

Minnesota Attorney General: Administrative Rules Proceedings

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SF-00006-05 (4/86)

STATE OF MINNESOTA

Office Memorandum

DEPARTMENT : ATTORNEY GENERAL

DATE : September 14, 1987

TO : RICHARD G. GOMSRUD
Commerce Division

FROM : MARTHA CASSERLY
Special Assistant
Attorney General

PHONE : 6-6204

SUBJECT : In the Matter of the Adopted Rule Relating to Financial Institution Audit Control Policies

The above-referenced rule has been approved as to its legality by the Attorney General on September 9, 1987.

Enclosed is the agency's copy of the approved rule. This office has already filed two copies with the Secretary of State, who will forward one copy to the Revisor of Statutes. The fourth is being retained by this division of the Attorney General's Office for its records.

Also enclosed are any petitions, requests, submission or comments received by the agency and any extra copies of documents which the agency submitted to the Attorney General.

In order for a permanent rule without a hearing to become effective, your agency must publish a notice of adoption in the State Register in accordance with Minn. Stat. § 14.27. An emergency rule becomes effective five working days after approval by the Attorney General; however, the agency must publish a notice in the State Register in accordance with Minn. Stat. § 14.34.

If you have any questions in this regard, please contact me.

MJC:nah
Enclosures

cc: Maryanne Hruby
Executive Director
Legislative Commission to Review
Adminsitrative Rules

Duane Harves
Chief Administrative Law Judge
Office of Administrative Hearings

ULE REVIEW CHECKLIST

File No. 1394
DATE RECEIVED 8/31/87
REVIEW DATE 9/9/87
DUE DATE 9/14/87

APPROVED 9-9-87 mjc
DISAPPROVED
WITHDRAWN

Docket No. 05.0009.0112
ADOPTED W/O HEARING X
EMERGENCY RULE

REVISOR APPROVED
REVISOR DISAPPROVED
FIELD W/SEC.STATE
RETURNED TO AGENCY

✓ Rule as adopted (4 copies)
✓ Notice to Solicit Outside Information/Opinion
May 27, 1985 Date published in State Register
none Comments
~~Petition for Adoption of a Rule~~
~~Board's Authorizing Resolution~~
Proposed rule
Revisor's Certificate
✓ Notice of Intent to Adopt Rule
46.01 & 45.023 Statutory Authority
yes Small Business Statement
no Expenditure of public money statement
yes Signature
✓ Statement of Need and Reasonableness
yes Small Business Statement
no Fees - § 16A.128
✓ Affidavit of Mailing Notice of Intent to Adopt Rule
9/2/86 Date (30)/25 days before adoption
✓ Publication in State Register
withdrawn → ~~7/28/86~~ 9/8/86 Date (30)/25 days before adoption
~~Resolution Adopting~~
✓ Findings of Fact, Conclusions & Order Adopting
8/3/87 Date
Written requests, submissions or comments
✓ Declaration of attorney
Greg Huwe Name of SAAG representing agency
✓ ~~Notice of Submission to Attorney General~~ Certificate
✓ ~~Affidavit of Mailing Notice to Attorney General~~ order For Noting Intent to Adopt Rules w/o public hearing

Department of Commerce

Adopted Permanent Rules Relating to Financial Institution Audit Control Policies

Rules as Adopted

2675.2600 INTERNAL AUDIT CONTROL POLICY.

The board of directors of a bank, trust company, or savings bank shall establish a written internal audit control system. Documentation of internal audit procedures performed and the reports shall be maintained by the bank for inspection by the supervisory examiners and by the external auditors. The scope of coverage and effectiveness of the internal audit control system shall be reviewed for adequacy and approved by the board annually. The board shall consider inclusion of recommendations made by supervisory examiners and external auditors in the internal audit control system.

2675.2610 ANNUAL AUDIT REPORT.

Subpart 1. **Contents.** The annual audit report made under the direction of the board of directors pursuant to Minnesota Statutes, section 48.10, must include as a minimum:

A. a review of the adequacy of the internal control system and a test check to determine that control procedures are being followed;

B. a review ~~of board~~ to determine that policies ~~for development and a test check to determine that policies~~ are in place, are adequate, and are being ~~followed~~ implemented;

C. confirmation of assets through a sample positive or negative verification and inspection of assets held at the bank;

D. confirmation of deposits through a sample positive or negative verification;

E. a review of all fixed assets, other real estate, and equity accounts since the last audit and recordation of board approval of transactions involving these accounts;

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F. a review of income, expense, and related accrual accounts since the last audit;

G. a review of all general ledger accounts to determine their balanced condition, prompt reconciliation and appropriateness of reconciling items, and account makeup;

H. a review of delinquent loans and collection action taking place;

I. a review of the allowance for loan loss account;

J. a review of charge off loans, including loan files and notes;

K. a test check of loan files for documentation and approvals required by loan policy;

L. review of the electronic data processing systems and procedures if applicable;

M. review of significant activity in employee and officer accounts (depository and loan) for propriety and compliance with bank policies and regulations; and

N. review of off-balance sheet items including letters of credit.

Subp. 2. **Quarterly progress report.** The board shall include in its meeting agenda, at least quarterly, a review of the progress on the completion of the annual audit report by the individual directing the internal audit.

Subp. 3. **Preparation.** A written report of the annual audit must be prepared and must include the scope of audit including the size of the samplings taken. The report must summarize the findings and make recommendations for improving conditions, where appropriate.

Subp. 4. **Transmittal.** The written report shall be transmitted to the board of directors within 30 days of completion of the annual audit.

Subp. 5. **Board response.** The board shall prepare a written response on the findings and recommendations contained in the report and submit the response, the report, and its findings and recommendations to the Department of Commerce, Division of Financial Examinations, within 60 days of receipt of

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the audit report.

The board response shall be filed with the annual audit report as part of the bank's permanent records.

2675.2620 QUALIFICATIONS OF EXAMINING AUTHORITY.

Subpart 1. **Board to specify examining authority.** The board shall have the discretion to determine the method of examination used to meet the requirements of this part provided the examination is accomplished through one of the methods in subparts 2 to 5.

Subp. 2. **Examining committee.** If the requirements of this part are to be accomplished in whole or in part by an examining committee appointed by the board, the annual audit must be completed by qualified directors or their appointees who are in fact reasonably independent. A director or appointee serving as a member of the examining committee will not be considered independent if:

A. the person is closely related to active officers or employees of the bank;

B. the person has outstanding loans with the bank subject to criticism by state or federal supervisory agencies; or

C. the person has other unusual relationships or affiliations with the bank that raise the question of independence.

Subp. 3. **Internal auditor.** If the requirements of this part are to be accomplished in whole or in part by an internal auditor, the examination must be completed by a qualified internal auditor who is in fact reasonably independent. An internal auditor will not be considered independent if:

A. the person is employed or accountable to anyone other than the board of directors, and salary and annual bonus are not set by the board;

B. the person's duties within the bank are not confined entirely to bank auditing;

C. the person has any proprietary interest in any

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partnership, firm, or corporation which controls the bank, directly or indirectly;

D. the person has outstanding loans subject to criticism by state or federal supervisory agencies;

E. the person is a member of the immediate family of an officer, director, attorney, or employee for the bank; or

F. the person has other unusual relationships or affiliations with the bank that raise the question of independence.

In banks of less than $40,000,000 in total assets as of the immediately preceding calendar year end, where duties of the internal auditor cannot be confined entirely to bank auditing, the internal auditor will be considered reasonably independent only if someone else audits the areas for which the internal auditor has operational responsibilities. The board is responsible for determining that this degree of internal audit dependence is maintained.

Subp. 4. **Certified public accountants or licensed public accountants.** If the requirements of this part are to be accomplished in whole or in part by a certified public accountant or licensed public accountant, the audit must be completed by a qualified certified public accountant or a qualified licensed public accountant who is in fact independent. A certified public accountant or licensed public accountant will not be considered independent if:

A. The certified public accountant, licensed public accountant, or any member of a firm performing the audit is connected with the bank as an officer, director, attorney, or employee or is a member of the immediate family of an officer, director, bank attorney, or employee.

B. He or she is the beneficial owner, directly or indirectly, of any of the shares of stock of the bank.

C. He or she has any proprietary interest in any partnership, firm, or corporation which controls the banks, directly or indirectly.

D. The bank under examination has outstanding loans

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to the certified public accountant, licensed public accountant, partners, principals of the firm, or employees of such a firm who are directly involved in the examination, unless the loans are adequately disclosed in the audit report to the board of directors of the bank. Adequate disclosure includes the name of the borrower, the amount of the loan, the security pledged, and the appraisal or market value of the security at the time of the engagement.

E. He or she makes entries or postings on the books of account or performs any other operating functions for the bank, except functions for which prior approval was requested and obtained in writing from the commissioner of commerce.

F. He or she has other unusual relationships or affiliations with the bank that raise the question of independence.

In circumstances where directors, appointees, or the internal auditor are considered not independent or qualified to perform the annual audit, the board should engage a certified public accountant or licensed public accountant.

Subp. 5. **Board of directors.** If the requirements of this part are to be accomplished by the board of directors as provided in Minnesota Statutes, section 48.10, the board must number at least five and include at a minimum one outside director.

Subp. 6. **Audit by outside parties.** At least one ~~**examination**~~ annual audit every four years must be completed by outside parties as set forth in subpart ~~3~~ 4.

APPROVED BY THE REVISOR OF STATUTES OFFICE BY:

STATE OF MINNESOTA
DEPARTMENT OF STATE
FILED

SEP 1 4 1987

Joan Anderson Growe
Secretary of State

1:40 PM

APPROVED AS TO FORM AND LEGALITY

September 9 1987

HUBERT H. HUMPHREY, III
ATTORNEY GENERAL

BY M J Carsely
SPECIAL ASSISTANT ATTORNEY GENERAL

STATE OF MINNESOTA
DEPARTMENT OF COMMERCE
DIVISION OF FINANCIAL EXAMINATIONS

Notice of Intent to Solicit Outside Opinion Concerning Amendments to Rules Governing the Operation of Commerical Banks Annual Audit and Report

Notice is hereby given that the Minnesota Department of Commerce is soliciting information and opinions from sources outside the agency and is preparing to promulgate new rules relating to commercial banks to establish directors audit scope and reporting pursuant to Minn. Stat. § 48.10.

