

NORTH DAKOTA LEGISLATIVE COUNCIL

Minutes of the

PUBLIC SERVICES COMMITTEE

Thursday, May 6, 2004
Roughrider Room, State Capitol
Bismarck, North Dakota

Senator Aaron Krauter, Chairman, called the meeting to order at 9:00 a.m.

Members present: Senator Aaron Krauter; Representatives Randy Boehning, Rod Froelich, Arlo E. Schmidt, Mike Timm

Members absent: Senator Jerry Klein; Representatives Chet Pollert, John Warner

Others present: See attached appendix

SURETY BONDS STUDY

At the request of Chairman Krauter, committee counsel presented a bill draft [50057.0100] to provide auctioneers and auction clerks the option of providing liability and errors and omissions insurance in lieu of a bond. He said the present bond required for an auctioneer is in an amount not less than \$5,000 and the bond required for an auction clerk is in an amount not less than \$10,000. He said the bill draft provides the option of providing at least \$100,000 per occurrence and \$500,000 annual aggregate limit of public liability insurance and errors and omissions insurance instead of providing a bond. He said the \$100,000 minimum limit in public liability insurance is the same minimum limit as for a master electrician. He said the \$100,000/\$500,000 minimum limit is the same as is required of a real estate broker or salesperson in obtaining errors and omissions insurance.

Representative Schmidt said the bill draft will not affect many auctioneers but may reduce costs for auctioneers who are real estate agents.

In response to a question from Senator Krauter, committee counsel said insurance is a contract. He said the particular terms of the contract govern what is included in the coverage. He said the errors and omissions policy for a real estate agent most likely would not cover errors and omissions of an auctioneer.

Mr. William G. Peterson, Vice President and Public Affairs Officer, CNA Surety Company, Sioux Falls, South Dakota, presented testimony on private surety companies. He provided a handout entitled *Surety-ship: A Practical Guide to Surety Bonding*. A copy of the handout is on file in the Legislative Council office. He said his testimony covers three main areas-- Western Surety, auctioneer bonds, and recovery funds.

Mr. Peterson said in 1997 Western Surety became a wholly owned subsidiary of CNA Surety. He said Western Surety is one of the oldest and largest surety companies. He said Western Surety is one of many companies in a competitive marketplace. He said there are 252 insurance agents in this state that sell Western Surety bonds. He said the prices of the bonds are based on what the market will bear and what is the cost to a surety company. He said surety companies are regulated under the property and casualty insurance laws in all 50 states.

Mr. Peterson said a bond is a three-way contract between a principal, for instance an auctioneer, a surety, and an obligee, usually a government entity. He said a surety bond is a form of public protection. He said surety underwriting evaluates three areas. The first area, he said, is the number of years in business and the reputation of the person seeking the bond. He said the second area is the financial stability and ability of the person seeking the bond. The third area, he said, is considering the agent's recommendations as to character issues. He said an auctioneer bond is to ensure that a consumer receives proper payment for goods sold by an auctioneer. He said in some states the bond covers fees and taxes that are paid to the state.

Mr. Peterson said in 30 states, Western Surety pays 12 percent on claims for the bonds of auctioneers. He said auctioneers have a high amount of claims compared to other bonded persons. He said used motor vehicle dealers have a higher percentage payout for claims. He said Western Surety has not paid on a bond in North Dakota for an auctioneer in a long time. He said the commission paid to an agent is 20 to 25 percent of the price of the bond. He said Western's market share has dropped from 80 percent of the market 15 years ago to 63 percent at present. He said the drop is the result of market competition.

Mr. Peterson said some states have recovery funds instead of requiring a bond. He said Louisiana had a recovery fund but it is returning to private bonding. He said Minnesota has a recovery fund for contractors and Virginia has a recovery fund for motor vehicles and both states are investigating a return to private bonding. He said a negative with a recovery fund is that most recovery funds require that all legal means be exhausted before there is recovery from

the fund. In other words, he said, a person first must obtain a judgment in a court.

In response to a question from Senator Krauter, Mr. Peterson said a 12 percent payout on auctioneers' bonds is determined by dividing the revenue by the amount paid for claims. He said he reviewed the records and there have been no claims against auctioneers in this state in the last four years. He said Western Surety has a \$100 minimum for most bonds. He said the cost for an auctioneer bond is \$100. He said there are other companies that will write an auctioneer bond for \$50.

In response to a question from Representative Timm, Mr. Peterson said an auctioneer bond for \$5,000 and an auction clerk bond for \$10,000 are both \$100 because of the minimum. He said to make a claim on the bond, a person would contact the Public Service Commission or write the surety company. He said the surety company would investigate the claim and pay the claim if valid. He said the \$5,000 limit for auctioneers and \$10,000 limit for auction clerks is an aggregate liability for a year.

In response to a question from Representative Boehning, Mr. Peterson said the majority of states have a bonding requirement for auctioneers in the range of \$10,000 to \$20,000. He said the highest requirement is approximately \$25,000. He said the cost of a bond for auctioneers is \$5 per \$1,000 of coverage with a \$100 minimum.

