Approved: 2/15/95
Date

MINUTES OF THE Senate Committee on Financial Institutions and Insurance.

The meeting was called to order by Chairperson Dick Bond at 9:05 a.m. on February 14, 1995 in Room 529-S of the Capitol.

Members present were: Senator Clark, Senator Corbin, Senator Hensley, Senator Lawrence, Senator Lee, Senator Praeger, Senator Steffes

Committee staff present: Dr. William Wolff, Legislative Research Department
Fred Carman, Revisor of Statutes
June Kossover, Committee Secretary

Conferees appearing before the committee: James Maag, Kansas Bankers Association
Chuck Stones, Kansas Bankers Association
Janet Chubb, Assistant Secretary of State
Judi Stork, State Banking Department

Others attending: See attached list

Senator Clark moved to approve the minutes of the meeting of February 13 as submitted. Senator Lawrence seconded the motion; the motion carried.

The chairman opened the hearing on **SB 249**, which relates to a state bank's authority to purchase life insurance on its officers and directors and for employee deferred compensation plans. James Maag, Kansas Bankers Association, appeared as a proponent and explained the history of this legislation. (Attachment #1) Mr. Maag advised the committee that the bill contains three amendments to KSA 9-1101(25) and that the difficulties which would be alleviated by passage of the bill are especially acute in small communities. In response to Senator Bond's question, Mr. Maag advised that passage of the section which "grandfathers" in plans purchased prior to July, 1993, has been determined by the State Banking Department and the FDIC to present no potential safety and soundness problems.

Judi Stork, State Banking Department, spoke to the issue of safety and soundness and stated that this issue would be looked at during annual reviews and that the Bank Commissioner's office supports the bill. Ms. Stork also agreed with Mr. Maag that the bill should be amended to be effective upon publication in the Kansas Register.

There were no other conferees and no further questions; the hearing on **SB 249** was closed. Senator Lawrence made a motion to amend the bill to make the effective date the date of publication in the Kansas Register and to pass the bill as amended. Senator Praeger seconded the motion; the motion carried.

The hearing was opened on **HB 2080**, relating to the reproduction of bank records. Chuck Stones, Kansas Bankers Association, appeared as a proponent and explained that this bill would change the state banking code to enable banks to utilize current cost saving technology to store records. (Attachment #2) There were no questions and no other conferees; the hearing was closed. Senator Lee made a motion to pass the bill favorably and to place it on the Consent Calendar. Senator Corbin seconded the motion. The motion carried.

The chairman opened the hearing on **HB 2082**, relating to the filing of financial statements with the Secretary of State's office. Chuck Stones also testified as a proponent of this bill. (Attachment #3) Mr. Stones explained that this bill does not make changes to the legal definition of partnership; the bill says only that where married debtors are jointly engaged in business and it is unclear whether a partnership exists, the financing statement may be filed in the names of the individual debtors.

Janet Chubb, Assistant Secretary of State, testified that the bill would create no additional expense for that office and that the Secretary of State supports passage of this legislation. (Attachment #4)

There being no further conferees, the hearing on **HB 2082** was closed. Senator Steffes, noting that he could imagine no one who would be damaged by this legislation, made a motion to pass it favorably. Senator Lawrence seconded the motion; the motion carried.

The hearing was reopened on **SB 126**, relating to late enrollees for group health and accident insurance. This bill was originally heard in committee on 2/1/95 and was tabled pending further study of Section 2, page 2. Senator Praeger stated that this section has the potential to drive up costs to everyone . Senator Lawrence made a motion to amend the bill by striking Section 2. The motion was seconded by Senator Praeger. The motion carried.

Senator Clark asked if page 1, line 34, should also include both individual and group policies. Dr. Woolf replied that this statute deals only with group policy enrollment and the issue of individual enrollment should be dealt with as a separate issue. Senator Clark agreed.

Senator Praeger made a motion to pass the bill favorably as amended. Senator Hensley seconded the motion; the motion carried.

The committee adjourned at 9:42 a.m. The next meeting is scheduled for February 15., 1995.

