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via e-mail [jchristian@utah.gov]

Ms. Jen Christian, MCM, PIR
Market Conduct Examiner
Utah Insurance Department
State Office Building, Suite 3110
Salt Lake City, UT 84114-6901

Re: **Response to Recommendation Letter dated November 20, 2014**
Investigation # 63777, Zenefits FTW Insurance Services

Dear Ms. Christian:

We write in response to your letter of November 20, 2014, which finds that Zenefits' business model illegally induces the purchase of insurance. Not only is this conclusion unsupported by the facts or law, it sets Utah apart from every other state in the Union, to the detriment of its business environment and its consumers. It sends the clear message that Utah insurance regulators are hostile to innovation, and that insurers and brokers in Utah run the risk of prosecution if they deviate from regulators' subjective opinions of how they should operate.

The Department's determination will also have ripple effects beyond the insurance marketplace, pegging the State as inhospitable to companies that use technology and innovation to reach new markets or disrupt existing ones. When regulators prefer to interpret statutes in a way that assumes the illegality of new business models, particularly when a fair reading of the statute requires the contrary result, innovative companies will invariably conclude that doing business in Utah isn't worth having to fight the preference for the status quo. The Department's decision is the equivalent of planting a sign at the state line that says, "Innovation Not Welcome."



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Specifically, the Department has concluded:

- that Zenefits offers a wide range of human resources products and services, some of which are offered for a fee and others that are offered free-to-all, and that it offers these services without any requirement of or special benefit for buying insurance from Zenefits;
- that “connecting” insurance with Zenefits’ many fee-based and free-to-all non-insurance products and services creates “advantages for customers to have a single internet access site to manage all [human resources] and insurance needs”;
- that aggregating of insurance and non-insurance services and products “creates an inducement violation,” apparently because employers might want to buy insurance from Zenefits because it’s efficient and convenient for them to consolidate their human resources and insurance needs with one company;
- that Zenefits’ free services are also “indirect rebates” for buying insurance, even though they are available free to anyone regardless of whether they buy insurance from Zenefits, another broker, and even if they aren’t in the market for insurance; and
- that the only way to cure these defects is to charge everyone in Utah for the free services, even the 85% of Zenefits’ customers who buy no insurance, because the Department believes there is a possibility that they might be “induced” to buy insurance.

The Department’s ruling requires Zenefits to start charging fees it does not want to charge and that its users do not want to pay. Ironically, the Department concluded this result is required by, of all things, a consumer protection statute.

The import of these findings is unmistakable: The Department believes that an insurer or broker illegally “induces” a customer to buy insurance by providing the mere convenience of also offering non-insurance products or services. As applied here, this rule reduces to an assertion that Zenefits makes it so convenient for consumers to buy its insurance products, that they just might do so. And indeed, some do, in the same way that consumers choose every day to buy products from one broker over another for myriad reasons—with ease, convenience, and customer support arguably being second only to price. In response to consumer demand, more and more companies are finding innovative ways to offer both insurance and non-insurance



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products. It is not enough to say that “connecting” insurance with non-insurance products is illegal merely because it’s convenient or makes buying insurance easier. But that is exactly what the Department has concluded, and it effectively bans companies from offering their customers both insurance and non-insurance products.

The Department attempts to skirt this effect by saying that it is permissible to offer both insurance and non-insurance services *if* the company charges whatever the Department believes is “fair market value” for what it now provides for free. But the reality is that no company can possibly do so in a way that would satisfy the Department’s broad interpretation of the anti-rebate statute. It is impossible as a practical matter to charge for customer service, document and data storage, access to web platforms, and other services that companies *must* provide incidental to offering non-insurance products. Take, for example, a bank that offers a range of banking and investment services and insurance products, as most major banks now do. How does the bank quantify and charge for the ease of conducting both banking, investment and insurance services in one place? And how does the bank avoid rebating when it offers free investment advice and checking accounts to its customers who eventually just might decide to buy insurance from the bank as well? The answer is that it can’t. And even if they could charge for everything, these companies would be so disadvantaged as against competitors that do *not* offer insurance as to make it impracticable as a matter of business reality. The result of the Department’s interpretation, if allowed to stand, is that no multifaceted business offering both insurance and non-insurance products will be able to comply with Utah’s anti-rebate law.

The Department’s interpretation fosters these absurd results because it has no limiting principle. But the statute the Department purports to interpret certainly does. The text, legislative history, and purposes of the anti-rebate statute all confirm that a service is only an “inducement” if it is offered in exchange for buying insurance. As the bill’s primary Senate sponsor told the Senate, the statute “prohibits inducements . . . inducement’s something that, *in exchange for* writing the policy, we’ll give you certain perks or benefits.” The services identified by the Department as inducements are not, by definition, offered by Zenefits in exchange for insurance: users access them on equal terms regardless of whether they also buy insurance.

