

16 A. If you're okay, do you mind if I show some of the apps, too,
17 first?

18 Q. Sure (inaudible) the third-party apps?

19 A. Yeah, since you just talked about it. So it's simple. What
20 I just did there, I will go back to it. If I want to add an
21 app -- you may know this if you have an iPhone, you know you
22 want to add an app, you just add an app. It's that simple
23 with us, as well.

24 And so here, we will show you all the apps that you can
25 add. We're constantly adding more partners. I think we

1 have around 46 partners today, but every month or every
2 quarter we're adding more partners to our platform, so we
3 have apps such as productivity apps to make you more
4 efficient:

5 Asana, which helps with customer management.

6 Box, for your records.

7 Gmail.

8 Microsoft sales force.

9 Slack for communication.

10 401(k) providers, Copilot and Principal.

11 Business insurance, so that's like P&C, our partner who
12 does that.

13 Expense management, Abacus and Expensify.

14 Stock options.

15 Performance management, and travel.

16 And also employee engagement.

17 So those are just a number of apps. And if I wanted to
18 download it, I could literally just click on here and then
19 go through the (inaudible) app. It's that simple.

20 Q. Mr. Hazard, so we have looked at the employees app and the
21 hiring app, just to clarify because you mentioned this
22 before, those are free for the Bronze?

23 A. Yes.

24 Q. And we just looked at some of the third-party apps.

25 A. Yes.

1 Q. You talked earlier about there was a charge (inaudible)?

2 A. By those providers, but there is no charge for us to use
3 them on the platforms.

4 Q. All right. Let's turn, if we can, to the business
5 intelligence app --

6 A. Sure.

7 Q. -- if you can show us that?

8 A. Sure. So basic reporting is free, I am going to show you
9 one of the basic reports and then I will show you a more
10 custom report that's charged.

11 So this is like a birthday report. Here, I can go click
12 on it and see who has what birthdays. This is pretty
13 important, believe it or not, like if you can let someone
14 know that you know it's their birthday the day they come in,
15 it makes it a great place to work. And this is hard for a
16 lot of companies. We make it real easy for them.

17 We also give them the ability to download reports. So
18 maybe you want to put this in Excel. And it's as simple as
19 clicking on the report, and here is your birthday report.
20 And now I can email this off to different people, you know,
21 the department or whatever it may be. So very simple to
22 use. So that's an example of one of our free reports.

23 If you wanted to see more of our, like, custom reports --
24 this would be a charge, this is on the Silver package --
25 this will give you some of our advanced reporting. So this

1 is a head count report over time. So I can see who worked
2 in what department. So you can see here, this is August,
3 2016. And I will show you how many people did we have in
4 customer support, how many executives, how many people in
5 finance. What's great about this: This is point in time.
6 So I can look at different months of the year and see how
7 many employees did we have in each department.

8 This could be very helpful when you're working with maybe
9 auditors or you're trying to look back, like how big was
10 this department? (Inaudible) who has grown, who has not
11 grown? This reporting is very helpful for companies if
12 they're not using software like this (inaudible). They're
13 doing this manually in Excel and it's very time consuming.

14 Q. And so this head count, Mr. Hazard, this is one that would
15 come with the Silver tier?

16 A. That's correct.

17 Q. Or Silver (inaudible)?

18 A. Yes.

19 Q. So some of the functionality of this particular app,
20 business intel would be free. You showed us the birthday
21 report?

22 A. Yes, the basic.

23 Q. And others would be part of what you pay?

24 A. Yes.

25 Q. Okay. Thank you.

1 Now, let's take a couple more, if you don't mind. Let's
2 take a look at the time off, paid time off.

3 A. Yeah, I think that makes a lot of sense. So this is a
4 charged service. This is part of the Silver package, and
5 this is the ability for the company to track all of their
6 employees' time off. This is important because it can be
7 quite a large liability, and you don't know who's working
8 when.

9 So over here, the basic -- there's some basic reporting
10 on the time-off dashboard. This tells me how many hours are
11 scheduled to be taken off this month, how many hours have
12 totally been taken off this year, and what is my company
13 liability for all of the company, if everyone were to take
14 that time off.

15 If I want to see individual balances, I just put it on
16 the balances and here I can see what each person has
17 scheduled and available and what the liability is.