SENATE FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE GUEST LIST

DATE: 2/14/95

NAME	REPRESENTING
Chuck Stones	KBA
Jim Maag	"
Kathy Taylor	"
Tom Wilder	Kansas Dept of Insurance
J. Chubb	S.O.S.
Danielle Noe	KCUA
Bill Sneed	HIAA
Judi Stork	OSBC
Roger Fauzke	FFC

The KANSAS BANKERS ASSOCIATION
A Full Service Banking Association

February 14, 1995

TO: Senate Committee on Financial Institutions and Insurance
RE: **SB 249** - The purchase of life insurance by banks

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to appear before the committee in support of **SB 249** which amends the state banking code. Specifically it makes three amendments to K.S.A. 9-1101(25) which relate to a state bank's authority to purchase life insurance for its officers and directors and for employee deferred compensation plans.

The first amendment to K.S.A. 9-1101(25) restricts the types of investments which a bank can make for policies where the bank has the authority to direct the investment of the policy's cash values. It states that such investments are limited to those assets which may be directly purchased by the bank for its own account.

The second amendment grandfathers life insurance policies in place before July 1, 1993, which may not meet new federal guidelines relating to the projected value of such policies. These are policies which have been in effect for some time and at the time they were entered into they were meeting state and federal requirements. To be forced to restructure such policies at this time could have very significant financial consequences for the bank from a standpoint of taxes and surrender charges. This is a particular problem for a number of small community banks where these policies are a very key part of retaining qualified management for the bank.

The third amendment removes the requirement of a mathematical test which attempts to determine the value of the policy at some future date which may be as much as four decades away. The test results are virtually meaningless since it is necessary to make assumptions on factors where there is little, if any, consensus. Again this is a particular problem for community banks which have a smaller capital base.

Attached to this testimony is a letter from Kevin Murphy of Bank Compensation Strategies. His company works with community banks in Kansas to create

Senate 7/+1
2/14/95
Attachment #1

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retirement plans and benefit plans for bankers. Mr. Murphy also addresses the proposed amendments and requests favorable consideration of **SB 249**.

The KBA has worked closely with the State Banking Department for the past three years in an attempt to resolve this very complex problem which has been exacerbated by the shifting guidelines of federal regulatory agencies. We sincerely hope this amendatory language will finally resolve what has been a highly troublesome impediment to community banks which need the ability to offer attractive benefit plans to qualified employees.

Your favorable consideration of **SB 249** would be greatly appreciated.

James S. Maag
Senior Vice President

BANK
COMPENSATION
STRATEGIES GROUP

February 10, 1995

The Honorable Richard Bond
Chairman
Senate Committee on Financial Institutions and Insurance
The State Senate
State Capital
Topeka, Kansas 66612

Sir:

Bank Compensation Strategies Group is a Minneapolis based company which designs and markets retirement and other benefit plans for bank executives, many of which are informally financed by bank-owned life insurance policies. We have approximately 700 client banks nationwide. Our firm is endorsed by the Kansas Bankers Association, the American Bankers Association and 39 other state bankers associations. We believe that affordable benefit plans enhance the ability of community banks to attract and retain competent managers which is critical to their continued success and viability.

We have had the opportunity to review the proposed amendments to K.S.A. 9-1101(25) as set forth in Senate Bill No. 249.

The proposed amendments would grandfather life insurance policies in place before July 1, 1993; strike the language contained in subsection (vii) of K.S.A. 9-1101(25); and where a bank has the authority to direct the investment of policy cash values, limit the investments to only those assets that may be directly purchased by the bank for its own account.

We believe that grandfathering existing policies is warranted because restructuring existing policies to meet new guidelines often requires the withdrawal of cash from a policy, which may result in adverse tax consequences or surrender charges to the bank which owns the policy. This amendment will enable banks which have owned life insurance policies for many years to avoid additional costs and taxes and we support the change.