The Department of Commerce requests information and comments concerning the subject matter of these rules. Interested or affected persons or groups may submit statements of information or comments orally or in writing. Written statements should be addressed to:

David A. Shern, Deputy Commissioner
Division of Financial Examinations
500 Metro Square Building
Seventh and Robert Streets
St. Paul, Minnesota 55101
(612) 296-2135

All statements of information and comment shall be accepted until June 30, 1985. Any written material received by the Department of Commerce shall become part of the record in the event that the rules are promulgated.

Michael A. Hatch
Commissioner of Commerce

Department of Commerce

Proposed Permanent Rules Relating to Financial Institution Audit Control Policies

Rules as Proposed (all new material)

2675.2600 INTERNAL AUDIT CONTROL POLICY.

The board of directors of a bank, trust company, or savings bank shall establish a written internal audit control system. The individual directing the internal audit control system shall submit to the board of directors each quarter a report detailing the areas audited, results obtained, and the degree of compliance with established policies and internal controls. Documentation of audit procedures performed and the reports shall be maintained by the bank for inspection by the supervisory examiners and by the external auditors. The scope of coverage and effectiveness of the internal audit control system shall be reviewed for adequacy and approved by the board annually. The board shall consider inclusion of recommendations made by supervisory examiners and external auditors in the internal audit control system.

2675.2610 ANNUAL AUDIT REPORT.

Subpart 1. **Contents.** The annual audit report made under the direction of the board of directors pursuant to Minnesota Statutes, section 48.10, must include as a minimum:

A. a review of the adequacy of the internal control system and a test check to determine that control procedures are being followed;

B. a review of board policies for development and a test check to determine that policies are being followed;

C. confirmation of assets through a sample positive or negative verification and inspection of assets held at the bank;

D. confirmation of deposits through a sample positive or negative verification;

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E. a review of all fixed assets, other real estate, and equity accounts since the last audit and recordation of board approval of transactions involving these accounts;

F. a review of income, expense, and related accrual accounts since the last audit;

G. a review of all general ledger accounts to determine their balanced condition, prompt reconciliation and appropriateness of reconciling items, and account makeup;

H. a review of delinquent loans and collection action taking place;

I. a review of the allowance for loan loss account;

J. a review of charge off loans, including loan files and notes;

K. a test check of loan files for documentation and approvals required by loan policy;

L. review of the electronic data processing systems and procedures if applicable;

M. review of significant activity in employee and officer accounts for propriety and compliance with bank policies and regulations; and

N. review of off-balance sheet items including letters of credit.

Subp. 2. **Preparation.** A written report of the annual audit must be prepared and must include the scope of audit including the size of the samplings taken. The report must summarize the findings and make recommendations for improving conditions, where appropriate.

Subp. 3. **Transmittal.** The written report shall be transmitted to the board of directors within 30 days of completion of the audit.

Subp. 4. **Board response.** The board shall prepare a written response on the findings and recommendations contained in the report and submit the response, the report, and its findings and recommendations to the Department of Commerce, Division of Financial Examinations, within 60 days of receipt of the audit report.

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The board response shall be filed with the audit report as part of the bank's permanent records.

2675.2620 QUALIFICATIONS OF EXAMINING AUTHORITY.

Subpart 1. **Examining committee.** If the requirements of this part are to be accomplished in whole or in part by an examining committee appointed by the board, the audit must be completed by qualified directors or their appointees who are in fact reasonably independent. A director or appointee serving as a member of the examining committee will not be considered independent if:

A. the person is closely related to active officers or employees of the bank;

B. the person has outstanding loans with the bank subject to criticism by state or federal supervisory agencies; or

C. the person has other unusual relationships or affiliations with the bank that question independence.

Subp. 2. **Internal auditor.** If the requirements of this part are to be accomplished in whole or in part by an internal auditor, the examination must be completed by a qualified internal auditor who is in fact reasonably independent. An internal auditor will not be considered independent if:

A. the person is employed or accountable to anyone other than the board of directors, and salary and annual bonus are not set by the board;

B. duties within the bank are not confined entirely to bank auditing;

C. the person has any proprietary interest in any partnership, firm, or corporation which controls the bank, directly or indirectly;

D. the person has outstanding loans subject to criticism by state or federal supervisory agencies;

E. the person is a member of the immediate family of an officer, director, attorney, or employee for the bank; or

F. the person has other unusual relationships or

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affiliations with the bank that question independence.

In banks of less than $25,000,000 in total assets, where duties of the internal auditor cannot be confined entirely to bank auditing, the internal auditor will be considered reasonably independent only if someone else audits the areas for which the internal auditor has operational responsibilities. The board is responsible for determining that this degree of internal audit dependence is maintained.

Subp. 3. **Certified public accountants or licensed public accountants.** If the requirements of this part are to be accomplished in whole or in part by a certified public accountant or licensed public accountant, the audit must be completed by a qualified certified public accountant or a qualified licensed public accountant who is in fact independent. A certified public accountant or licensed public accountant will not be considered independent if:

A. The certified public accountant, licensed public accountant, or any member of a firm performing the audit is connected with the bank as an officer, director, attorney, or employee or is a member of the immediate family of an officer, director, bank attorney, or employee.

B. Is the beneficial owner, directly or indirectly, of any of the shares of stock of the bank.

C. Has any proprietary interest in any partnership, firm, or corporation which controls the banks, directly or indirectly.

D. The bank under examination has outstanding loans to the certified public accountant, licensed public accountant, partners, principals of the firm, or employees of such a firm who are directly involved in the examination, unless the loans are adequately disclosed in the audit report to the board of directors of the bank. Adequate disclosure includes the name of the borrower, the amount of the loan, the security pledged, and the appraisal or market value of the security at the time of the engagement.

E. Makes entries or postings on the books of account

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OFFICE

or performs any other operating functions for the bank, except functions for which prior approval was requested and obtained in writing from the commissioner of commerce.

F. Has other unusual relationships or affiliations with the bank that question independence.

In circumstances where directors, appointees, or the internal auditor are considered not independent or qualified to perform the annual audit, the board should engage a certified public accountant or licensed public accountant.

Subp. 4. **Board of directors.** If the requirements of this part are to be accomplished by the board of directors as provided in Minnesota Statutes, section 48.10, the board must number at least five and include at a minimum one outside director.

Subp. 5. **Audit by outside parties.** At least one examination every four years must be completed by outside parties as set forth in subpart 3.

2675.2630 PERSONAL FINANCIAL STATEMENT.

A stockholder who owns or controls 25 percent or more of bank stock, or 25 percent or more stock in a holding company that owns controlling interest of the bank, and who also serves as an active officer or director of the bank or bank holding company, must annually complete a personal financial statement. This statement must consist of a listing of assets and liabilities and be dated no more than one year before the annual audit. The statement must be submitted to the commissioner of commerce along with the audit report as prescribed in part 2675.2610, subpart 4.

APPROVED IN THE
REVISOR OF STATUTES
OFFICE BY:

Office of the Revisor of Statutes

Administrative Rules

TITLE: Proposed Permanent Rules Relating to Financial Institution Audit Control Policies

AGENCY: Department of Commerce

MINNESOTA RULES: Chapter 2675

The attached rules are approved for publication in the State Register

Paul M. Marinac
Assistant Deputy Revisor

State of Minnesota
Department of Commerce

In the Matter of the Proposed Adoption of Rules Relating to Financial Institution Audit Control Policies

Notice of Intent to Adopt Rules Without a Public Hearing

Notice is hereby given that the Department of Commerce proposes to adopt the above-entitled rules without a public hearing. The Commissioner of Commerce has determined that the proposed adoption of these rules will be noncontroversila in nature and has elected to follow the procedures set forth in Minnesota Statutes, Section 14.21.

Persons interested in these rules shall have 30 days to submit comments in support of or in opposition to the rules. Each comment should identify the portion of the proposed rule addressed, the reason for the comment, and any change proposed. The proposed rules may be modified if the modifications are supported by the data and views submitted to the Department and does not result in a substantial change.

No public hearing will be held unless twenty-five (25) or more persons make a written request for a hearing within the 30 day comment period. In the event a public hearing is required, the agency will proceed according to the provisions of Minnesota Statutes, Section 14.14, subd. 1.

Persons who wish to submit comments or a written request for a public hearing should submit them to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Building, St. Paul, MN 55101 telephone (612) 296-5689. Any person requesting a public hearing should state her or his name and address and is encouraged to identify the portion of the proposed rule addressed, the reason for the request and any change proposed and send this information to the above address.

Authority for the adoption of these rules is contained in Minnesota Statutes, Sections 45.023 and 46.01.
Additionally a Statement of Need and Reasonableness of each provision and identifying the data and information relied upon to support the proposed rules has been prepared and is available upon request.

Pursuant to Minnesota Statutes Section 14.115, subdivision 2, the impact on small business has been considered in the promulgation of the rules. Anyone wishing to present evidence or argument as to the rules' effect on small business may do so. The Department's position regarding the impact of the rules on small business is set forth in the Statement of Need and Reasonableness.

Upon adoption of the final rules without a public hearing the proposed rules, this Notice, the Statement of Need and Reasonableness, all written comments received, and the final Rules as Adopted will be delivered to the Attorney General for review as to form and legality,

including the issue of substantial change. Persons who wish to be advised of the submission of this material to the Attorney General, or who wish to receive a copy of the final rules as proposed for adoption, should submit a written statement of such request to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Building, St. Paul, MN 55101.

A copy of the proposed rules is attached to this Notice. Copies of this Notice and proposed rules are available and may be obtained by contacting Richard G. Gomsrud at the above address.

MICHAEL A. HATCH
Commissioner of Commerce

STATE OF MINNESOTA
DEPARTMENT OF COMMERCE
DIVISION OF FINANCIAL EXAMINATIONS

In the Matter of the Proposed Rules Relating to Financial Institutions Audit Control Policies

STATEMENT OF NEED AND REASONABLENESS OF PROPOSED AMENDMENTS

STATEMENT OF AUTHORITY

Minn. Stat. § 46.01, subd. 2 (1984) as amended, provides that the Commissioner of Commerce (hereinafter "Commissioner") has the power to promulgate rules as necessary to administer or execute the laws relating to financial institutions subject to the Commissioner's supervision and examination. Commercial banks and savings banks are organized pursuant to Minn. Stat. Chs. 45, 47, 48, 50 and 300 and are subject to the constant supervision and examination by the Commissioner as directed in Minn. Stat. § 46.04. These rules are proposed by the Commissioner pursuant to this authority.

On May 27, 1985, the Commissioner published Notice of Intent to Solicit Outside Opinion regarding the proposed amendment.