Now, to remedy what it sees as a violation of the anti-inducement law, the Department proposes to require that Zenefits charge all of its Utah customers for every product and service it offers—even the more than 85% of customers that do not use Zenefits as their insurance broker. It has directed Zenefits to immediately discontinue offering free services and make clear in all advertising that “services are not free in the State of Utah.” (Department of Insurance Recommendation Letter Regarding Zenefits FTW Insurance Services (Nov. 20, 2014)



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(“Department Letter”) at 5.) This demand draws no distinction between Zenefits’ insurance clients and its non-insurance clients. The Department specifically finds that Zenefits is an inducement for those customers “who eventually purchase, renew, or terminate and transfer insurance contracts through Zenefits.” (Department Letter at 2.) Since Zenefits has no way of knowing which of its customers might eventually choose to purchase insurance, we can only comply with the Department’s mandate by levying a surcharge on every Utah customer. For this reason, Zenefits has stopped signing up new customers in Utah.

Zenefits respectfully declines the Department’s proposed settlement (which also included a substantial fine, a probationary period, and reporting requirements) and requests that the Department reconsider its preliminary findings and recommendations before requesting that the Attorney General initiate a formal adjudicative proceeding. Zenefits also appreciates and accepts the Department’s offer to meet to discuss the new information and legal analysis provided in this letter.

The Department Ignores That Zenefits’ Insurance And Non-Insurance Customers Access Its Platform And Services On Equal Terms.

We agree with the Department that “Zenefits does not operate like other insurance producers.” (Department Letter at 4.) It doesn’t. Zenefits is a technology company that provides an integrated platform for businesses to efficiently manage human resources and employee benefits. Offering insurance isn’t Zenefits’ sole reason for existence; insurance is just one part of a full complement of HR administration tools and employee benefit services and options that Zenefits offers.

The idea for Zenefits was sparked by its founder’s own experience as a small business owner. He saw firsthand how cumbersome and time consuming it is for business owners to manage employees and their benefits. Like most small business owners, he did not have an in-house HR department, and the day-to-day work of managing employees fell to him. He spent significant time each week filling out paperwork: Paperwork to hire employees. Paperwork to sign them up for insurance and other benefits. Paperwork every time an employee married, had a child or changed a name. Paperwork when an employee left the company. He saw that technology could integrate human resources and benefits and minimize the burden—and headaches—of hiring employees so that he and other small business owners could focus on growing the business.

He formed Zenefits, which has developed an internet software solution that eliminates the needless duplication of filling out paperwork for multiple disconnected benefit systems. Zenefits streamlines HR administration by automatically updating information for multiple benefits



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systems, which simplifies on-boarding, off-boarding, interim changes, and everything along the way. Zenefits' software pulls information from the employee's payroll file and populates the forms for all the benefits the employer selects for that employee—turning a mountain of paperwork into a few keystrokes and mouse clicks.

Here is how it works. Zenefits makes accounts available to everyone, for free. After the customer creates an account, the customer has immediate access to the Zenefits online HR platform and dashboard. Here, Zenefits offers a variety of services, some of which are entirely free (e.g., viewing and updating employee information and PTO tracking), and others for which there is a fee or charge (e.g., insurance and flex-spending accounts). Access to the platform and its free services is not conditioned *in any way* on the purchase of insurance or any other fee-based service from Zenefits, nor is there any discount on fee-based services if the employer also purchases insurance.

Zenefits' HR and benefit services are offered à la carte, and the employer chooses the services it wants. For example, an employer can use Zenefits only for PTO tracking—in which case, the customer pays nothing to Zenefits. Another customer might choose to use Zenefits for a full range of HR and benefits services. For most (but not all) of these services, customers pay a fee to Zenefits or to a third-party vendor from which Zenefits receives a commission. Services that are offered for free are offered free to everyone, irrespective of whether they purchase insurance from Zenefits. And for services on the platform that are fee-based, the rates are the same irrespective of whether a business purchases insurance or any other benefits through Zenefits. There is fundamentally no requirement that employers buy anything from Zenefits, much less insurance.

Our customer data demonstrates that, in fact, the vast majority of Zenefits users do not obtain insurance benefits from us. Nationwide, about 85% of users do not buy insurance from Zenefits. In Utah, the percentage of non-insurance users is even higher; about 87% of Zenefits users in the state have not purchased insurance. These customers, though, still have full access to the Zenefits platform and its services on the same terms as insurance clients. Under the Department's view of the law, however, Zenefits has to charge all of them for every non-insurance product or service it offers, on the chance that they might, at some point, also decide to buy insurance.