In response to a question from Representative Schmidt, Mr. Peterson said North Dakota auctioneers have been profitable to Western Surety because Western Surety has not had to pay any claims recently. He said the cost of a Western Surety bond for auctioneers was raised from \$50 to \$100 because the minimum for bonds was raised in that amount.

In response to a question from Representative Schmidt, Mr. Peterson said a surety company has the right of recovery against an auctioneer if the claim is paid on the bond. He said a bond is basically the surety company lending the surety company's credit to the auctioneer. He said Western Surety recovers about 10 cents on the dollar on all claims. He said a bond is canceled if a claim is made on the bond because the person has shown that they are a harm to the public. He said a bond is meant to protect the public.

In response to a question from Representative Froelich, Mr. Peterson said the cost of bonds ranges from \$5 to \$50 per \$1,000 of coverage.

Ms. Illona Jeffcoat-Sacco, Executive Secretary, Public Service Commission, provided testimony on the bill draft. She said the bill draft does not affect licensing functions of the Public Service Commission.

Representative Schmidt said although \$10,000 in bond coverage does not cover the amount of money brought in during most sales, raising the amount of bond may place an unnecessary burden on auctioneers.

Representative Froelich said cattle buyers are bonded for \$50,000 and that does not cover one load of cattle. He said increasing the bond for auctioneers would set a precedent that would place a burden on other businesses in this state.

Representative Timm said he is opposed to raising any required minimum for a bond.

In response to a question from Representative Boehning, committee counsel said the protection afforded by a bond is the review and investigation of the person bonded by a surety company.

Committee counsel provided copies of information provided by Mr. Jeff Bitz, Insurance Department, at a previous meeting. The information included the state bonding fund balance as of September 30, 2003, open bond claims against the fund, and a claim balance report for January 2004. In addition, information included a list of the 2,920 obligees bonded under the fund and the amount of the bond for each obligee. A copy of each handout is on file in the Legislative Council office.

Mr. Bitz provided testimony on the handouts. He provided a handout on the state bonding fund balance as of December 31, 2003, and open bond claims as of March 10, 2004. He said the fund balance on December 31, 2003, was \$3,549,000. He said the increase in the fund balance is attributed to investment income. He said the fund will transfer \$1.5 million to the general fund by the end of this fiscal year. He said the \$2 million threshold for premiums should not be triggered this biennium. He said the claim by the Fargo Park District is for \$226,000 plus interest from the date of the claim. A copy of each handout is on file in the Legislative Council office.

Representative Timm said the park board hired an employee that stole money from the park board and made a profit by receiving interest on the claim.

In response to a question from Representative Timm, Mr. Bitz said the Minot Air Force Base is bonded under the fund because of the school district.

In response to a question from Senator Krauter, Mr. Bitz said it is very difficult to collect on claims paid because the party that stole the money usually does not have any money. He said the legal system must be used to collect from these people and that is administratively burdensome. He said some parties are in prison. He said the recovery rate is not very good and compares with the 10 percent recovery rate of the private sector.

In response to a question from Representative Schmidt, Mr. Bitz said the state bonding fund balance in 1995 was approximately \$4.4 million.

At the request of Chairman Krauter, committee counsel presented a bill draft [50059.0100] creating an application procedure under the state bonding fund. He said the bill draft continues the concept enacted in 1999 Senate Bill No. 2360 to remove specific references to state officials being required to

have a bond. He said they are required to have a bond en masse. He said the goal of the bill draft was to have an application procedure in which the obligee requests a bond in an amount based on the amount of money and property handled and the opportunity for defalcation. He said the bill draft places more responsibility on the obligee to provide information to the Insurance Commissioner and to review matters relating to the bond. He said the main substantive provisions require an application on a biennial basis or when there is a change in coverage requested and require the application to include certain information, including 25 percent of the money in control of the public officials or employees for which the bond is requested for the preceding year based on total monthly balances. He said this is the standard used by the State Auditor to determine if a bond is adequate, except the State Auditor looks at daily balances. He said the bill draft provides that interest on a claim runs from the date of filing of the claim. He said the bill draft limits liability on the fund to two years before the date of filing of the claim. He said this places the responsibility to find wrongdoing within two years on those in a position to find the wrongdoing.

In response to a question from Representative Boehning, committee counsel said counties, cities, most school districts, and park districts are audited on a biennial basis. He said they are audited by the State Auditor or a private firm. He said townships and other political subdivisions are not required to have a biennial audit.

AGRICULTURAL INSPECTION AND STANDARDS FUNCTIONS TO PUBLIC SERVICE COMMISSION STUDY

At the request of Chairman Krauter, committee counsel presented information on a study conducted during the 1975-76 interim by the Legislative Council's interim Industry, Business and Labor "A" Committee on the jurisdiction of the Public Service Commission. He said the study provides historical information on the areas of regulation transferred from the Public Service Commission to other state agencies. He said the study assigned to this committee is on the transfer of agriculturally related inspections and standard functions to the Public Service Commission. He said the Industry, Business and Labor "A" Committee recommended a bill to transfer licensing responsibility for auctioneers from the Public Service Commission to an occupational board. He said the bill did not pass.