FACTS ESTABLISHING NEED AND REASONABLENESS

Minnesota Statute § 48.10, anticipates the need for the board to be fully informed on the bank's activities by requiring that they conduct or have conducted an annual examination of the bank's books. However, the statute lacks definition to insure a meaningful examination. These proposed rules amend the guidelines for carrying out the intent of the statute. The need for these rules focuses on and is

directly responsive to two major concerns of the Commissioner in fulfilling the responsibility in Minnesota Statutes, Section 46.04, to maintain the constant supervision over Minnesota state chartered banks. The primary supervisory role of the Department is accomplished through on-site examinations which are conducted at least every 18 months. This on-site examination is supplemented by quarterly reports from the bank which are made in March, June, September, and December. These examinations and quarterly reports are structured to address current conditions, operations and potential areas of chief concern as primary regulator.

A secondary mechanism to monitor banks is through the requirement that the bank conduct an annual audit and report under Minn. Stat. § 48.10. This requirement was designed to be useful to the board in its duty to oversee the bank's operation. In addition, a copy of the report, together with the board's response to the report, is submitted to the Commissioner, who uses the report as a means of off-site inspection.

The amendments will hopefully promulgate a more uniform annual audit and report. Under current rules the bank board may perform its own audit. In such a case, a two sided report is commonly used and submitted, but in many cases the report is incomplete and outdated for current bank purposes. In addition, many banks create different audit formats, which do not fulfill any meaningful purpose under the statute.

The bank board may also use public accountants and certified public accountants to complete the annual audit

and report. These reports, however, are also inconsistent and vary considerably in terms of meaningful comment for either the bank board or the department. Some of the reports serve little useful purpose in large part without rules setting forth minimum standards.

In addition to uniformity, the second purpose of the amendmends is the increased concern of the Commissioner and bank boards as to the frequency of losses to banks through employee and official misconduct, errors, and lack of systematic oversight. The solvency of many banks has been threatened in part due to the ineffectiveness of the audit system. As has been seen over the last year in the media, at least a half dozen banks have discovered defalcation and embezzlement of funds by company officers. In some cases the discovery was accomplished through the annual audit, and the matter was resolved without effecting the bank's condition. In other cases the discovery was not made until the on-site examination, and in at least one case the discovery was too late to save the bank. Accordingly, the amendments do set minimum standards concerning the audit, with the intent being that the audit focus in some part on the conduct of bank employees and officials.

The need for these rules is not only demonstrated through the recent proliferation of embezzlement charges against bank employees, but also through the difficulty banks currently have in obtaining bond coverage from insurance companies. In 1984 over 59 state banks received bond cancellation notices, and through the first months of 1986, 16

banks received such cancellation notices. The use of internal audit controls and procedures, together with the external audits promulgated under the rules, would contribute toward minimizing risks to banks and their insureds, and hopefully would reduce the cost of bond coverage as well as increase the availability of such coverage. Discussions with insurance companies indicate that one of their concerns in underwriting such risks deals with the lack of uniformity in internal bank audits.

Bank closings in the United States have escalated to unprecedented numbers. In the aftermath of a bank failure, the bank's board of directors are often named as defendants in a lawsuit by the Federal Deposit Insurance Corporation. The charges in the lawsuit generally state that the bank board was not aware of improprieties which, through the use of reasonable audit controls, they should have discovered. As a result of these lawsuits and the increased responsibility associated with being a director, it is becoming increasingly difficult to find qualified directors willing to serve in this position of community interest. Thus, with a more standard uniformity in the audit structure, it is hoped that the chances of such litigation will be reduced.

To take responsible action under specific rule making authority is incumbent upon the Commissioner as follows:

MINNESOTA RULE 2675.2600 requires each bank to develop its own internal audit control policy and establishes a mechanism for reporting to keep the board informed on the degree of compliance with established policies and controls.

Additionally, it provides for review and update of the system on an ongoing basis. This is an expected and prudent banking practice which is now being included in rule form.

MINNESOTA RULE 2675.2610 establishes minimum guidelines and minimum requirements for the completion of an annual directors' examination as required by Minnesota Statutes, Section 48.10. In addition, the rule provides a mechanism to insure that the board is informed of the examination findings and that it properly addresses disclosed deficiencies and so informs the Commissioner.

MINNESOTA RULE 2675.2620 establishes who may perform the annual examination as well as conditions which may preclude certain individuals from qualifying to conduct the examination. This rule provides that the examination may be done by an examining committee appointed by the board, an internal auditor, a certified public accountant or qualified licensed public accountant or the board of directors, provided these bodies conform to conditions established by the rule. Additionally, this rule provides that every fourth year the examination must be performed by outside auditors who are certified public accountants or qualified licensed public accountants.

MINNESOTA RULE 2675.2630 requires financial statements from persons controlling more than 25% interest in the bank and who are directors or active officers of the bank or its holding company. Highly leveraged bank owners are often unable to correct deficiencies requiring the addition of capital. Additionally, these individuals sometimes have a difficult time servicing debt secured by equity interest

in the bank. In such situations, it may be advisable for regulatory authorities to investigate the advisability of the individual serving in the capacity of active officer or director of the bank.

CONCLUSION

For the reasons stated above, it is in the public interest to adopt these rules. These rules are deemed noncontroversial and offer positive impact on small business constituting banks under our supervision and control. These rules and their enforcement will not require additional expenditures by this supervisory agency and any additional costs to the supervised banks will be offset by contemplated savings in bond costs, Federal Deposit Insurance Corporation insurance premiums, examination fees, audit fees and overall efficiency. It is believed to be clear that the proposed rules reasonably effectuate the above stated need.

MICHAEL A. HATCH
Commissioner of Commerce

In the Matter of the Proposed Rules
Relating to Financial Institution Audit
Control Policies

STATE OF MINNESOTA)
) ss
COUNTY OF RAMSEY)

AFFIDAVIT OF MAILING

Richard G. Gomsrud, being first duly sworn, deposes and says:

That on the 2nd day of September, 1986, at the City of St. Paul, County of Ramsey, State of Minnesota, the attached Notice of Intent to Adopt Rules Without Hearing was served by depositing in the State of Minnesota Central Mail System for United States mailing at said City of St. Paul, a copy properly prepared with first-class postage prepaid, on all persons and associations who have requested that their names be placed on file with the Minnesota Department of Commerce for thepurpose of receiving notice of the proposed adoption of rules by the department

Richard G. Gomsrud

Subscribed and sworn to
before me this 3rd day of September, 1986

Nancy I. Link

NANCY I. LINK
NOTARY PUBLIC-MINNESOTA
HENNEPIN COUNTY
MY COMMISSION EXPIRES DECEMBER 3, 1990

STATE OF MINNESOTA

DEPARTMENT OF COMMERCE
500 METRO SQUARE BUILDING
ST. PAUL, MN 55101

ATTENTION:
RULE RELATED MATERIAL

FIRST CLASS MAIL

State of Minnesota
Department of Commerce

In the Matter of the Proposed Adoption of Rules Relating to Financial Institution Audit Control Policies

Notice of Intent to Adopt Rules Without a Public Hearing

Notice is hereby given that the Department of Commerce proposes to adopt the above-entitled rules without a public hearing. The Commissioner of Commerce has determined that the proposed adoption of these rules will be noncontroversial in nature and has elected to follow the procedures set forth in Minnesota Statutes, Section 14.21.

Persons interested in these rules shall have 30 days to submit comments in support of or in opposition to the rules. Each comment should identify the portion of the proposed rule addressed, the reason for the comment, and any change proposed. The proposed rules may be modified if the modifications are supported by the data and views submitted to the Department and does not result in a substantial change.

No public hearing will be held unless twenty-five (25) or more persons make a written request for a hearing within the 30 day comment period. In the event a public hearing is required, the agency will proceed according to the provisions of Minnesota Statutes, Section 14.14, subd. 1.

Persons who wish to submit comments or a written request for a public hearing should submit them to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Building, St. Paul, MN 55101 telephone (612) 296-5689. Any person requesting a public hearing should state her or his name and address and is encouraged to identify the portion of the proposed rule addressed, the reason for the request and any change proposed and send this information to the above address.

Authority for the adoption of these rules is contained in Minnesota Statutes, Sections 45.023 and 46.01. Additionally a Statement of Need and Reasonableness of each provision and identifying the data and information relied upon to support the proposed rules has been prepared and is available upon request.

Pursuant to Minnesota Statutes Section 14.115, subdivision 2, the impact on small business has been considered in the promulgation of the rules. Anyone wishing to present evidence or argument as to the rules' effect on small business may do so. The Department's position regarding the impact of the rules on small business is set forth in the Statement of Need and Reasonableness.

Upon adoption of the final rules without a public hearing, the proposed rules, this Notice, the Statement of Need and Reasonablenss, all written comments received, and the final Rules as Adopted will be delivered to the Attorney General for review as to form and legality, including the issue of substantial change. Persons who wish to be advised of the submission of this material to the Attorney General, or who wish to receive a copy of the final rules as proposed for adoption, should submit a written statement of such request to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Bldg., St. Paul, MN 55101.

A copy of the proposed rules is attached to this Notice. Copies of this Notice and proposed rules are available and may be obtained by contacting Richard G. Gomsrud at the above address.

Michael A. Hatch
Commissioner of Commerce

Department of Commerce

Proposed Permanent Rules Relating to Financial Institution Audit Control Policies

Rules as Proposed (all new material)

2675.2600 INTERNAL AUDIT CONTROL POLICY.

The board of directors of a bank, trust company, or savings bank shall establish a written internal audit control system. The individual directing the internal audit control system shall submit to the board of directors each quarter a report detailing the areas audited, results obtained, and the degree of compliance with established policies and internal controls. Documentation of audit procedures performed and the reports shall be maintained by the bank for inspection by the supervisory examiners and by the external auditors. The scope of coverage and effectiveness of the internal audit control system shall be reviewed for adequacy and approved by the board annually. The board shall consider inclusion of recommendations made by supervisory examiners and external auditors in the internal audit control system.