18 If I want to see who has requested time off, here are all
19 of the requests, so this is great for auditing purpose,
20 like, "Oh, wait, did Jeremy tell me he was taking time off?"
21 You just go to the request, and here you can see it.

22 If you're not using our software application, you might
23 be doing this in email. Oh, my gosh, what a nightmare to
24 try to find out who's taking time off when. It's very
25 difficult.

1 Timeline. So here I can see who asked for what and when.
2 And then I also have the ability to do reports here, so I
3 can download time (inaudible) balances, that type of thing.
4 So this really helps you manage your vacation and sick time
5 for your employees.

6 Q. Show us, Mr. Hazard, the human resources library briefly, if
7 you will.

8 A. Sure. So this is the HR library. This is another
9 application that is part of our Silver package today. And
10 really what this is, this is a very helpful tool to manage
11 everything you might have to manage in HR. A lot of our
12 companies don't even have an HR person, so this type of tool
13 is really helpful for them to build certain things out. So
14 maybe you need to build a job description or you want to
15 see, you know, benefit benchmarking, what are other
16 companies paying for benefits. Employee cost calculator.
17 How to build a handbook. It will basically prompt you on
18 how to build a handbook for each state and what information
19 you have to put in there.

20 Federal posters.

21 And I'm going to go to multi-state law as a comparison
22 tool. A lot of companies, they may start in a state and
23 then they start hiring people in different states. And this
24 is very helpful for them to say, "Okay, I only have people
25 in California. I'm how hiring in Washington. What are the

1 different requirements or the different laws in Washington
2 versus California?"

3 So it's as simple as: I click on Washington, click on
4 California, and I say, okay, let's create a chart. What do
5 I want to look at? Let's just look at new-hire reporting,
6 because I'm hiring someone. That probably makes sense.
7 What do I have to do reporting-wise? I'm going to create a
8 chart just so I can see it in a real easy way.

9 So here's California, the new-hire reporting
10 requirements. And here are the Washington reporting
11 requirements. So I can read through all this and say:
12 Okay, what do I need to do in California versus what do I
13 need to do in Washington?

14 So this is a good example of how the tool can help you
15 better manage your employees.

16 Q. And then one more app, if you would show us, please, the
17 medical/dental/vision. So this is the benefits app.

18 A. Yes. So if we were your broker, this is some of the
19 information that we would have for you.

20 Q. So if Zenefits is the broker, you have access to this.

21 There is no charge. It would be part of the free Bronze --

22 A. That is correct. So as the broker of record, we now can
23 work with the carrier. And so here we're showing you what
24 your medical cost is for the month, what your dental cost is
25 per month, vision, and total cost.

1 And how we can do this is, since we're your broker of
2 record, we are online or connected with your carrier so we
3 know exactly what your costs are.

4 Q. Why -- I'm sorry. Go ahead.

5 A. Sure. Now showing just all the different employees and what
6 different -- you know, do they have medical, do they have
7 dental. I can actually just click on them, and I can see
8 exactly what Adam has made. Both for Adam, you know, the
9 employee, all the costs there.

10 You can go even further and one of the -- since we are
11 connected with the carrier, one thing we can do is estimate
12 costs. So you may have a prospective employee who's like,
13 "Hey, look, you know, I want to come on board, but how much
14 is my medical cost going to be?"

15 You can go in here and the information you need for this
16 carrier is: Age, gender and zip code. That's how they do
17 the pricing. Let it calculate, and here is the cost that I
18 would -- the employee would be paying and the employer would
19 be paying for all of the difference in price, like Gold,
20 Bronze, Silver from the carrier.

21 So this really helps automate understanding what the
22 costs could be to a prospective employee.

23 ALJ DUBLIN: Can you scroll back down?

24 THE WITNESS: Sure.

25 ALJ DUBLIN: (Inaudible) page in the Exhibit B-0.

1 MR. WALSH: To the extent we have been able to print it
2 out, yes. I will confirm that during a break, Your Honor.
3 We can (inaudible). If they're aren't, we can screenshot
4 all of these and add them. I will double-check.

5 A. That's the basic demo. If you'd like I could go create a
6 new account and show you what that would look like.

7 Q. (By Mr. Walsh) Just -- if you would briefly.

8 A. Sure.

9 Q. Just give us a quick tutorial on how if you're a new
10 prospective customer you would want to create an account,
11 like we talked about earlier. Go ahead and do that.