The Department's Interpretation Prejudices Consumers, Discourages Innovation, And Stifles Competition.

Zenefits may be different from traditional insurance producers, but it doesn't stand alone. The insurance market is changing. Driven by consumer demand for convenience and efficiency,



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companies in the modern economy are adopting innovative business models that integrate insurance and non-insurance products. The financial sector is at the forefront of this trend. Federal law now permits banks to offer insurance, and most now do. Tech companies like Zenefits will increasingly provide convenient, easier alternatives for employers and individuals to buy insurance and receive other products and services. Many major retailers are registered insurance producers in Utah and elsewhere—offering members a range of insurance products and services. Travel-related businesses—from car companies to airlines to travel booking services—offer trip insurance to customers. Even traditional insurance companies are expanding their products and services beyond insurance, and now offer financial products like retirement accounts and home loans.

There is no dispute, nor could there be, that Utah law allows for this sort of integration of insurance and non-insurance services. Yet the Department’s interpretation of the anti-rebating statute to deem it an inducement to “connect” insurance and non-insurance products legally and practically bars integration. The modern economy and evolving insurance market demand instead that regulators: (i) understand how integrated business models work to determine if they actually harm consumers or competition; and (ii) accept that they cannot apply a presumption of illegality just because an integrated business model is new or innovative or successful.

Thus far, the Department has declined to do either in its consideration of Zenefits’ model. Many of our users are small businesses owners. The platform not only reduces the costs of administration for small businesses, it makes it much easier for them to buy insurance and non-insurance products—meaning they will be more likely to offer less expensive or more comprehensive benefits to their employees. Unquestionably, public policy should encourage, or at least not stand in the way of, expanding Utahns’ access to employer-sponsored health plans and other benefits. When business models like ours make it easier to buy insurance, competing insurance brokers and insurers will inevitably do the same, and that enhances all Utahns’ access to insurance products and workplace benefits.

Zenefits is not the only business model that would be adversely affected by the Department’s constrained interpretation of the anti-rebating statute. Banks routinely offer “free” checking accounts to customers. Some waive foreign transaction fees on credit cards or provide free bill pay services. Retailers, of course, provide free and discounted services to customers every day. None of these businesses could offer any such discounts or free services under the Department’s rule because they also broker insurance—even for the vast majority of their customers who do not buy insurance from them. Thus, in light of the Department’s rule:



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- Zions Bank should evaluate the legality of free basic checking accounts because they might “induce” customers to buy its life insurance products, since they might find it more convenient to bank and buy insurance from the same company rather than multiple ones;
- Hertz should stop its loyalty rewards programs because the perks of skipping lines and receiving complimentary upgrades encourages customers to keep renting cars from Hertz and buying the rental car insurance it offers, rather than renting cars and buying insurance from competing companies; and
- Marriott should reconsider its decision to offer travel insurance in connection with its vacation clubs because it might be too convenient for customers to make travel plans and buy travel insurance on the same platform.

If the Department’s standard is that “connecting” free services with insurance products creates an inducement, then that’s the same as having no standard at all.

The anti-rebate statute is a blunt tool that when interpreted too broadly harms consumers, discourages competition, and manipulates the market. The Department’s findings and preferred remedy do just that. It is easier and more efficient to buy insurance in the context of an integrated platform that connects all HR services and benefits. Requiring that a broker charge more for this service reduces consumers’ ease of access to insurance. Utah businesses will be left with less efficient alternatives—more headache and higher costs. That has important consequences for employees, who will be offered fewer employer-sponsored benefits. As for its competitive effects, requiring that Zenefits charge minimum prices for non-insurance products artificially reduces competitive pressures on other insurance brokers *and* impairs the free market for non-insurance products by imposing minimum prices on only those companies that also sell insurance.

This result is out of sync with the modern information economy and undermines the stated purposes of the Insurance Code, which include “maintain[ing] freedom of contract and enterprise” and preserving a “health insurance market, characterized by competitive conditions, the spirit of innovation, and the exercise of initiative.” Utah Code Ann. § 31A-1-102(3) & (7).

The Department’s Interpretation Of The Anti-Rebate Statute Is Wrong.