2675.2610 ANNUAL AUDIT REPORT.

Subpart 1. **Contents.** The annual audit report made under the direction of the board of directors pursuant to Minnesota Statutes, section 48.10, must include as a minimum:

A. a review of the adequacy of the internal control system and a test check to determine that control procedures are being followed;

B. a review of board policies for development and a test check to determine that policies are being followed;

C. confirmation of assets through a sample positive or negative verification and inspection of assets held at the bank;

D. confirmation of deposits through a sample positive or negative verification;

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E. a review of all fixed assets, other real estate, and equity accounts since the last audit and recordation of board approval of transactions involving these accounts;

F. a review of income, expense, and related accrual accounts since the last audit;

G. a review of all general ledger accounts to determine their balanced condition, prompt reconciliation and appropriateness of reconciling items, and account makeup;

H. a review of delinquent loans and collection action taking place;

I. a review of the allowance for loan loss account;

J. a review of charge off loans, including loan files and notes;

K. a test check of loan files for documentation and approvals required by loan policy;

L. review of the electronic data processing systems and procedures if applicable;

M. review of significant activity in employee and officer accounts for propriety and compliance with bank policies and regulations; and

N. review of off-balance sheet items including letters of credit.

Subp. 2. **Preparation.** A written report of the annual audit must be prepared and must include the scope of audit including the size of the samplings taken. The report must summarize the findings and make recommendations for improving conditions, where appropriate.

Subp. 3. **Transmittal.** The written report shall be transmitted to the board of directors within 30 days of completion of the audit.

Subp. 4. **Board response.** The board shall prepare a written response on the findings and recommendations contained in the report and submit the response, the report, and its findings and recommendations to the Department of Commerce, Division of Financial Examinations, within 60 days of receipt of the audit report.

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The board response shall be filed with the audit report as part of the bank's permanent records.

2675.2620 QUALIFICATIONS OF EXAMINING AUTHORITY.

Subpart 1. **Examining committee.** If the requirements of this part are to be accomplished in whole or in part by an examining committee appointed by the board, the audit must be completed by qualified directors or their appointees who are in fact reasonably independent. A director or appointee serving as a member of the examining committee will not be considered independent if:

A. the person is closely related to active officers or employees of the bank;

B. the person has outstanding loans with the bank subject to criticism by state or federal supervisory agencies; or

C. the person has other unusual relationships or affiliations with the bank that question independence.

Subp. 2. **Internal auditor.** If the requirements of this part are to be accomplished in whole or in part by an internal auditor, the examination must be completed by a qualified internal auditor who is in fact reasonably independent. An internal auditor will not be considered independent if:

A. the person is employed or accountable to anyone other than the board of directors, and salary and annual bonus are not set by the board;

B. duties within the bank are not confined entirely to bank auditing;

C. the person has any proprietary interest in any partnership, firm, or corporation which controls the bank, directly or indirectly;

D. the person has outstanding loans subject to criticism by state or federal supervisory agencies;

E. the person is a member of the immediate family of an officer, director, attorney, or employee for the bank; or

F. the person has other unusual relationships or

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affiliations with the bank that question independence.

In banks of less than $25,000,000 in total assets, where duties of the internal auditor cannot be confined entirely to bank auditing, the internal auditor will be considered reasonably independent only if someone else audits the areas for which the internal auditor has operational responsibilities. The board is responsible for determining that this degree of internal audit dependence is maintained.

Subp. 3. **Certified public accountants or licensed public accountants.** If the requirements of this part are to be accomplished in whole or in part by a certified public accountant or licensed public accountant, the audit must be completed by a qualified certified public accountant or a qualified licensed public accountant who is in fact independent. A certified public accountant or licensed public accountant will not be considered independent if:

A. The certified public accountant, licensed public accountant, or any member of a firm performing the audit is connected with the bank as an officer, director, attorney, or employee or is a member of the immediate family of an officer, director, bank attorney, or employee.

B. Is the beneficial owner, directly or indirectly, of any of the shares of stock of the bank.

C. Has any proprietary interest in any partnership, firm, or corporation which controls the banks, directly or indirectly.

D. The bank under examination has outstanding loans to the certified public accountant, licensed public accountant, partners, principals of the firm, or employees of such a firm who are directly involved in the examination, unless the loans are adequately disclosed in the audit report to the board of directors of the bank. Adequate disclosure includes the name of the borrower, the amount of the loan, the security pledged, and the appraisal or market value of the security at the time of the engagement.

E. Makes entries or postings on the books of account

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or performs any other operating functions for the bank, except functions for which prior approval was requested and obtained in writing from the commissioner of commerce.

F. Has other unusual relationships or affiliations with the bank that question independence.

In circumstances where directors, appointees, or the internal auditor are considered not independent or qualified to perform the annual audit, the board should engage a certified public accountant or licensed public accountant.

Subp. 4. **Board of directors.** If the requirements of this part are to be accomplished by the board of directors as provided in Minnesota Statutes, section 48.10, the board must number at least five and include at a minimum one outside director.

Subp. 5. **Audit by outside parties.** At least one examination every four years must be completed by outside parties as set forth in subpart 3.

2675.2630 PERSONAL FINANCIAL STATEMENT.

A stockholder who owns or controls 25 percent or more of bank stock, or 25 percent or more stock in a holding company that owns controlling interest of the bank, and who also serves as an active officer or director of the bank or bank holding company, must annually complete a personal financial statement. This statement must consist of a listing of assets and liabilities and be dated no more than one year before the annual audit. The statement must be submitted to the commissioner of commerce along with the audit report as prescribed in part 2675.2610, subpart 4.

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OFFICE BY:

STATE OF MINNESOTA

STATE REGISTER

DEPARTMENT OF ADMINISTRATION—DOCUMENTS DIVISION



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PROPOSED RULES

Pursuant to Minn. Stat. of 1982, §§ 14.22, an agency may propose to adopt, amend, suspend or repeal rules without first holding a public hearing, as long as the agency determines that the rules will be noncontroversial in nature. The agency must first publish a notice of intent to adopt rules without a public hearing, together with the proposed rules, in the *State Register*. The notice must advise the public:

1. **that they have 30 days in which to submit comment on the proposed rules;**
2. **that no public hearing will be held unless 25 or more persons make a written request for a hearing within the 30-day comment period;**
3. **of the manner in which persons shall request a hearing on the proposed rules; and**
4. **that the rule may be modified if the modifications are supported by the data and views submitted.**

If, during the 30-day comment period, 25 or more persons submit to the agency a written request for a hearing of the proposed rules, the agency must proceed under the provisions of §§ 14.14-14.20, which state that if an agency decides to hold a public hearing, it must publish a notice of intent in the *State Register*.

Pursuant to Minn. Stat. §§ 14.29 and 14.30, agencies may propose emergency rules under certain circumstances. Proposed emergency rules are published in the *State Register* and, for at least 25 days thereafter, interested persons may submit data and views in writing to the proposing agency.

Department of Commerce

Proposed Permanent Rules Relating to Financial Institution Audit Control Policies

Notice of Withdrawal of Rules

On Monday July 28, 1986, at 11. SR. 101 The Commissioner of Commerce published his Notice of Intent to Adopt Rules without a Public Hearing in the above-captioned matter along with a copy of the proposed rules. Based upon those comments the Commissioner determined that certain changes should be made in the rules. As these changes appeared to be substantial in nature, the Commissioner has ordered that the rules published at 11 S.R. 101 be withdrawn and that notice be published accordingly. The Commissioner furthered ordered that a new Notice of Intent to Adopt Rules without a Public Hearing be published incorporating the changes. That Notice and rules appear elsewhere in this *State Register*.

Michael A. Hatch
Commissioner of Commerce

Notice of Intent to Adopt Rules without a Public Hearing

Notice is hereby given that the Department of Commerce proposes to adopt the above-entitled rules without a public hearing. The Commissioner of Commerce has determined that the proposed adoption of these rules will be noncontroversial in nature and has elected to follow the procedures set forth in Minnesota Statutes, Section 14.21.

Persons interested in these rules shall have 30 days to submit comments in support of or in opposition to the rules. Each comment should identify the portion of the proposed rule addressed, the reason for the comment, and any change proposed. The proposed rules may be modified if the modifications are supported by the data and views submitted to the Department and does not result in a substantial change.

No public hearing will be held unless twenty-five (25) or more persons make a written request for a hearing within the 30 day comment period. In the event a public hearing is required, the agency will proceed according to the provisions of Minnesota Statutes, Section 14.14, subd. 1.

Persons who wish to submit comments or a written request for a public hearing should submit them to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Building, St. Paul, MN 55101 telephone (612) 296-5689. Any person requesting a public hearing should state her or his name and address and is encouraged to identify the portion of the proposed rule addressed, the reason for the request and any change proposed and send this information to the above address.

Authority for the adoption of these rules is contained in Minnesota Statutes, Sections 45.023 and 46.01. Additionally a Statement of Need and Reasonableness of each provision and identifying the data and information relied upon to support the proposed rules has been prepared and is available upon request.

KEY: PROPOSED RULES SECTION — Underlining indicates additions to existing rule language. ~~Strike outs~~ indicate deletions from existing rule language. If a proposed rule is totally new, it is designated "all new material." **ADOPTED RULES SECTION** — Underlining indicates additions to proposed rule language. ~~Strike outs~~ indicate deletions from proposed rule language.

Pursuant to Minnesota Statutes Section 14.115, subdivision 2, the impact on small business has been considered in the promulgation of the rules. Anyone wishing to present evidence or argument as to the rules' effect on small business may do so. The Department's position regarding the impact of the rules on small business is set forth in the Statement of Need and Reasonableness.

Upon adoption of the final rules without a public hearing, the proposed rules, this Notice, the Statement of Need and Reasonableness, all written comments received, and the final Rules as Adopted will be delivered to the Attorney General for review as to form and legality, including the issue of substantial change. Persons who wish to be advised of the submission of this material to the Attorney General, or who wish to receive a copy of the final rules as proposed for adoption, should submit a written statement of such request to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Bldg., St. Paul, MN 55101.

A copy of the proposed rules is attached to this Notice. Copies of this Notice and proposed rules are available and may be obtained by contacting Richard G. Gomsrud at the above address.

Michael A. Hatch
Commissioner of Commerce

Rules as Proposed (all new material)

2675.2600 INTERNAL AUDIT CONTROL POLICY.

The board of directors of a bank, trust company, or savings bank shall establish a written internal audit control system. Documentation of audit procedures performed and the reports shall be maintained by the bank for inspection by the supervisory examiners and by the external auditors. The scope of coverage and effectiveness of the internal audit control system shall be reviewed for adequacy and approved by the board annually. The board shall consider inclusion of recommendations made by supervisory examiners and external auditors in the internal audit control system.