12 A. Yeah, sure. So let's say I'm a new company coming in. I'm
13 going to go in -- it's called incognito -- the company knows
14 who I am, so if I don't do this, then it will just go back
15 to one of my accounts that I filled. So I would just
16 literally go to Zenefits, go to the website, let it load.

17 So I went into the login. I'm not a customer yet so I
18 want to sign up. And what it's basically doing right now is
19 it's looking to see if I'm already a customer, look at the
20 browser cookies, but since I'm incognito it won't do that.

21 And then in a second it's going to come up and it's going
22 to ask me if I'm a company or an employee. Let it load
23 here. We use (inaudible) card. It's a little slow.

24 Q. Mr. Hazard, while we're waiting -- oh, there it is.

25 A. So I click on "company," and now it's going to ask for some

1 basic information. So the internet company has a dot-com.
2 Now I'm going to put a zip code in California so this way
3 you will be able to get the free account.

4 Q. And what would happen if you put a Washington zip code in?

5 A. It would go right to the pricing page. So let's -- now it's
6 looking through the database, am I someone that has already
7 done this before? And it's saying: Oh, we need to verify
8 your account, please go to your email.

9 I'm going to go to my email real quick. So I went to my
10 email. I confirmed. And now I add a new account. So it's
11 going to ask me: Tell us some more about your company. It
12 will basically start walking me through different things to
13 load: Can I add my employees in bulk, do I have an Excel
14 upload or do I just key them individually.

15 And then here are all the apps.

16 Q. So some of those apps have dotted lines around them, and
17 some of them are filled in.

18 What's the distinction there?

19 A. Sure. So some of them are basically free, you can start
20 using them right away. If I click on "time-off," I could
21 say "set time-off," and it should take me right to the
22 present page.

23 Q. So have you just established what, in essence, is a Bronze
24 account?

25 A. Yes. Right now I can start using this. I can start loading

1 employees. You will see there's nothing here because I
2 haven't loaded any employees yet. But I can start adding,
3 start using Zenefits right away. So I mean, it's instant.

4 Q. Why don't we go back to the dashboard. Mr. Hazard, so you
5 mentioned before when you were showing us the medical,
6 dental and vision, that those were only available if
7 Zenefits was the broker of record for a specific customer?

8 A. Yes.

9 Q. Why do you need the customer -- why do you need to be the
10 broker of record for that customer in order for them to be
11 able to use the functionality of the, for example, the
12 medical/dental/vision app?

13 A. Sure. So it's how we built the system. We have a lot of
14 sensitive data that we're going to be moving back and forth
15 with the company and the carrier. And the only way the
16 carrier will work with you is if you're the broker of record
17 to handle that sensitive information.

18 Q. Does the functionality of the medical/dental/vision app, for
19 example, depend on having data that is provided to you by
20 the carriers?

21 A. Yeah. Without it, it's just a shell of information.

22 Q. And you cannot access that data unless you are the broker of
23 record?

24 A. That's how we go back and forth with the carrier.

25 Q. And it's the same case for COBRA and savings accounts,

1 flexible spending accounts?

2 A. How we built the system is those are all interconnected.

3 Q. What is -- the insurance benefits side, what's unique about
4 Zenefits' insurance benefits (inaudible)?

5 A. Sure. So in some ways it's not unique; it's the same.

6 (Inaudible) carrier is just like any other benefit broker.

7 I think the win here, though, is we're collecting all the
8 employee information, and so there's less information, less
9 systems they have to go to to manage their benefits because
10 it's all in one spot.

11 Q. And you mentioned before that you are connected here to the
12 carrier and interface directly with the carrier?

13 A. Yes. A good example of that is, let's say you have a baby.
14 And two or three days later you come back home and you want
15 to make sure the baby is part of insurance. You can
16 literally go in and add a dependent. And you add a baby and
17 then we're connected to the health carrier, so we're sending
18 that information to the health carrier letting them know
19 that you just had a baby. It's called a qualified life
20 change.