When interpreting a statute, the “primary objective is to ascertain the intent of the legislature.” *Summit Operating, LLC v. Utah State Tax Commission*, 293 P.3d 369, 372 (Utah 2012) (internal quotations omitted). A statute’s words are the best evidence of the legislature’s



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intent, and it is important not to “view individual words and subsections in isolation.” *Id.* “Each part or section [must] be construed in connection with every other part or section as to produce a harmonious whole,” *id.*, and to “avoid interpretations which render some part of a provision nonsensical or absurd,” *Marion Energy, Inc. v. KFJ Ranch P’ship*, 267 P.3d 863, 869 (Utah 2011) (internal quotations and citation omitted). When the statute’s meaning is unclear from its language, Utah courts “seek guidance from legislative history.” *Id.* at 866-67 (internal quotations and citation omitted).

Four principles explain how the Department’s interpretation departs from the statutory text, legislative history, and policies underlying Utah’s regulatory scheme.

Principle 1: Under a fair reading of the statute, benefits are “inducements” only if offered in exchange for entering into, extending, or terminating an insurance contract.

Section 402.5’s “inducement” ban only prohibits brokers from providing benefits that are contingent upon or linked to the purchase of insurance. This transactional nexus requirement appears in subsection (1)(a), the operative provision banning inducements, and is repeatedly confirmed by the other provisions of the section that elaborate upon the ban’s scope.

Subsection 1(a) establishes the general inducement ban. Insurance brokers “may not induce a person to enter into, continue, or terminate an insurance contract by offering a benefit that is not [] specified *in the insurance contract*[] or *directly related to the insurance contract.*” Utah Code Ann. § 31A-23a-402.5(1)(a) (emphasis added). According to the Department, this language prohibits insurance brokers from offering any and all benefits unrelated to an insurance contract to any and all persons. Period. It refuses to acknowledge any exception for benefits completely unrelated to insurance transactions and leaves no room for insurance brokers to innovate to make it easier for Utah businesses to purchase insurance.

The Department reached this conclusion by overlooking the text’s transaction nexus requirement. It proscribes “offering a benefit” to “induce a person to enter into, continue, or terminate an insurance contract.” The statutory text does *not* prohibit “offering a benefit” for some purpose *other* than to induce a person to enter into, continue, or terminate an insurance contract. In this way, the statute distinguishes offering benefits in exchange for purchasing insurance (which are impermissible) from offering benefits that are not offered in exchange for purchasing insurance (which are permissible). Moreover, by twice referring to “the insurance contract,” subsection (1)(A) suggests the Legislature’s intent to prohibit only those benefits offered in the exchange for purchasing insurance—that is, benefits offered as part and parcel of entering into an insurance contract. The products and services the Department identified here as “inducements” fall firmly within the second camp: our non-insurance products and services are



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available to every user on equal terms without any regard to whether they buy any insurance product. A customer that also decides to buy insurance receives no benefits that are not available to every other customer on equal terms, except only the convenience of having insurance and non-insurance products on a single platform. There is absolutely no basis, then, to conclude that Zenefits is “offering a benefit” in exchange for buying, continuing, or terminating an insurance contract.

Other parts of the statute confirm that the legislature only sought to ban benefits offered in exchange for insurance. Subsection (4)(a) permits insurance brokers to engage “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.” *Id.* § 31A-23a-402.5(4)(a)(emphasis added). In other words, the Act permits brokers to provide people with benefits like meals, and perhaps movie tickets, so long as the benefits are “not conditioned on” a particular insurance transaction—while the same benefits become impermissible when they are “conditioned on” an insurance transaction. This makes sense. The Legislature recognized that insurance brokers live ordinary lives and should have the freedom, like all Utahns, to give gifts and benefits when they are not engaging in insurance transactions.

It is telling that the statute focuses on “rebates” in defining what constitutes an inducement. A rebate necessarily requires that the broker provide the “rebate” after first selling insurance to the customer. *See* Black’s Law Dictionary 1458 (10th ed. 2014) (defining “rebate” as “a return of part of a payment, serving as a discount or reduction.”). Reflecting the plain meaning of the term “rebate,” the statute provides that rebates consist primarily of “refunds”—yet another term that by its plain meaning requires, first, a sale of insurance.¹ When a broker provides products and services that are available to every user regardless of whether they ever buy insurance, as here, those products and services cannot be deemed to be either “rebates” or “refunds”—and is further evidence that the legislature only sought to prohibit “inducements” offered in exchange and as a quid pro quo for buying insurance.

Finally, the Department’s bulletin interpreting the anti-rebating statute recognizes that that a good or service is an “inducement” only if it is provided in exchange for buying insurance.