2675.2610 ANNUAL AUDIT REPORT.

Subpart 1. **Contents.** The annual audit report made under the direction of the board of directors pursuant to Minnesota Statutes, section 48.10, must include as a minimum:

A. a review of the adequacy of the internal control system and a test check to determine that control procedures are being followed;

B. a review of board policies for development and a test check to determine that policies are being followed;

C. confirmation of assets through a sample positive or negative verification and inspection of assets held at the bank;

D. confirmation of deposits through a sample positive or negative verification;

E. a review of all fixed assets, other real estate, and equity accounts since the last audit and recordation of board approval of transactions involving these accounts;

F. a review of income, expense, and related accrual accounts since the last audit;

G. a review of all general ledger accounts to determine their balanced condition, prompt reconciliation and appropriateness of reconciling items, and account makeup;

H. a review of delinquent loans and collection action taking place;

I. a review of the allowance for loan loss account;

J. a review of charge off loans, including loan files and notes;

K. a test check of loan files for documentation and approvals required by loan policy;

L. review of the electronic data processing systems and procedures if applicable;

M. review of significant activity in employee and officer accounts for propriety and compliance with bank policies and regulations; and

N. review of off-balance sheet items including letters of credit.

Subp. 2. **Quarterly progress report.** The board shall include in its meeting agenda, at least quarterly, a review of the progress on the completion of the annual audit report by the individual directing the internal audit.

Subp. 3. **Preparation.** A written report of the annual audit must be prepared and must include the scope of audit including the size of the samplings taken. The report must summarize the findings and make recommendations for improving conditions, where appropriate.

Subp. 4. **Transmittal.** The written report shall be transmitted to the board of directors within 30 days of completion of the audit.

Subp. 5. **Board response.** The board shall prepare a written response on the findings and recommendations contained in the report and submit the response, the report, and its findings and recommendations to the Department of Commerce, Division of Financial Examinations, within 60 days of receipt of the audit report.

The board response shall be filed with the audit report as part of the bank's permanent records.

2675.2620 QUALIFICATIONS OF EXAMINING AUTHORITY.

Subpart 1. **Board to specify examining authority.** The board shall have the discretion to determine the method of examination used to meet the requirements of this part provided the examination is accomplished through one of the methods in subparts 2 to 5.

Subp. 2. **Examining committee.** If the requirements of this part are to be accomplished in whole or in part by an examining committee appointed by the board, the audit must be completed by qualified directors or their appointees who are in fact reasonably independent. A director or appointee serving as a member of the examining committee will not be considered independent if:

A. the person is closely related to active officers or employees of the bank;

B. the person has outstanding loans with the bank subject to criticism by state or federal supervisory agencies; or

C. the person has other unusual relationships or affiliations with the bank that question independence.

Subp. 3. **Internal auditor.** If the requirements of this part are to be accomplished in whole or in part by an internal auditor, the examination must be completed by a qualified internal auditor who is in fact reasonably independent. An internal auditor will not be considered independent if:

A. the person is employed or accountable to anyone other than the board of directors, and salary and annual bonus are not set by the board;

B. duties within the bank are not confined entirely to bank auditing;

C. the person has any proprietary interest in any partnership, firm, or corporation which controls the bank, directly or indirectly;

D. the person has outstanding loans subject to criticism by state or federal supervisory agencies;

E. the person is a member of the immediate family of an officer, director, attorney, or employee for the bank; or

F. the person has other unusual relationships or affiliations with the bank that question independence.

In banks of less than $40,000,000 in total assets as of the immediately preceding calendar year end, where duties of the internal auditor cannot be confined entirely to bank auditing, the internal auditor will be considered reasonably independent only if someone else audits the areas for which the internal auditor has operational responsibilities. The board is responsible for determining that this degree of internal audit dependence is maintained.

Subp. 4. **Certified public accountants or licensed public accountants.** If the requirements of this part are to be accomplished in whole or in part by a certified public accountant or licensed public accountant, the audit must be completed by a qualified certified public accountant or a qualified licensed public accountant who is in fact independent. A certified public accountant or licensed public accountant will not be considered independent if:

A. The certified public accountant, licensed public accountant, or any member of a firm performing the audit is connected with the bank as an officer, director, attorney, or employee or is a member of the immediate family of an officer, director, bank attorney, or employee.

B. Is the beneficial owner, directly or indirectly, of any of the shares of stock of the bank.

C. Has any proprietary interest in any partnership, firm, or corporation which controls the banks, directly or indirectly.

D. The bank under examination has outstanding loans to the certified public accountant, licensed public accountant, partners, principals of the firm, or employees of such a firm who are directly involved in the examination, unless the loans are adequately disclosed in the audit report to the board of directors of the bank. Adequate disclosure includes the name of the borrower, the amount of the loan, the security pledged, and the appraisal or market value of the security at the time of the engagement.

E. Makes entries or postings on the books of account or performs any other operating functions for the bank, except functions for which prior approval was requested and obtained in writing from the commissioner of commerce.

KEY: PROPOSED RULES SECTION — Underlining indicates additions to existing rule language. ~~Strike outs~~ indicate deletions from existing rule language. If a proposed rule is totally new, it is designated "all new material." ADOPTED RULES SECTION — Underlining indicates additions to proposed rule language. ~~Strike outs~~ indicate deletions from proposed rule language.

F. Has other unusual relationships or affiliations with the bank that question independence.

In circumstances where directors, appointees, or the internal auditor are considered not independent or qualified to perform the annual audit, the board should engage a certified public accountant or licensed public accountant.

Subp. 5. **Board of directors.** If the requirements of this part are to be accomplished by the board of directors as provided in Minnesota Statutes, section 48.10, the board must number at least five and include at a minimum one outside director.

Subp. 6. **Audit by outside parties.** At least one examination every four years must be completed by outside parties as set forth in subpart 3.

Department of Human Services

Proposed Permanent Rules Relating to Nursing Home Payment Rate Determination

Notice of Proposed Adoption of Amendments to Permanent Rules without a Public Hearing

Notice is hereby given that the State Department of Human Services proposes to amend the above-entitled rule without a public hearing following the procedures set forth in the Administration Procedure Act for adopting rules without a public hearing in Minnesota Statutes, sections 14.22 to 14.28. The statutory authority for the rules is found in Minnesota Statutes, section 256B.502.

All persons have 30 days or until 4:30 p.m. on October 8, 1986 in which to submit comment in support of or in opposition to the proposed rule amendments or any part or subpart of the rule amendments. Comment is encouraged. Each comment should identify the portion of the proposed amendments addressed, the reason for the comment, and any change proposed.

Any person may make a written request for a public hearing on the rule amendments within the 30-day comment period. If 25 or more persons submit a written request for a public hearing within the 30-day comment period, a public hearing will be held unless a sufficient number withdraw their request. Any person requesting a public hearing should state his or her name and address and is encouraged to identify the portion of the proposed rule addressed, the reason for the request, and any change proposed. If a public hearing is required, the agency will proceed pursuant to Minnesota Statutes, sections 14.131 to 14.20.

Comments or written requests for a public hearing must be submitted to:

Jane Delage
Rules Unit
4th Floor, Centennial Building
St. Paul, Minnesota 55155
Telephone: 612/297-4302

The proposed rule amendments may be modified if the modifications are supported by data and views and do not result in a substantial change in the proposed rule amendments as noticed.

A copy of the proposed rule amendment is attached to this notice.

A free copy of the rule amendments is available upon request from Jane Delage. The rule is also available for viewing at each county welfare department in the state of Minnesota.

A Statement of Need and Reasonableness that describes the need for and reasonableness of each of the proposed rule amendments and identifies the data and information relied upon to support the proposed rule has been prepared and is available from Jane Delage upon request.

The adoption of these rule amendments will not result in additional spending by local public bodies in either of the first two years following implementation of the rule.

If no hearing is required, upon adoption of the amendments, the rule and the required supporting documents will be submitted to the Attorney General for review as to legality and form to the extent the form relates to legality. Any person may request notification of the date of submission to the Attorney General. Persons who wish to be advised of the submission of this material to the Attorney General, or who wish to receive a copy of the adopted rule, must submit the written request to Jane Delage.

Leonard W. Levine, Commissioner
Department of Human Services

STATE OF MINNESOTA

STATE REGISTER

DEPARTMENT OF ADMINISTRATION—DOCUMENTS DIVISION



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PROPOSED RULES

Pursuant to Minn. Stat. of 1982, §§ 14.22, an agency may propose to adopt, amend, suspend or repeal rules without first holding a public hearing, as long as the agency determines that the rules will be noncontroversial in nature. The agency must first publish a notice of intent to adopt rules without a public hearing, together with the proposed rules, in the *State Register*. The notice must advise the public:

1. **that they have 30 days in which to submit comment on the proposed rules;**
2. **that no public hearing will be held unless 25 or more persons make a written request for a hearing within the 30-day comment period;**
3. **of the manner in which persons shall request a hearing on the proposed rules; and**
4. **that the rule may be modified if the modifications are supported by the data and views submitted.**

If, during the 30-day comment period, 25 or more persons submit to the agency a written request for a hearing of the proposed rules, the agency must proceed under the provisions of §§ 14.14-14.20, which state that if an agency decides to hold a public hearing, it must publish a notice of intent in the *State Register*.

Pursuant to Minn. Stat. §§ 14.29 and 14.30, agencies may propose emergency rules under certain circumstances. Proposed emergency rules are published in the *State Register* and, for at least 25 days thereafter, interested persons may submit data and views in writing to the proposing agency.

Department of Commerce

Proposed Permanent Rules Relating to Financial Institution Audit Control Policies

Notice of Intent to Adopt Rules without a Public Hearing

Notice is hereby given that the Department of Commerce proposes to adopt the above-entitled rules without a public hearing. The Commissioner of Commerce has determined that the proposed adoption of these rules will be noncontroversial in nature and has elected to follow the procedures set forth in Minnesota Statutes, Section 14.21.

Persons interested in these rules shall have 30 days to submit comments in support of or in opposition to the rules. Each comment should identify the portion of the proposed rule addressed, the reason for the comment, and any change proposed. The proposed rules may be modified if the modifications are supported by the data and views submitted to the Department and does not result in a substantial change.

No public hearing will be held unless twenty-five (25) or more persons make a written request for a hearing within the 30 day comment period. In the event a public hearing is required, the agency will proceed according to the provisions of Minnesota Statutes, Section 14.14, subd. 1.

Persons who wish to submit comments or a written request for a public hearing should submit them to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Building, St. Paul, MN 55101 telephone (612) 296-5689. Any person requesting a public hearing should state her or his name and address and is encouraged to identify the portion of the proposed rule addressed, the reason for the request and any change proposed and send this information to the above address.