21 Q. Going back to the Bronze, the free tier, who is that
22 available to?

23 A. To anyone other than Washington.

24 Q. The general public?

25 A. The general public.

1 Q. Anybody who signs up for an account?

2 A. Anyone who goes to www.zenefits.com and they want to create
3 an account.

4 Q. Do you need to sit for a demo or anything like that before
5 you can create that account?

6 A. No.

7 Q. If you sign up for Bronze, are you obligated to purchase
8 insurance?

9 A. No.

10 Q. Are you obligated to sit for a pitch?

11 A. No.

12 Q. Are you obligated to purchase any fee-based service?

13 A. No.

14 Q. Do you make that clear to customers and prospective
15 customers?

16 A. Very clear.

17 Q. How so?

18 A. We let them know that our software is free to use and that
19 anyone can use it. If you would like to have some of our
20 paid applications, we can show them to you. If you would
21 like us to be your broker, then we can have a conversation
22 about that, as well.

23 Q. Is that also -- do you also provide that to your customers,
24 your prospective customers in writing?

25 A. Yes.

1 Q. Can you please turn to Exhibit (inaudible) --

2 A. Do you want me to keep this going or do you want me to --

3 Q. No, you know what? I think we can --

4 A. Just so we can turn the fan off.

5 Q. -- just continue the -- thank you.

6 A. And what exhibit is this?

7 Q. B-W, B as in boy. Do you recognize this document?

8 A. In terms of service, yes.

9 Q. What is it?

10 A. It's basically everything that, you know -- our rules and
11 agreements that you need to sign to leverage our software.

12 Q. Is this provided to all customers?

13 A. Yes.

14 Q. When you sign up, it's part of your agreement?

15 A. Yes, yes. I clicked on it and I could have gone right to
16 the link and read the entire thing.

17 Q. No need to do that. But if you would turn, please, to the
18 bottom of page 2 at Exhibit B-W, Section F, Insurance
19 Services, and it continues on to the top of page 3.

20 Do you see where I am?

21 A. Yes.

22 Q. And can you point out for the Court if there's anything
23 there that instructs or warns customers about whether or not
24 they're required to use insurance services to access any
25 services?

1 A. This top line here -- I'm having a hard time reading, it's
2 very small -- but, "You are not required to use Zenefits for
3 insurance services in order to obtain an account and use the
4 services."

5 Q. And is that one of the examples of how it's communicated in
6 writing that you referenced before?

7 A. Yes, to customers.

8 Q. Mr. Hazard, when you -- a few moments ago you were talking
9 about -- you answered some questions I asked you about
10 whether Bronze was free to everybody with no conditions or
11 obligations. That's the case today.

12 Has that been the case at all times with Zenefits?

13 A. It's always been free.

14 Q. It hasn't changed. It's always been consistent even though,
15 for example, this particular metallic tier system was
16 adopted in the fall of 2016?

17 A. Yes.

18 Q. If an employer does elect to designate Zenefits as his
19 broker of record, do they get any discounts on fee-based
20 services?

21 A. No.

22 Q. Has that also been the case at all times?

23 A. That's correct. They never have.

24 Q. Are there any special benefits or incentives associated with
25 designating Zenefits as a broker of record that are not

1 available to others?

2 A. No, other than our software.

3 Q. Are customers penalized or disadvantaged in any way if they
4 don't buy insurance or make Zenefits their broker of record?

5 A. No.

6 Q. That, again, was the case before the metallic tier, as well
7 as after?

8 A. Yes.

9 Q. I would like you to turn in your book, please, to what's
10 been entered into evidence as Exhibit B-B, boy, boy. Can
11 you read --

12 A. B-B.

13 Q. Now, (inaudible) on its face, but I will represent to you
14 that this is a press release issued on December 1, 2016 by
15 the Office of the Insurance Commissioner of Washington. And
16 I would like to direct you to the third paragraph. The
17 paragraph begins, "California-based Zenefits." I would ask
18 you to read that paragraph, but then in particular I'm going
19 to ask you a question about the third sentence, starting
20 with "to access."

21 A. "California-based Zenefits began operations in Washington in
22 2014, selling online human resource services to businesses.
23 As part of its free software offer, Zenefits provided
24 certain features with a paid commission. To access three
25 premium features, the company required to client to

1 designate Zenefits as its broker of record, then collected
2 the commissions associated with the insurance products
3 sold."

4 Q. Just concentrating primarily on the second and third
5 sentence, and primarily the third, is this an accurate
6 statement?