¹ The Act defines a rebate as “giving, or offering to pay . . . (i) *a refund* of premium or portion of premium; (ii) *a refund* of commission or portion of commission; (iii) *a refund* of all or a portion of a consultant fee; or (iv) providing services or *other benefits not specified in an insurance or annuity contract.*” Utah Code Ann. § 31A-1-301(145) (emphases added). To be sure, subparagraph (iv) makes no reference to a refund. Read in light of the plain meaning of “rebate” and in context of subparagraphs (i)-(iii), the legislature plainly intended the catch-all provision to stop brokers from circumventing subparagraphs (i)-(iii) by rebating premiums through discounted services rather than cash rebates. *See State ex rel A.T.*, 34 P.3d 228, 232 (Utah 2001) (general term to be construed to mean “things of the same kind’ as those specifically enumerated).



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In Bulletin No. 2031-5 (2013), the Department concluded that a product or service is offered for “fair market value” and is therefore not an inducement if the consumer pays “what anyone would pay with or without the purchase of an insurance product.” In other words, a broker provides a good or service for less than fair market value if its non-insurance customers pay one price but its insurance customers pay another, lower price—a prototypical quid pro quo, which encourages customers to buy insurance with the enticement of lower prices on unrelated products and services. Here, by contrast, there is no quid pro quo or exchange for buying insurance: Zenefits insurance and non-insurance customers access all of its products and services on equal terms.

Principle 2: Legislative history confirms that only benefits offered in exchange for insurance qualify as “inducements.”

The legislative history of the bill that enacted this section further confirms that the legislature intended to prohibit only those benefits offered in exchange for buying insurance. Representative Dunnigan—the bill’s sponsor in the House and an insurance broker himself—and Senator Bramble—the primary Senate sponsor—repeatedly made clear that only benefits linked to a specific insurance transaction qualify as inducements:

- On the Senate floor, Senator Bramble explained: “This bill prohibits inducements . . . inducement’s something that, ***in exchange for*** writing the policy, we’ll give you certain perks or benefits.”
- On the House floor, Representative Dunnigan likewise provided an example of the practices the bill prohibited: “***If you will let me sell you health insurance***, I will provide free payroll for your company.”
- Before the Senate Business and Labor Standing Committee, Representative Dunnigan again described prohibited inducements as “***If you buy health insurance*** from me, I will give you free legal service, or I will give you free payroll service, or I will give you free accounting services.”
- Before the House Business and Labor Standing Committee, Representative Dunnigan described problematic inducements as “including free legal, free accounting, ***if you buy a policy from me***” and explained that the bill was “trying to prohibit some of these more egregious activities—of promises, and under-the-table, and behind-the-door stuff that had been going on to try to obtain and retain business.”



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(emphases added). The bill sponsor’s repeated statements that the bill prohibits benefit for insurance exchanges confirms that the legislature only intended section 402.5 to bar benefits offered in the context of an insurance transaction.

Principle 3: The absurd results fostered by a contrary interpretation confirm that “inducements” are limited to benefits offered in exchange for insurance.

Indeed, were “induce” not limited to benefits offered during insurance transactions, absurd results would follow, in addition of the ills flowing from the Department’s interpretation discussed above. Representative Dunnigan, the sponsor of the legislation and an insurance broker, for example, would violate the statute by providing constituent services, on the off chance that it might induce them to buy insurance from him in the future. So too would any insurance broker who made a charitable contribution to a church (undoubtedly a “benefit”) and the church also happened to later enter into or renew an insurance contract. A broker that operates multiple businesses would violate the statute by offering any promotion unrelated to insurance—a bank offering free checking or a special interest rate or a retailer offering discounts on non-insurance products—if a small portion of customers receiving those benefits also bought insurance.

Principle 4: The statute expressly permits storing and using data for enrollment purposes.

The Department also fails to take into account § 402.5(4)(f),(h), which explicitly authorize Zenefits’ “free importing, storing and subsequent use of the electronic employee data.” According to the Department, “the ease of using Zenefits already imported, stored and free electronic employee data in setting up the customer’s employee insurance” induces customers to buy insurance from Zenefits. (Department Letter at 3.) But subsection (4)—“Items *not prohibited* by Subsection (1)” —specifically authorizes brokers to provide customers with just this convenience. Subsection (4)(f) permits “*preparing or providing a form* that is directly related to an insurance product purchased from, or offered by, the licensee” and subsection (h) permits “*providing enrollment and billing assistance, including ... providing technology services such as an electronic enrollment platform or application system.*” Utah Code Ann. § 31A-23a-402.5(f) & (h). That is what Zenefits does. It provides an “electronic enrollment platform” that allows employers to easily import their employee data and then uses this data to “prepar[e] form[s]” “directly related” to Zenefits’ insurance products.



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The Department's Interpretation Of The Anti-Rebate Statute Exceeds Its Authority.