Authority for the adoption of these rules is contained in Minnesota Statutes, Sections 45.023 and 46.01. Additionally a Statement of Need and Reasonableness of each provision and identifying the data and information relied upon to support the proposed rules has been prepared and is available upon request.

Pursuant to Minnesota Statutes Section 14.115, subdivision 2, the impact on small business has been considered in the promulgation of the rules. Anyone wishing to present evidence or argument as to the rules' effect on small business may do so. The Department's position regarding the impact of the rules on small business is set forth in the Statement of Need and Reasonableness.

Upon adoption of the final rules without a public hearing, the proposed rules, this Notice, the Statement of Need and Reasonableness, all written comments received, and the final Rules as Adopted will be delivered to the Attorney General for review as to form and legality, including the issue of substantial change. Persons who wish to be advised of the submission of this material to the Attorney General, or who wish to receive a copy of the final rules as proposed for adoption, should submit a written statement of such request to Richard G. Gomsrud, Department Counsel, Department of Commerce, 500 Metro Square Bldg., St. Paul, MN 55101.

KEY: PROPOSED RULES SECTION — Underlining indicates additions to existing rule language. ~~Strike outs~~ indicate deletions from existing rule language. If a proposed rule is totally new, it is designated "all new material." ADOPTED RULES SECTION — Underlining indicates additions to proposed rule language. ~~Strike outs~~ indicate deletions from proposed rule language.

A copy of the proposed rules is attached to this Notice. Copies of this Notice and proposed rules are available and may be obtained by contacting Richard G. Gomsrud at the above address.

Michael A. Hatch
Commissioner of Commerce

Rules as Proposed (all new material)

2675.2600 INTERNAL AUDIT CONTROL POLICY.

The board of directors of a bank, trust company, or savings bank shall establish a written internal audit control system. The individual directing the internal audit control system shall submit to the board of directors each quarter a report detailing the areas audited, results obtained, and the degree of compliance with established policies and internal controls. Documentation of audit procedures performed and the reports shall be maintained by the bank for inspection by the supervisory examiners and by the external auditors. The scope of coverage and effectiveness of the internal audit control system shall be reviewed for adequacy and approved by the board annually. The board shall consider inclusion of recommendations made by supervisory examiners and external auditors in the internal audit control system.

2675.2610 ANNUAL AUDIT REPORT.

Subpart 1. **Contents.** The annual audit report made under the direction of the board of directors pursuant to Minnesota Statutes, section 48.10, must include as a minimum:

A. a review of the adequacy of the internal control system and a test check to determine that control procedures are being followed;

B. a review of board policies for development and a test check to determine that policies are being followed;

C. confirmation of assets through a sample positive or negative verification and inspection of assets held at the bank;

D. confirmation of deposits through a sample positive or negative verification;

E. a review of all fixed assets, other real estate, and equity accounts since the last audit and recordation of board approval of transactions involving these accounts;

F. a review of income, expense, and related accrual accounts since the last audit;

G. a review of all general ledger accounts to determine their balanced condition, prompt reconciliation and appropriateness of reconciling items, and account makeup;

H. a review of delinquent loans and collection action taking place;

I. a review of the allowance for loan loss account;

J. a review of charge off loans, including loan files and notes;

K. a test check of loan files for documentation and approvals required by loan policy;

L. review of the electronic data processing systems and procedures if applicable;

M. review of significant activity in employee and officer accounts for propriety and compliance with bank policies and regulations; and

N. review of off-balance sheet items including letters of credit.

Subp. 2. **Preparation.** A written report of the annual audit must be prepared and must include the scope of audit including the size of the samplings taken. The report must summarize the findings and make recommendations for improving conditions, where appropriate.

Subp. 3. **Transmittal.** The written report shall be transmitted to the board of directors within 30 days of completion of the audit.

Subp. 4. **Board response.** The board shall prepare a written response on the findings and recommendations contained in the report and submit the response, the report, and its findings and recommendations to the Department of Commerce, Division of Financial Examinations, within 60 days of receipt of the audit report.

The board response shall be filed with the audit report as part of the bank's permanent records.

2675.2620 QUALIFICATIONS OF EXAMINING AUTHORITY.

Subpart 1. **Examining committee.** If the requirements of this part are to be accomplished in whole or in part by an examining committee appointed by the board, the audit must be completed by qualified directors or their appointees who are in fact reasonably independent. A director or appointee serving as a member of the examining committee will not be considered independent if:

A. the person is closely related to active officers or employees of the bank;

B. the person has outstanding loans with the bank subject to criticism by state or federal supervisory agencies; or

C. the person has other unusual relationships or affiliations with the bank that question independence.

Subp. 2. **Internal auditor.** If the requirements of this part are to be accomplished in whole or in part by an internal auditor, the examination must be completed by a qualified internal auditor who is in fact reasonably independent. An internal auditor will not be considered independent if:

A. the person is employed or accountable to anyone other than the board of directors, and salary and annual bonus are not set by the board;

B. duties within the bank are not confined entirely to bank auditing;

C. the person has any proprietary interest in any partnership, firm, or corporation which controls the bank, directly or indirectly;

D. the person has outstanding loans subject to criticism by state or federal supervisory agencies;

E. the person is a member of the immediate family of an officer, director, attorney, or employee for the bank; or

F. the person has other unusual relationships or affiliations with the bank that question independence.

In banks of less than $25,000,000 in total assets, where duties of the internal auditor cannot be confined entirely to bank auditing, the internal auditor will be considered reasonably independent only if someone else audits the areas for which the internal auditor has operational responsibilities. The board is responsible for determining that this degree of internal audit dependence is maintained.

Subp. 3. **Certified public accountants or licensed public accountants.** If the requirements of this part are to be accomplished in whole or in part by a certified public accountant or licensed public accountant, the audit must be completed by a qualified certified public accountant or a qualified licensed public accountant who is in fact independent. A certified public accountant or licensed public accountant will not be considered independent if:

A. The certified public accountant, licensed public accountant, or any member of a firm performing the audit is connected with the bank as an officer, director, attorney, or employee or is a member of the immediate family of an officer, director, bank attorney, or employee.

B. Is the beneficial owner, directly or indirectly, of any of the shares of stock of the bank.

C. Has any proprietary interest in any partnership, firm, or corporation which controls the banks, directly or indirectly.

D. The bank under examination has outstanding loans to the certified public accountant, licensed public accountant, partners, principals of the firm, or employees of such a firm who are directly involved in the examination, unless the loans are adequately disclosed in the audit report to the board of directors of the bank. Adequate disclosure includes the name of the borrower, the amount of the loan, the security pledged, and the appraisal or market value of the security at the time of the engagement.

E. Makes entries or postings on the books of account or performs any other operating functions for the bank, except functions for which prior approval was requested and obtained in writing from the commissioner of commerce.

F. Has other unusual relationships or affiliations with the bank that question independence.

In circumstances where directors, appointees, or the internal auditor are considered not independent or qualified to perform the annual audit, the board should engage a certified public accountant or licensed public accountant.

Subp. 4. **Board of directors.** If the requirements of this part are to be accomplished by the board of directors as provided in Minnesota Statutes, section 48.10, the board must number at least five and include at a minimum one outside director.

Subp. 5. **Audit by outside parties.** At least one examination every four years must be completed by outside parties as set forth in subpart 3.

2675.2630 PERSONAL FINANCIAL STATEMENT.

A stockholder who owns or controls 25 percent or more of bank stock, or 25 percent or more stock in a holding company that owns controlling interest of the bank, and who also serves as an active officer or director of the bank or bank holding company, must annually complete a personal financial statement. This statement must consist of a listing of assets and liabilities and be dated no more than one year before the annual audit. The statement must be submitted to the commissioner of commerce along with the audit report as prescribed in part 2675.2610, subpart 4.

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STATE OF MINNESOTA
DEPARTMENT OF COMMERCE

In the Matter of the Proposed Rules Relating to Financial Institution Audit Control Policies

FINDINGS OF FACT, CONCLUSIONS, AND ORDER ADOPTING RULES WITHOUT PUBLIC HEARING

Notice of the Commissioner's intent to adopt the above rules was published in the State Register on September 8, 1986 and was sent by United States mail to all persons on the list maintained by the Department pursuant to Minnesota Statutes, sections 14.14, subdivision 1a and 14.22 on September 2, 1986. The statement of need and reasonableness was prepared before the notice of intent to adopt a rule without public hearing was mailed to all persons on the rulemaking list and published in the State Register and was available to the public.

All persons were given the opportunity to submit comment on the rule for 30 days after notice of proposed rulemaking. No requests for hearing were received. In addition, on June 8, 1987, the time period for comments was extended until July 8, 1987. No requests for hearing were received in regard to that notice.

No submissions or comments were received by the department regarding the rules, nor were and requests for notice of submission to the attorney general received by the department.

Based on the comments and evidence in the record before the departmen I find the following:

That certain minor grammatical changes are needed to make the rules as clear as possible and also to correct improper gender references. The changes are indicated on the attached copy of the rules. None of the changes are substanative and merely state the rule as proposed in a clearer way.

The above captioned rule as modified is needed and reasonable.

NOW, THEREFORE, IT IS ORDERED that the rules identified as Rules Relating to Financial Institution Audit Control Policies, as modified, are adopted this 3rd day of August, 1987 pursuant to the authority vested in me by Minnesota Statutes, sections 45.023 and 46.01

MICHAEL A. HATCH
Commissioner of Commerce

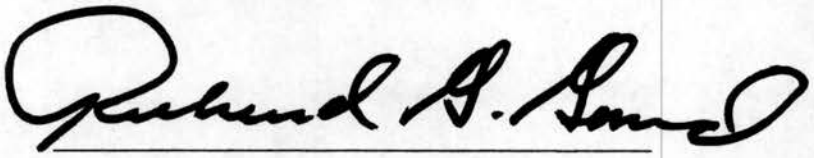
STATE OF MINNESOTA

DEPARTMENT OF COMMERCE

In the Matter of the Rules
Relating to Financial
Institution Audit Control
Policies

Statement of Department
Counsel

Richard G. Gomsrud, Department Counsel for the Minnesota Department of Commerce does hereby state that he is the person charged with the responsibility for the adoption of the above captioned rules. That after the Notice to Solicit Outside Opinions was published no opinions were received. Accordingly the Department published proposed rules on July 26, 1986 at 11 S.R. 101. Due to the number of comments about the proposed rules they were withdrawn by order of the Commissioner on August 25, 1986 and new rules were proposed and published in the State Register. 25 or more requests for hearing were not received in regard th the subsequent publication. Due to the length of time between that subsequent publication and the submission to the Attorney General's Office the comment period was extended and notice of the same was published in the State Register.