7 A. I don't believe so, no.

8 Q. Why not?

9 A. Because you don't need to use us as an insurance broker for
10 our premium features.

11 Q. Would you look, please -- turn, please, to Exhibit C-Q.

12 Mr. Hazard, I've been getting into a lot of detail. This
13 exhibit, which is in evidence, is C-Q, that I will represent
14 to you is an email from Lonnie Johns-Brown of the Office of
15 the Insurance Commissioner to State Senator Joe Fain and
16 other members of the state legislature.

17 I want to direct your attention particularly to the
18 second page of that email. In particular, if you look at
19 the paragraph that begins, "Expedia's principal business."

20 A. Mm-hmm.

21 Q. And then you work your way down about halfway through the
22 paragraph to the sentence that begins, "It is in the
23 insurance business, not the payroll business."

24 Do you see that?

25 A. Yes.

1 Q. In particular it reads, "It is in the insurance business,
2 not the payroll/human resources, et cetera, business."

3 Is that an accurate statement?

4 A. No.

5 Q. Why?

6 A. Because we're a full HR operating system. That's everything
7 from payroll benefits, time and attendance. There's a lot
8 of paid products. We're not just in the insurance business.

9 Q. Is that reflected by the percentage of your customer revenue
10 that the company is deriving now from non-insurance
11 products?

12 A. Certainly.

13 Q. And if you would go down a few lines further to the sentence
14 on the line that begins, "However," halfway through that
15 line reads, "Zenefits developed the platform and provides
16 the bulk of the services offered without charge for the
17 purpose of selling insurance."

18 Is that an accurate statement?

19 A. It's more evolving. We have more and more paid products.

20 Q. And do you offer the bulk of your services without charge?

21 A. No.

22 Q. And are the bulk of your services offered for the purpose of
23 selling insurance?

24 A. No.

25 Q. Do you require prospective customers to sit through a pitch

1 of Zenefits insurance services?

2 A. No.

3 Q. Will you show them the insurance offerings during the demo?

4 A. Initial demo? No.

5 Q. Is the demo that you just gave us in the court, for material
6 effects, is that similar to or different from what you would
7 give with respect to (inaudible)?

8 A. There isn't one.

9 Q. Mr. Hazard, I noticed that in the long and convoluted name
10 of Zenefits, your official name, it has the phrase FTW
11 Insurance Services. Do you know why that is in the name of
12 the company?

13 A. I believe in California you have to put something in there
14 if you're in insurance, you have to say "insurance
15 services."

16 Q. It's, to your understanding, a legal requirement?

17 A. That's my understanding.

18 Q. I want to turn now to the consent order. You're familiar in
19 this case with the consent order issued in the fall of 2016?

20 A. Yes.

21 Q. Has any other state, to your knowledge, found Zenefits in
22 violation of anti-rebating in any business statutes?

23 A. No, I know that Utah had something but that got overturned,
24 and I believe it was a different statute or something.

25 Q. With respect -- with the exception of Utah, no other state

1 has found the company in violation?

2 A. That is correct, no other state.

3 Q. Do you currently offer the Bronze tier for free in Utah?

4 A. Yes, we do.

5 Q. Why?

6 A. Because we can, and companies -- the legislature is okay
7 with it. And companies want to use the software and we want
8 to help companies in Utah.

9 Q. Have other states concluded that Zenefits -- specifically
10 that Zenefits is not in violation of the statutes? The
11 anti-inducement and anti-rebate statutes, I should say.

12 A. I do know that there are states that have basically
13 documented that.

14 Q. Describe for us what it took for the company to comply with
15 the consent order?

16 A. It was a lot of work. We basically had to change how we
17 were operating our software for one particular state, which
18 meant a lot of changed management, so we had to communicate
19 to the whole company what this meant, who would need to do
20 what.

21 You know, in sales, we had to dedicate three individuals
22 to work with our Washington clients, you know, over the
23 phone to communicate and to educate them on what happened.
24 And we had to do it very quickly. We only had 30 days. But
25 sales was only one portion of it.

1 We had to work with PR so they understood what was
2 happening.

3 We had to work with operations so we had to change
4 certain software and engineering on the back end. So even
5 the website, I think we had to change. If you had a
6 Washington zip code, what does that mean, where does it go?