The Department's application of the anti-rebate statute violates Section 5 of the Federal Trade Commission Act of 1914 (the "FTC Act"), which outlaws unfair competition, because it is acting as the hub of a conspiracy by entrenched Utah insurance brokers to preclude competition from Zenefits and impede innovation. *See* 15 U.S.C. § 45. The scope of Section 5 is at least as broad as Section 1 of the Sherman Act, which outlaws conspiracies in restraint of trade. 15 U.S.C. § 1.

The Federal Trade Commission routinely brings actions under Section 5 against state agencies or officials acting on behalf of entrenched commercial interests seeking to shield themselves from competition in a manner not "clearly articulated and affirmatively expressed as state policy." *California Retail Liquor Dealers Ass'n v. Midcal Aluminum*, 445 U.S. 97, 105 (1980) (internal quotations omitted). For example, the FTC sued the city of Minneapolis, charging it with unfair competition by combining with taxicab operators to impose regulations that limited the number of taxicab licenses, increased fares, and eliminated competition in violation of the federal antitrust laws. The complaint against Minneapolis was withdrawn after the city revised its ordinance to permit more competition.²

More recently, the FTC successfully sued the North Carolina State Board of Dental Examiners for precluding non-dentists from providing teeth-whitening services in North Carolina, in competition against dentists. The FTC found that the State Board was effectively controlled by dentists and had violated Section 5 of the FTC Act by depriving consumers of price-competition for tooth whitening. The Fourth Circuit affirmed, finding no state-action immunity. *North Carolina State Bd. of Dental Exam'rs v. FTC*, 717 F.3d 359 (4th Cir. 2013), cert. granted, 134 S.Ct. 1491 (2014). *See also Goldfarb v. Virginia State Bar*, 421 U.S. 773, 791 (1975) (holding that, although the State Bar was a "state agency by law," it was not immune from the antitrust laws when it "foster[ed] anticompetitive practices for the benefit of its members"). The Department's interpretation of the anti-rebate statute has the same anti-competitive effects.

A state enjoys sovereign immunity from the antitrust laws only if its actions are undertaken pursuant to a "clearly articulated and affirmatively expressed as state policy" to replace competition with regulation. *California Retail Liquor Dealers Ass'n*, 445 U.S. at 105; *See generally Parker v. Brown*, 317 U.S. 341 (1943). Here, the statute that the Department

² *See generally* FTC, 1985 ANNUAL REPORT 5 (1985), available at <http://www.ftc.gov/os/annualreports/ar1985.pdf>.



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purports to enforce does not on its face or under any reasonable construction seek to displace competition among insurance brokers. To the contrary, it expressly seeks to promote “competitive conditions, the spirit of innovation, and the exercise of initiative” and “maintain[ing] freedom of contract and enterprise.” Utah Code Ann. §31A-1-102.

While the states are also exempt from the antitrust laws under the McCarran-Ferguson Act to the extent they are regulating competition in the “business of insurance,” 15 U.S.C. § 1011, there is no such exemption for the regulation of non-insurance products—even ones offered by companies that are also insurers or insurance brokers. As the U.S. Supreme Court has explained, the Act “does not exempt the business of insurance companies from the scope of the antitrust laws. The exemption is for the ‘business of insurance,’ not the ‘business of insurers.’” *Group Life & Health Ins. Co. v. Royal Drug Co.*, 440 U.S. 205, 210-11 (1979).

The regulation of non-insurance services and products, which by the Department’s own admission are not directly related to the provision of insurance, falls far outside the state’s exemption from the antitrust laws. The “business of insurance” is limited to the relationship between insurer and insured as such, the type of policy that can be issued, its reliability, interpretation, and enforcement. *See Union Life Ins. v. Pireno*, 458 U.S. 119, 128 (1982). The Supreme Court has recognized that one “indispensable characteristic of insurance” is the “spreading and underwriting of a policyholder’s risk,” and that the McCarran-Ferguson Act’s legislative history “strongly suggest that Congress understood the business of insurance to be the underwriting and spreading of risk.” *Group Life*, 440 U.S. at 211-12, 221.