ADOPTED RULES

The adoption of a rule becomes effective after the requirements of Minn. Stat. § 14.14-14.28 have been met and five working days after the rule is published in *State Register*, unless a later date is required by statutes or specified in the rule.

If an adopted rule is identical to its proposed form as previously published, a notice of adoption and a citation to its previous *State Register* publication will be printed.

If an adopted rule differs from its proposed form, language which has been deleted will be printed with strikeouts and new language will be underlined. The rule's previous *State Register* publication will be cited.

An emergency rule becomes effective five working days after the approval of the Attorney General as specified in Minn. Stat. § 14.33 and upon the approval of the Revisor of Statutes as specified in § 14.36. Notice of approval by the Attorney General will be published as soon as practicable, and the adopted emergency rule will be published in the manner provided for adopted rules under § 14.18.

Department of Labor and Industry

Adopted Permanent Rules Relating to Qualifying Eligibility Criteria

The rules proposed and published at *State Register*, 22 September 1986, Volume 11, Number 12, pages 487-490 (11 S.R. 487) are adopted with the following modifications. The entire rule containing all amendments is reprinted below.

Rules as Adopted

5220.1400 QUALIFYING ELIGIBILITY CRITERIA FOR REHABILITATION CONSULTANT.

Subpart 1. **Requirement.** To become registered as a qualified rehabilitation consultant, the certification, education, and internship requirements of subparts 2 to 5 must be met.

Subp. 2. **Certification and education.** A qualified rehabilitation consultant/affiliated/independent shall possess the following credentials as applicable:

A. holder of a baccalaureate degree, together with certification by the Board of Rehabilitation Certification as a certified rehabilitation counselor or a certified insurance rehabilitation specialist; or

B. holder of a baccalaureate degree together with certification by the Association of Rehabilitation Nurses as a certified rehabilitation registered nurse and current licensure as a registered nurse in Minnesota.

Persons who are qualified rehabilitation consultants on the effective date of this part must obtain the certification described in item A or B within two years of that effective date. If a qualified rehabilitation consultant lacks two years or more of the experience required to meet the certifying body's minimum experience or internship requirement, the time for becoming certified shall equal the time remaining for completion of the certifying body's minimum experience or internship requirement. If a qualified rehabilitation consultant must also obtain a baccalaureate degree to meet the certifying body's minimum education requirements, the qualified rehabilitation consultant shall have an additional four years to become certified. If an examination is required for certification, the time allowed for certification under this part must include at least two scheduled examinations which the applicant is eligible to take. The qualified rehabilitation consultant shall select on the consultant's next annual application for registration the certifying body and program under which the qualified rehabilitation consultant is seeking certification. Persons who are qualified rehabiliation consultant interns on that effective date may become qualified rehabilitation consultants under the requirements in place prior to the effective date. Upon becoming qualified rehabilitation consultants, such persons must obtain certification as required by this paragraph.

Subp. 3. **Rehabilitation consultant intern.** An individual who meets the requirements of subpart 2, item A or B may be registered as a consultant intern. An individual who meets the requirements of subpart 2, item A or B, except that two years or less of internship or experience remains as a requirement for certification, may be registered as a consultant intern. The intern must work for at least one year as a qualified rehabilitation consultant intern in the rehabilitation of injured workers. When the intern is registered, the intern's employer shall provide the commissioner with the name of the qualified rehabilitation consultant under whose direct supervision the intern will work, and shall submit a plan of supervision on forms required by the commissioner. Direct supervision means that the supervisor is directly responsible for the rehabilitation work on any case. The supervisor shall co-sign all work being done by the intern and there shall be no billing by the supervisor for these supervisory duties. The supervisor shall attend all administrative conferences with the intern and shall arrange for training and seminars as required by the commissioner. So that all parties are aware of the intern's status, the intern shall be designated as an "intern" on all documents bearing the name of the intern. The intern may make application for "qualified" status when the minimum requirements in subpart 2, item A or B have been met.

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STATE OF MINNESOTA

DEPARTMENT OF COMMERCE

In the Matter of the Adoption of the Rules of the State Commerce Department Governing Financial Institution Audit Control Policies.

DECLARATION OF COUNSEL

I, Gregory P. Huwe, Special Assistant Attorney General, do hereby declare that I have examined the above-captioned rules, and the supporting rulemaking record, and that, based on my examination, the Administrative Procedure Act and Minnesota Rules, chapter 2010 have been followed. For Attorney General billing purposes, the four-digit docket client code is 0112.

Gregory P. Huwe

GREGORY P. HUWE
Special Assistant
Attorney General

Dated: 9-1-87

STATE OF MINNESOTA

COUNTY OF RAMSEY

CERTIFICATE

In the Matter of the Proposed Rules
Relating to Financial Institution Audit
Control Policies

I hereby certify that the list of persons, associations, and other interested groups who have requested, pursuant to Minnesota Statutes, section 14,14, subd. 1a, that their names be placed on file with and maintained by the Department of Commerce for the purpose of receiving notice of the proposed adoption of rules is accurate and complete as of 12:00 P.M.,' this 2nd day of September, 1986

Richard G. Gomsrud

Regulation Analyst
Alliance of American Insurers
1501 W[illegible]eld Rd., Suite 400 West
Schaumb[illegible], IL 60195-4980

Mr. Robert J. Demichelis
American Council of Life Insurance
1850 K Street NW
Washington, DC 20006

Frederick P. McGarvey
American Insurance Association
230 W. Monroe St.
Chicago, IL 60606

Daniel D. Foth
Associated Builders & Contractors
6989 Washington Ave. So., Suite 200
Edina, MN 55435

Morris J. Anderson, Exec. Dir.
Association of Minnesota Counties
555 Park Street, Suite 300
St. Paul, MN 55103

R. G. Lanham, Dir. of Research
Carleton Financial Computations
P.O. Box 570
South Bend, IN 46624

Rosalie Beck Detmer, Counsel
Central Life Assurance Company
P.O. Box 5099
Madison, WI 53705

Glen Tullman
Certified Collateral Corporation
640 N. LaSalle, Suite 640
Chicago, IL 60610

M. D. Monette, V. P. & Counsel
Colonial Penn Group, Inc.
5 Penn Center Plaza
Philadelphia, PA 19181

Barbara Weisenbach
Continental American Life Ins Company
P.O. Box 15750
Wilmington, Delaware 19850

Coury, Schwinn & Kodadek
400 Marquette Ave. Suite 300
Minneapolis, MN 55401

Norman E. Nelson
Manager, Govt. Affairs Dept.
Crum & Forster Corporation
305 Madison Avenue CN 1932
Morristown, NJ 07960

Gerald G. Dederick, P.A.

6800 France Ave. S., #750
Edina, MN 55435

Conrad M. Fredin

811 Norwest Center
Duluth, MN 55802

Susan J. Ladwig
North Star Policy Associates
114 Metro Square Bldg. 7 & Robert St.
St. Paul, MN 55101

Ron Marien

9604 13th Ave. S.
Bloomington, MN 55420

Randy Nornes

1740 W. Larpenteur Ave. #3F
St. Paul, MN 55113

Kris Novak

4537 Ridgeview Dr.
Eagen, MN 55123

Archibald Spencer

3500 IDS Center
Minneapolis, MN 55402-2213

Karen Koast
Dean Witter Reynolds Inc.
Compliance Dept.
5 World Trade Center, 4th Floor
New York, NY 10048

C. Warren Coulter, Asst. Dir.
Dept. of Land Registration
P.O. Box 569
Bentonville, AR 72712

Jeffrey A. Redmon
Doherty, Rumble & Butler
Professional Association
East 1500 First Nat'l Bank Bldg.
St. Paul, MN 55101

Dominic J. Sposeto
Dominic Sposeto & Associates
2824 Irving Avenue S.
Minneapolis, MN 55408

Fireman's Fund Emp. Ins. Co.
Contracts Department
Green Bay, WI 54344

Joyce Bulleri
Frank B. Hall & Co. of CA
1550 W. Fremont, P.O. Box C
Stockton, California 95201-3003

Harold J. Soderberg
Hessian, McKasy & Soderberg
4700 IDS Center
Minneapolis, MN 55402

Peggy Jacobs
IDS Financial Serv., Inc. - Unit 53
IDS Tower
Minneapolis, MN 55474

Norbert A. McCrady
Independent Bankers of Minn.
7850 Metro Pkway., Suite 211
Bloomington, MN 55420

Rudy D. Broyles, CPCU
Insurance Services Office, Inc.
111 North Canal Street
Chicago, IL 60606

Richard Schinler, President
Integrity Mutual Insurance Company
P.O. Box 539
Appleton, WI 54912

Susan Burgess
Investment Company Institute
1600 M Street NW
Washington, DC 20036

Jerrold T. Miller
J. T. Miller Company
1000 [redacted]e Avenue
Minneapolis, MN 55403

John B. LaMacchia & Associates
Actuaries Management Consultants
12 North Central Avenue
St. Louis, MO 63105

Maryanne Hruby, Exec. Director
LCRAR
Rm. 55, State Office Building
St. Paul, MN 55155

John R. Houston, Esq.
Lindquist & Vennum
4200 IDS Center
Minneapolis, MN 55402

Kathleen M. Kellerman
Mairs and Power, Inc.
W-2062 First National Bank Bldg.
St. Paul, MN 55101

Mr. Ronald R. Radtke, Mgr., Comp. Svcs.
Metropolitan Prop. & Liability Ins. Co.
700 Quaker Lane
Warwick, RI 02887

Gary K. Thaden
MN Asbestos Abatement Contract Assn
766 Transfer Road
St. Paul, MN 55114

John S. Jackson, Gen. Counsel
Minnesota Bankers Association
332 Baker Building
Minneapolis, MN 55402

Thomas Houser, Managing Sec'y.
Minnesota Insurance Guaranty Association
4640 West 77th Street Suite 342
Edina, MN 55435

Tom Haider
Minnesota League of Credit Unions
575 University Ave.
St. Paul, MN 55103

MN Motor Transport &
Permit Carriers Assn.
1821 University Ave., Room 134N
St. Paul, MN 55104