7 Certainly customer service representatives, so if a
8 company called and asked questions about it, that they were
9 informed.

10 Finance, to make sure that they were ready to start
11 charging and to handle that, so basically it entailed almost
12 the entire company.

13 Q. Was it disruptive?

14 A. It was.

15 A. Are you able to estimate costs in connection with some of
16 the compliance steps you just described?

17 A. Sure. I think it cost us probably over \$100,000 in sales
18 because we had to dedicate three individuals for over a
19 month, basically almost two months.

20 And that's just a portion of the cost. I think it was
21 \$30,000 in engineering, operations cost to change the
22 website and the back part of our software. But it's hard to
23 gel all of the other soft costs of like everyone else having
24 to adjust, but certainly there was a lot of soft dollars,
25 time spent, productivity lost, those type of things.

1 Q. Was this a big deal for the company?

2 A. Yes.

3 Q. Did you get any feedback from customers about the change in
4 the pricing scheme?

5 A. Yes.

6 Q. How did Washington customers react to the consent order and
7 the new pricing?

8 A. They weren't happy. They basically had something for free
9 and now had to pay for it. They didn't have much time
10 either. It was like 30 days. It was holiday season. It
11 disrupted their business. It cost them money.

12 Specifically, nonprofits were very vocal on how it hurt
13 them with their mission. It's mid-year for them. Most of
14 them do their budgeting in June for a July start for the
15 fiscal year. So many of of them didn't have budget dollars
16 for it. It was just highly disruptive.

17 Q. Do you know if you lost any customers as a result?

18 A. It's hard to tell, like, when customers leave, you know,
19 what are the reasons for it? Certainly, though, anecdotally
20 some of them told me or others, like, you know, I'm leaving,
21 I'm not going to be able to pay for this.

22 I don't know exactly how it affected us, but I do know
23 that it affected us.

24 MR. WALSH: Your Honor, may I have a moment?

25 ALJ DUBLIN: Sure.

1 MR. WALSH: Thank you, Your Honor.

2 Thank you. I have no further questions for this witness.

3 ALJ DUBLIN: All right, thank you.

4 Are you able to do cross-examination in the current setup
5 or do you need to take down the screen before cross?

6 THE WITNESS: We can leave all this if you would like.

7 MR. COLMAN: I'm comfortable with whatever, Your Honor,
8 so if you prefer it moved, that's fine with me, but I'm
9 happy with whatever.

10 ALJ DUBLIN: Let's deconstruct. Let's go off the record,
11 deconstruct, and then we can move it back around. Thank
12 you.

13 (Recess)

14 ALJ DUBLIN: We're back on the record after a break to
15 deconstruct the set. We will begin with cross-examination.

16 MR. COLMAN: Thank you, Your Honor.

17

18 C R O S S - E X A M I N A T I O N

19 BY MR. COLMAN:

20 Q. And thank you, Mr. Hazard, for your testimony and your
21 demonstration. That was helpful.

22 You may have already answered most of my questions so
23 this will be fairly brief. I have a few clarification
24 questions.

25 First off, when this slide says (inaudible)

1 demonstration, that primarily refers to insurance benefits,
2 correct?

3 A. Yes, that's correct.

4 Q. Thank you. Just making sure I was tracking with that.

5 You referred to the revenue trend in 2017. What did you
6 do to find out those numbers?

7 A. Those are based on our sales numbers and finance numbers.

8 Q. And how did you get those numbers?

9 A. It's our sales force numbers. It's in our ERP.

10 Q. Okay. Thank you. Did you check those numbers for 2016?

11 A. No, I have not.

12 Q. Just curious. Thank you.

13 And I think you might have answered this, but just to
14 clarify, which services must a consumer name Zenefits as
15 broker of record in order to access on the Bronze plan? You
16 mentioned a couple. I just want to remember.

17 A. Sure, like health care.

18 Q. Okay.

19 A. So health care coverage. Dental. Certain ancillary plans.
20 Could be vision, life insurance, LTD, short-term disability.
21 Those type of items.

22 Q. Okay. You talked about the initial demo for -- that you
23 provide to consumers, right? Does -- doesn't the sales rep,
24 during that initial demo, disclose that Zenefits is
25 available for insurance services?