Providing free features and software on the Zenefits dashboard for non-insurance products does not involve spreading and underwriting of a policyholder’s risk or affect the type of policy which could be issued, its reliability, interpretation, and enforcement. Indeed, the Department can point to no decision of the U.S. Supreme Court or any other federal court that blesses the use of McCarran-Ferguson powers to regulate non-insurance products and services in the way the Department has. Indeed, courts have repeatedly declined to apply the exemption in analogous contexts.³ Thus, regulating these non-insurance offerings is beyond the scope of

³ In *Ticor Title Insur. v. FTC*, 998 F.2d 1129, 1137 (3d Cir. 1993), the Third Circuit held that the FTC had jurisdiction to bring an action against title insurance companies that had agreed on fees for title searches. The court reasoned that “[t]he title search and examination does not itself spread or transfer risk.” *Id.* at 1134. *See also Pireno*, 458 U.S. at 134 n.8 (“ancillary activities” that do not affect performance of the insurance contract or enforcement of contractual obligations do not enjoy the antitrust exemption for laws regulating the “business of insurance.”). Similarly, in *American Standard Life & Accident Ins. Co. v. U.R.L., Inc.*, 701 F. Supp. 527, 532-33 (M.D. Pa. 1988), the court held that an insurance agent’s attempt to induce customers to switch policies is not the business of insurance. And in *In re Ins. Brokerage Antitrust Litig.*, 618 F.3d 300, 356-57 (3d Cir. 2010), the Third Circuit held that a conspiracy between an insurance broker and insurers that limited competition was subject to the



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insurance regulation as contemplated by the McCarran-Ferguson Act because it is not the “business of insurance” and exceeds the scope of the agency’s authority.

The Department’s Interpretation Of The Anti-Rebate Statute Is Unconstitutional.

The Department’s interpretation of the anti-rebate statute is unconstitutional because it impermissibly burdens interstate commerce and has no rational connection to the state’s interest in protecting consumers. At a minimum, these constitutional concerns are so substantial that the Department must interpret the statute, as the statutory text requires, so as to avoid calling the law’s constitutionality into question. *Cf. How v. Tax Comm’n*, 10 Utah 2d 362, 365 (“[I]f there is doubt or uncertainty as to the meaning to be given to a statute, one of which would make it unconstitutional and the other constitutional, the latter should be given effect.”).

The anti-rebate statute as interpreted by the Department is unconstitutional if its incidental burdens on interstate commerce outweigh its benefits to the state. *See Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970). The notion that a company cannot offer both insurance and non-insurance products, or that it must charge a minimum price for services incidental to non-insurance products (assuming that’s even possible), will have profound effects on interstate commerce. According to the Department, Utah law actually or effectively prohibits companies from offering both insurance and non-insurance products, even though doing so is commonplace nationwide. These businesses must adopt business practices unique to Utah, which not only increases their costs and burdens the efficiency of their interstate operations, but also gives a competitive advantage to wholly in-state companies that do not have to have one set of products for Utah and another for everywhere else. *See Bibb v. Navajo Freight Lines, Inc.*, 359 U.S. 520, 529-30 (1959) (striking down a regulation because the state imposed requirements “out of line with the requirements of almost all the other States,” which posed “great burden . . . and inconvenience on those . . . entering or crossing its territory.”

Here, the state cannot insulate the burden it seeks to impose from Commerce Clause challenge because it cannot point to any state interests demonstrably furthered by interpreting the anti-rebate statute in this manner. *See Pike*, 397 U.S. at 142. Indeed, as discussed above, the Department’s ruling *thwarts* the state’s interests in protecting consumers and ensuring healthy competition in the insurance market. Moreover, even if there may be minor ways in which such a law furthers a legitimate state interests, the state will not be able to show either (i) that these

antitrust laws. *Accord Merchants Home Delivery Serv., Inc. v. Frank B. Hall & Co.*, 50 F.3d 1486, 1491 (9th Cir. 1995) (explaining the activities of a broker who allegedly collected money for false claims was “not even arguably the business of insurance”).



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benefits outweigh the heavy burden placed on interstate commerce; or (ii) that it could not achieve the same benefits through less burdensome means. *See id.*

Because the Department's ruling actually impedes the anti-rebate statute's dual goals of protecting consumers and preserving competition, it renders the statute unconstitutional under a host of other federal constitutional provisions—all of which require at least a minimal showing that the law as applied has no rational relationship (i.e., it does not reasonably advance) the state's purported interests. *See City of Cleburne v. Cleburne Living Center*, 473 U.S. 432, 440 (1985) (a state law violates the Equal Protection Clause if it draws classifications that are not "rationally related to a legitimate state interest"); *United States Trust Co. of New York v. New Jersey*, 431 U.S. 1, 22 (1977) (a state law violates the Contracts Clause if it is not a "reasonable condition" that advances "the public purpose justifying its adoption"); *Nebbia v. New York*, 291 U.S. 502, 537 (1934) (a state law violates the Due Process Clause if it does not "have a reasonable relation to a proper legislative purpose").

The Department's Conclusions Are Based On A Number Of Inaccurate Factual Findings.