Jean Dawson
Minn. Government Report
B-12 Press Room, State Capitol
St. Paul, MN 55155

Minn. Mfg. Housing Assoc.
222 E. Little C[redacted]a Rd., S222
St. Paul, MN 5[redacted]

John G. Horner
Minnesota Multi Housing Assn.
4740 Park Glen Road
Minneapolis, MN 55416

Minn. Petroleum Council
386 N. Wabasha, Suite 1025
St. Paul, MN 55102

John Van Doorn
Minn. Retail Merchants Assoc.
180 Metro Square Bldg.
St. Paul, MN 55101

Minn. School of Real Est. Inc.
9944 West 74th St.
Eden Prairie, MN 55344

Mary Miranowski, Exec. Dir.
Minn. State Builders Assoc.
1410 Energy Park Dr. #6
St. Paul, MN 55108-5296

Abe Rosenthal, Pres.
Minn. Transport Services Assn.
1821 University Ave. (Suite N310)
St. Paul, MN 55104

Michael J. Ahern
Moss & Barnett
200 S. Sixth St.
Minneapolis, MN 55402

John F. Stone
Moss & Barnett
200 S. Sixth St.
Minneapolis, MN 55402

Robert L. Zeman, Asst. Couns.
Natl. Assoc. of Ind. Insurers
2600 River Road
Des Plaines, IL 60018-3286

William R. Anderson, Counsel
Natl. Assoc. of Life Underwriters
1922 F Street, NW
Washington, D.C. 20006-4387

Richard Bouhan, Gov't. Relations Dir.
Natl. Assoc. of Prof. Surplus Lines Off.
P.O. Box 1507
Roswell, GA 30077

Lee [illegible] Peterson
Nelson, Nelson, Kufus & Peterson
66[redacted] Snelling Ave.
St[redacted]aul, MN 55104

NIARS Corporation
Three Eighteen West Franklin
Minneapolis, MN 55404

Dan Boyle, Assoc. Gen'l Counsel
Northern Assurance Co. of Amer.
One Beacon Street
Boston, MA 02108

Mark A. Welshons, Secretary
NWNL Reinsurance Company
P.O. Box 20
Minneapolis, MN 55440

Sam Ruhle
Office of Administrative Hearings
400 Summit Bank Building
Minneapolis, MN 55415

R. Mark Lawrence, Contract Specialist
Ohio State Life Insurance Company
2500 Farmers Drive
Columbus, OH 43085

Lois A. Hout, Asst Gen'l Coun & VP
Orion Group - Law Division
9 Farm Springs Dr.
Farmington, CT 06032

Donna Jerex, I-5
Pennsylvania Life Insurance Company
3130 Wilshire Blvd.
Santa Monica, CA 90406

Peter S. Popovich

1300 Amhoist Tower
St. Paul, MN 55102

Phillips Legislative Service, Inc.
459 Rice Street
St. Paul, MN 55103

Bruce A. Poulsen, V.P. & Counsel
Prudential Insurance Co. of America
8th Fl., P.O. Box 1143
Minneapolis, MN 55440

James M. Shamberger, Vice President
Reinsurance Association of America
1025 Connecticut Ave. NW,
Washington, D.C. 20036

St. Paul Companies, Inc.
385 Washington Stre[redacted]
St. Paul, MN 5510[redacted]

Karen Langland, Government Affairs
St. Paul Fire & Marine Ins. Co.
385 Washington St.
St. Paul, MN 55102

Paul Dwyer, Gen'l Counsel's Office
Title Insurance Company of MN
400 Second Avenue South
Minneapolis, MN 55401

John M. Marshall, V.P. & Chief Coun.
Union Fidelity Life Insurance Co.
4850 Street Road
Trevose, PA 19049

Jerome Scheibl, Vice President
Wausau Insurance Group
2000 Westwood Dr.
Wausau, WI 54401

Larry J. Smith Asst Sec'y Public Affairs
Western Insurance Companies
14 East First
Fort Scott, Kansas 66701

John A. Knapp, Esq.
Winthrop & Weinstine
1800 Conwed Tower, 444 Cedar
Saint Paul, MN 55101

Workers Comp. Reinsurance Assoc.
900 Minnesota Mutual Life Center
400 North Robert Street
St. Paul, MN 55101-2092

[redacted]

Rider, Bennett, Egan & Arundel
2500 First Bank Pl. W.
M[redacted]apolis, MN 55402

Ford M. Robbins
Robbins & Rashke
5200 Willson Road, Suite 407
Minneapolis, MN 55424

Robert R. Abrohams Agency, Inc.
1112 Plymouth Bldg.
Minneapolis, MN 55402

Bernard Rosenberg
Robins, Zelle, Larson & Kaplan
1800 International Centre
900 South Second Avenue South
Minneapolis, MN 55402

Gerard J. Quinn, Asst. Gen'l Coun.
Securities Industry Association
120 Broadway
New York, NY 10271

Ted Burton
Security Schools
268 West Burnsville Parkway
Burnsville, MN 55337

Cezar M. Froelich, Esq.
Shefsky, Saitlin & Froelich, Ltd.
444 N. Michigan Ave., Suite 2300
Chicago, IL 60611

George M. Boyd
Squire, Sanders & Dempsey
1800 Huntington Building
Cleveland, OH 44115

David A. Peterson
State Bond & Mortgage Company
100 North Minnesota Street
New Ulm, MN 56073

Charles F. Happach, President
State Capitol Credit Union
95 Sherburne
St. Paul, MN 55103

Randall Young
State Planning Agency
101 Capitol Square Building
St. Paul, MN 55101

Mary Stanton, Staff Assoc./Fin.
State University System
555 Park St., Suite 230
St. Paul, MN 55103

STATE OF MINNESOTA
DEPARTMENT OF COMMERCE

In the Matter of the Proposed Rules Relating to Financial Institution Audit Control Policies	ORDER FOR NOTICE OF INTENT TO ADOPT RULES WITHOUT PUBLIC HEARING

IT IS ORDERED this 26th day of August 1986 that Notice of Intent to Adopt Rules Without Public Hearing in the above-entitled matter be given to all persons who have registered their names with the Department of Commerce for that purpose and be published in the State Register.

MICHAEL A. HATCH
Commissioner of Commerce

STATE OF MINNESOTA

DEPARTMENT OF COMMERCE

In the Matter of the Proposed Rules Relating to Financial Institution Audit Control Policies

CERTIFICATE OF COMPLIANCE WITH RULEMAKING PROCEDURES

I, do hereby declare that I have examined the rules and related documents and that, based on my examination and my personal familiarity with the applicable procedures, the Administrative Procedures Act, the rules of the Office of Administrative Hearings, and the rules of the Attorney General have been followed. Any exceptions are noted belowl

_____

Dated:

SF-00006-04

STATE OF MINNESOTA

Office Memorandum

DEPARTMENT : of Commerce

PHONE : 296-5689

DATE :

TO : Martha Casserly

FROM : Richard G. Gomsrud
Department Counsel

SUBJECT : Bank Credit Rules.

These are the rules you & I discussed that had to have the comment period extended. Anything you can do to expedite them would be greatly appreciated.

Enclosed are copies of the following materials regarding the above captioned rules (only those items with a circled number are enclosed):

(1.) Notice of Intent to Solicit Outside Opinion (2000.0400 subpart 1 B)

~~2.~~ Written material received as a result of Notice to Solicit Outside Opinion (2000.0400 subpart 1 B) NONE

(3.) Mailing List Certificate (2000.0400 subpart 1 E)

(4.) Statement of Need & Reasonableness (2000.0400 subpart 1 G)

(5.) Order for Notice of Intent to Adopt Rule Without Public Hearing (2000.0400 subpart 1 C)

(6.) Notice of Intent to Adopt Rule Without Public Hearing (2000.0400 subpart 2)

(7.) Affidavit of Mailing Notice of Intent to Adopt Rule Without Public Hearing (2000.0400 subpart 3)

(8.) Copy of Notice of Intent to Adopt Rule Without Public Hearing and rules as published in the State Register (2000.0400 subpart 4)

~~9.~~ Written Comments on Rule (2000.0400 subpart 1 I) NONE

(10.) Findings of Fact (if applicable) (2000.0400 subpart 1 F)

~~11. Affidavit of Mailing Notice of Submission to Attorney General (2000.0400 subpart 1 K); or~~ See 10

RECEIVED
ATTORNEY GENERAL'S OFFICE

AUG 31 1987

204 ADMINISTRATION BLDG.
50 SHERBURNE AVENUE
ST. PAUL, MN 55155

~~12. Affidavit that no request for Notice of Submission to Attorney General were received~~ See 10

13. Original and three copies of Rule as adopted (2000.0400 subpart 5)

14. ~~Two copies of the Order Adopting Rule~~ (2000.0400 subpart 6) See 10

15. Certificate of Compliance With Rulemaking Procedure (2000.0400 subpart 1 J).

16. Statement of Department Counsel

17. Copy of S.P. w/Notice of Extension

SF-00006-05 (4/86)

STATE OF MINNESOTA

Office Memorandum

DEPARTMENT : of Commerce

DATE : September 4, 1987

TO : Rita Desmond

FROM : Richard G. Gomsrud

PHONE : 296-5689

SUBJECT : Financial Institution Audit Control Policies

Attached please find a copy of the proposed rules in regard to the above captioned matter which we inadvertantly left out of the packet. Please let us know if you need anything else.

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SEP 09 1987

204 ADMINISTRATION BLDG.
50 SHERBURNE AVENUE
ST. PAUL, MN 55155

Read: Statement of Department Counsel.

Memo: Requested expiration of approval.

Notice of Intent - ok

Proposed Rule - not Recd: called. Greg Haire

Authority -

~~401~~ 46.01 ok

45.023 ok

Rule:

Changes made on "Adopted Rule"

SF-00006-05 (4/86)

STATE OF MINNESOTA

Office Memorandum

DEPARTMENT : ATTORNEY GENERAL - Bremer Tower

DATE : September 1, 1987

TO : MARTY CASSERLY
Administration Division

FROM : GREGORY P. HUWE
Special Assistant
Attorney General

PHONE : 6-9418

SUBJECT : Financial Institution Audit Control Policies.

I understand that Department staff attorney Dick Gomsrud has forwarded the above-referenced rules and supporting documents to you for your review.

Enclosed is my Declaration of Counsel as recommended by Attorney General Rule 2010.9935.

Please contact me if you have any questions.

GPH:sab
Enclosure

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