1 A. We do say that we're a licensed broker.

2 Q. Okay. Will a sales rep give a quote, if requested by the
3 consumer?

4 A. If you're a licensed broker.

5 Q. Right.

6 A. We won't do that like right then and there. We will
7 basically say, we should set up another meeting to
8 discuss --

9 Q. Okay.

10 A. -- what they're looking for.

11 Q. Okay. So if a consumer asks you for a quote, you will say
12 you will set up an appointment. Is that fair?

13 A. That's fair.

14 Q. Thank you. To transact insurance through Zenefits, is it
15 required that a consumer designate Zenefits as a broker of
16 record?

17 A. You could work with them on quoting before, but once you
18 transact, once you're transacting and working on behalf of
19 that client, you need to be a licensed broker.

20 Q. Okay.

21 A. You need to be the broker of record.

22 Q. Okay. So broker of record to transact insurance, okay. And
23 that, to reiterate, opens up those the -- maybe I have got
24 it down here -- the medical/dental/vision app on the
25 Zenefits app; is that correct? Or do I have that wrong?

1 When you designate Zenefits as the broker of record, which
2 apps on the HR platform are opened up to you?

3 A. Basically that app, the medical/dental will basically be
4 turned on because now we will have the information from the
5 carrier.

6 Q. Right. Okay.

7 A. We're connected.

8 Q. No, that makes sense. Do you know how many of the clients
9 that did end up going with Zenefits for insurance needs saw
10 a demo first? Do you have that information?

11 A. I wouldn't know what that number would be.

12 Q. Okay. Do you -- can you tell me how many insurance clients
13 of Zenefits do not use the HR platform?

14 A. I wouldn't know specifically what number that is.

15 Q. Would you say it's fair that most insurance clients of
16 Zenefits use the HR platform?

17 A. I would think that most do, but I don't know what the exact
18 percentage is.

19 Q. Okay. You showed a couple of third-party apps. Could you
20 tell me which ones of those are free for customers, or are
21 they all charged?

22 A. It all depends on the customer.

23 Q. Okay.

24 A. Like, for example -- and I don't know the specifics here --
25 Google, maybe gmail for some customers is free.

1 Q. Okay.

2 A. But once you have a business, I believe the business then
3 gets charged. I don't really know the specifics there.

4 Q. Okay.

5 A. Because that's really the third parties.

6 Q. Okay. So it depends on the third-party whether to charge or
7 not charge?

8 A. That's correct. All the charging is through that
9 third-party, not through us.

10 Q. Okay. But there may be some of those apps that are free. I
11 was just trying to understand from when you were doing the
12 demonstration.

13 A. There could be yes.

14 Q. Okay.

15 A. Some of those providers have some free options.

16 Q. Okay. So some of them are free?

17 A. I believe they are.

18 Q. Okay. What benefit does a Zenefits client get from using
19 Zenefits for its insurance programs?

20 A. Sure. So, certainly, having everything in one place just
21 makes it easier for the client. The insurance offerings
22 that we offer are like what every other broker can offer.
23 We provide better service, and so if I happen to provide
24 better service, certainly that is great for our clients.

25 MR. COLMAN: I think that's it for me. Thank you.

1 ALJ DUBLIN: Okay.

2 Any redirect?

3 MR. WALSH: Yes, thank you.

4

5 R E D I R E C T E X A M I N A T I O N

6 BY MR WALSH:

7 Q. Mr. Hazard, I just want to clarify. Mr. Colman asked you a
8 question, and I may have misheard it, but I thought it was
9 to the effect of: To transact through Zenefits, are you
10 required to designate Zenefits as a broker of record?

11 And I just want to clarify. Is -- you're only required
12 to be a broker of record for Zenefits for the
13 insurance-related apps that you described in your
14 demonstration.

15 A. That's correct.

16 ALJ DUBLIN: It was a leading question. That really
17 impacted the testimony. I feel like you have testified half
18 the time and he's testified half the time. It does affect
19 the level of credibility I give your witness's testimony.
20 So could you please phrase your question in a way that helps
21 me?

22 MR. WALSH: I would be happy to. And I apologize, Your
23 Honor. I sometimes only do it just to try to keep the
24 process moving along.

25 ALJ DUBLIN: I understand. Not helpful.

1 MR. WALSH: I hear you. Thank you, Your Honor.

2 Q. (By Mr. Walsh) So I would just like to clarify. What
3 specifically are the apps for which a customer <sic> must be
4 a broker of record for them to use utilize?