The Department bases its conclusions and recommended penalties against Zenefits on an unsupported interpretation of the statute that contradicts the text of the statute and its legislative history and undermines the express objectives of the Insurance Code to promote competition and innovation. But that is not all. The Department's conclusions also rest on a number of inaccuracies:

- Page 3 of the Department Letter provides: "As part of setting up the free initial Zenefits account, Zenefits requires that account customers allow Zenefits to import the customers' electronic employee data." This is inaccurate. Zenefits does not require customers to import payroll data or to sign up with a payroll service. Customers may do so if they choose. Customers that do not have a payroll provider or do not want to link Zenefits to their payroll data may manually input data regarding their employees.
- Page 4 of the Department Letter states: "At the time the Department's investigation began, Zenefits advertised on their [sic] website, 'Our technology allows us to operate profitably on insurance commissions alone, which allows us to keep Zenefits free.' Zenefits now claims that the company operates profitably on the revenue share paid by the service providers in its system, allowing Zenefits to remain free to a customer. If this is indeed true, Zenefits has violated" The referenced statement has not been on our website for nearly six months (a long time in the lifespan of a 2-year-old company). The Department's letter fails to acknowledge that Zenefits advised the Department that the



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cited language was in the process of being updated when Utah's investigation began. When Zenefits was initially founded in California its focus was on its ability to generate sustainable insurance commission revenue. As the company has evolved, it has added additional services, and it now derives significant revenue from non-insurance services. The update to the information on the website reflected this evolution. It was replaced with new language within a few business days after Zenefits became licensed in Utah. Zenefits continues to develop new service modules that it anticipates will provide it with additional revenue sources, and will openly discuss the costs and benefits of those new services with its customers.

- Page 3 of the Department Letter includes, as item No. 1 in a list of “additional considerations,” a lengthy paragraph, the gist of which seems to be that Zenefits earns commissions as a result of insurance sales, and then devotes that revenue to develop innovative software solutions – thus making the solutions and services “violating inducements and indirect rebates.” There are factual assertions in this paragraph that are inaccurate and conclusions that are unsupported:
 - Zenefits openly embraces the fact that brokering insurance is a major component of Zenefits’ business and hence its revenue. Zenefits is an excellent insurance broker, and in that capacity it adds value for all of its insurance clients. But the allegation that insurance sales is the “most important part of the company’s purpose” is not true. Simply put, Zenefits’ purpose is to be a one-stop integrated platform for employers to manage all aspects of HR and employee benefits, and potentially to manage other aspects of their businesses. In the same way that Amazon started as an on-line bookseller, book sales remain part of Amazon’s business model, but book sales are not the “most important part of the company’s purpose.”
 - Zenefits also strenuously disputes the Department’s assertion that “Zenefits business model is mainly driven by insurance commissions, not by the terms, conditions or benefits found in any insurance policy itself.” This finding suggests that Zenefits is focused solely on the generation of commission income, not on serving its customers by providing them the tools and information they need to select, apply for and administer their insurance benefits. That is both insulting and inaccurate. Zenefits has invested tens of millions of dollars to develop software and gather detailed market and plan data that allows consumers to comparison shop among insurance plans and quickly and efficiently sign up for



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and manage their insurance benefits. Ironically, it is these very innovations—making it easy for customers to enroll and manage their health insurance benefits by linking to existing employee data—that the Department proposes to penalize.

- Finally, there is nothing illegal or inappropriate about using commission revenue to develop and provide additional services to customers. Indeed, the Department expressly permits brokers to pay for and provide software and other resources so long as they are directly related to insurance sales. This form of investment becomes problematic only if the company does not have the liquidity to respond to commission charge-backs from insurance carriers when customers cancel their insurance early. That is a fact-intensive analysis. The Department has not reached such a conclusion—nor could it—because Zenefits operates in a financially stable manner given its investor capital, insurance commissions, revenue from third party service providers, and revenue from services it provides customers directly.

* * * * *

For these reasons, we request that the Department reconsider its conclusions with respect to our business model and its interpretation of the anti-rebating statute. The Department's broad interpretation of the anti-rebating statute will negatively affect competition in the insurance industry and beyond, to the great detriment of Utah's businesses and residents. The Department should, instead, adopt a narrower interpretation of the statute in line with its text, history, and policy goals, and conclude that businesses like Zenefits may offer insurance and non-insurance products consistent with Utah law so long as all of their products are offered in the same terms to all customers and they offer no inducements as a quid pro quo for purchasing insurance.

If you have any questions or require further information, please do not hesitate to call. We look forward to meeting with the Department to discuss these matters further.

Very truly yours,

A handwritten signature in black ink that reads "Thomas J. Welsh".

Thomas J. Welsh