Ms. Jeffcoat-Sacco provided written testimony on revenues and expenses associated with the Public Service Commission's grain elevator licensing functions and the agriculturally related weights and measures functions. Mr. Alan Moch, Director of Safety and Testing, Public Service Commission, provided specific testimony on Attachment 1 of her

testimony. A copy of her testimony is on file in the Legislative Council office. The draft of her testimony with additional information related to total expenses and revenues was provided to the committee and is on file in the Legislative Council office.

In response to a question from Representative Schmidt, Ms. Jeffcoat-Sacco said the other category includes other expenses such as dues and memberships paid by the Public Service Commission to belong to regulatory-related groups.

Representative Schmidt said fees paid by auctioneers is a good portion of the revenue because the only expense is to mail the envelope to collect more fees.

Representative Froelich said the Public Service Commission makes approximately \$10,000 from licensing auctioneers.

At the request of Chairman Krauter, committee counsel presented a bill draft [50058.0100] to transfer regulation of wholesale potato dealers from the Seed Department to the Public Service Commission. He said the major change in the bill draft was changing the word "commissioner" to "commission." He said the only other substantive change was to remove the continuing appropriation to the Seed Department for fees and other charges collected under the chapter.

Mr. Ken Bertsch, Seed Commissioner, State Seed Department, provided testimony on the bill draft. He said the bill draft was meant as a point of discussion and after discussing the concept of the bill draft with the Public Service Commission, the Public Service Commission and Seed Commissioner agreed to work together to make the law more effective. He said the bill draft provides a straight transfer of duties; however, at present the regulation of wholesale potato dealers is not an effective program because of changes in the industry. He said the major reason for moving regulation to the Public Service Commission is because of large processors purchasing large volumes of potatoes. He said the current program is not fitted to these types of entities. He said the State Seed Department has the regulation of wholesale potato dealers because it administers most everything else related to potatoes. He said the program has outgrown the department. He said the department is a seed agency, not a regulatory agency.

Senator Krauter said it makes some sense to transfer the duties to the Public Service Commission because the sale of potatoes is the sale of commodities that are otherwise regulated by the Public Service Commission.

Ms. Jeffcoat-Sacco provided testimony on the bill draft. She said further working sessions with the State Seed Department are needed and it would be better to work out the issues with the department than to use the bill draft.

In response to a question from Representative Timm, Ms. Jeffcoat-Sacco said there will probably be no additional cost to transfer the present program to

the Public Service Commission. She said there would be more cost if duties were added to meet the changes in the wholesale potato dealer industry. She said the cost depends on the regulatory scheme the Legislative Assembly decides is best.

STATE SEED DEPARTMENT STUDY

At the request of Chairman Krauter, committee counsel reviewed a bill draft [50027.0100], previously presented, that clarified state seed law. He said a question at a previous meeting related to the appropriateness of the per diem of \$62.50. He said the per diem for state officials has been decoupled from the legislative per diem. He said the most common amount of per diem for commissions similarly situated to the State Seed Department is \$62.50 and \$75.

Mr. Bertsch provided written testimony on the bill draft. A copy of his testimony is on file in the Legislative Council office. He proposed a change to return to nine-month germination testing instead of the proposed change of 12 months.

Mr. Jim Swanson, Manager of Regulatory Programs, State Seed Department, answered questions for the committee.

In response to a question from Representative Froelich, Mr. Swanson said all states vary as to germination testing for seeds. He said Minnesota and Montana are 12 months and South Dakota is nine months on some and 12 months on others. He said a seed company must label as to the law of the receiving state. He said the 12-month germination testing standard was considered to provide consistency. He said soybeans and edible beans are fragile

and the 12-month standard may not provide adequate consumer protection. He said the consumer protection issues that are addressed by a nine-month standard are why the State Seed Department changed the time period back to 12 months. He said there are longer times for certain seed in the bill draft.

In response to a question from Representative Timm, Mr. Swanson said seed companies are accustomed to the nine-month germination testing standard in this state.

Senator Krauter said the main issue with a nine-month or 12-month standard is seed carried over from one year to another. He said a 12-month standard would allow some seed to be carried over to the next year without a retest.

In response to a question from Senator Krauter, Mr. Bertsch said because the germination testing standard only applies to carryover seed it would only apply to a small amount of seed in limited circumstances. He said those circumstances might arise if there is a shortage of seed.

Representative Schmidt said the label on seed should advertise that this state is No. 1 in seed production in the nation.

No further business appearing, Chairman Krauter adjourned the meeting at 12:04 p.m.

Timothy J. Dawson
Committee Counsel

ATTACH:1