5 A. It's the medical/dental app. All the other free
6 applications you can use if you're a broker-client or not,
7 insurance client or not.

8 MR. WALSH: Thank you. No further questions.

9 ALJ DUBLIN: Thank you.

10 Anything else?

11

12 R E C R O S S E X A M I N A T I O N

13 BY MR. COLMAN:

14 Q. Just to clarify on that one issue. What I mean by -- maybe
15 I misphrased the question. But when I mean "transact
16 insurance," I mean sell, solicit, negotiate insurance.

17 In order to do that, must a Zenefits customer designate
18 Zenefits as broker of record; is that correct? I can
19 rephrase if that's confusing.

20 A. It might be better to re phrase.

21 Q. Okay. So in order to transact in terms of the business of
22 selling policies as an insurance producer, which Zenefits
23 is, must a Zenefits customer designate Zenefits as the
24 broker of record in order to do that?

25 A. We can give them ideas when they're looking to get a quote.

1 You do not need to be the broker of record to do that. Once
2 you transact insurance and you're advising on insurance,
3 then you need to be the broker of record.

4 Q. Okay. Then I think that makes sense. So, for example, in
5 Exhibit B-W, when it says in the Terms of Service, "If you
6 choose to use Zenefits to obtain professional advice with
7 respect to any line of insurance that Zenefits is licensed
8 to transact, insurance services, you agree to, one,
9 designate Zenefits as your broker of record or agents of
10 record."

11 Is that what you're talking about?

12 A. Could you --

13 Q. What would you like me to repeat?

14 A. Maybe just re-read it again.

15 Q. No problem.

16 ALJ DUBLIN: And where are you reading from, for the
17 record?

18 MR. COLMAN: I'm reading from Exhibit B-W, page 3. It
19 was the same page that Mr. Walsh read from earlier. Same
20 paragraph.

21 A. (Inaudible).

22 Q. Feel free to read it for yourself. So page 3 of Exhibit
23 B-W.

24 A. Page 3 and where?

25 Q. The second sentence. And you can read as far as you want,

1 but I am really only asking you about the first -- that
2 second sentence through "broker of record or agent of
3 record."

4 Does that help?

5 A. Okay.

6 Q. So what does that sentence mean to you?

7 A. Basically if we're to transact insurance and give advice,
8 that we need to be the broker of record.

9 Q. Okay, thank you. That's what I was asking?

10 MR. COLMAN: And that's it for me, Your Honor.

11 ALJ DUBLIN: Thank you.

12 Any re-redirect.

13 MR. WALSH: Nothing from me, Your Honor.

14 ALJ DUBLIN: All right. Then you're dismissed from
15 testifying.

16 It's approximately 11:25. Do you have any thoughts about
17 your next witness, length of time, lunch?

18 MR. WALSH: Your Honor, I think our next witness
19 shouldn't be too long, but if it's acceptable to you, we can
20 take our lunch break and then it's primarily just a question
21 of getting her over here. She's just down the street and it
22 may take a few minutes. Would it be possible to take a
23 lunch break and bring her right in?

24 MR. COLMAN: It's certainly acceptable to us, if it works
25 for you.

1 ALJ DUBLIN: Sure. All right. Let's go off. Does 12:45
2 work or do you want until 1:00?

3 MR. WALSH: 12:45 is fine with me.

4 MR. COLMAN: That's fine.

5 ALJ DUBLIN: All right. We will go off the record till
6 then. Thank you.

7 (Lunch recess)

8 (Conclusion of requested testimony)

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C E R T I F I C A T E

STATE OF WASHINGTON)
)
COUNTY OF SNOHOMISH)

I, the undersigned, do hereby certify under penalty of perjury that the foregoing court proceedings were transcribed under my direction as a certified transcriptionist; and that the transcript is true and accurate to the best of my knowledge and ability, including any changes, if any, made by the trial judge reviewing the transcript; that I received the audio and/or video files in the court format; that I am not a relative or employee of any attorney or counsel employed by the parties hereto, nor financially interested in its outcome.

IN WITNESS WHEREOF, I have hereunto set my hand this 3rd day of November, 2017.

Marjorie Jackson

Marjorie Jackson, CET