As contained in the current law, subsection (vii) applies when life insurance is purchased for the purpose of providing deferred compensation and benefit plans and reads as follows:

> "the present value of the projected cash flow from the policy must not substantially exceed the present value of the projected cost of the deferred compensation or benefit program liabilities"

The current language requires that a mathematical test be prepared when a bank purchases a life insurance policy in connection with compensation or benefit plans. Compliance with this provision requires that financial projections be made far into the future (30 to 40 years is not uncommon) which are then converted back to current dollars by way of present value calculations. In order to perform the calculations, assumptions must be made concerning interest rates, insurance mortality costs, tax rates and life expectancy of plan participants. The calculations are very sensitive to minor

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changes in assumptions and there is no consensus concerning the reasonableness of assumptions used in these computations. Also, many insurance vendors are unable or unwilling to unbundle the costs and income components of their policies and provide the information needed to make the calculations. Our experience with the tests required by this subsection is that they are needlessly complex, not well understood by bankers, bank regulatory officials and insurance providers, and we believe that the test results have little or no economic significance. The test requirements are a significant burden to community banks and we support the elimination of this portion of the law.

The third element of the proposed amendment would add language to K.S.A. 9-1101(25) which would, in the situation where a bank has the authority to direct the investment of the life insurance policy cash values, limit the types of investments to those which may be directly purchased by the bank for its own account. There are a myriad of life insurance products available in the marketplace today, including variable life insurance policies, where the policy owner selects where the policy cash values are to be invested. Several options are typically available, including money market funds, bond funds and common stock funds. With this type of life insurance policy, the policy owner bears all of the investment risks associated with fluctuations in the value of the policy cash values. While these types of policies are suitable and appropriate in many circumstances, both state legislatures and the U.S. Congress have enacted laws which generally prohibit commercial banks from investing in corporate equity instruments and common stocks. The proposed amendment would prohibit a state bank from making an investment through the purchase of a life insurance policy that it would be prohibited from making directly. We believe that the addition of this provision is appropriate.

In summary, we believe that the proposed amendments would be beneficial to the banking industry, without any adverse effect on bank soundness or solvency.

We appreciate the opportunity to submit comments.

Thank you in advance for your consideration.

Very truly yours,

Kevin M. Murphy
Vice President of Compliance

The Kansas Bankers Association

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February 14, 1995

TO: Senate Financial Institutions and Insurance Committee

FROM: Chuck Stones, Director of Research

RE: HB 2080

Mr. Chairman and Members of the Committee,

The Kansas Bankers Association appreciates the opportunity to appear today in support of HB 2080.

State law requires that banks retain certain records for periods of time prescribed by the Bank Commissioner. The retention of these records has been made more cost-efficient with technological advances. HB 2080 would allow banks to use read-only imaging technology by allowing such records to be admissible in court.

Attached is a memo from Bill Grant, General Counsel for the State Banking Department that outlines the reasoning for HB 2080. In essence the memo states that while K.S.A. 9-1130 would allow banks to use read-only imaging, technically a bank could not because such records are not admissible by banks in a court of law. Last year, K.S.A. 60-469 was amended to allow the admissibility of business records using such technology. However, the banking code allows for a specific type of imaging and therefore takes precedent over the general business statute.

We are therefore requesting this change in the banking code which mirrors KSA 60-469 to enable banks to utilize current cost saving technology.

Thank you for your attention and we urge your favorable action.

Senate 7/4
2/14/95
Attachment #2

Office of the State Bank Commissioner
Memorandum

EXHIBIT J

Date: October 4, 1994

From: William Grant
General Counsel

RE: **Record Storage by Electronic Means**

THIS MEMO SUPERSEDES THE PREVIOUS MEMO OF AUGUST 31, 1994, RELATING TO OPTICAL DISK STORAGE OF RECORDS CONTAINED IN THE RECENT ALL BANK MAILING. THE PREVIOUS MEMO SHOULD BE DESTROYED.

K.S.A. 9-1130 provides in general that a bank or trust company must retain records for periods prescribed by the commissioner. These periods have been more definitively defined by promulgation of K.A.R. 17-15-1 and amendments thereto. With regard to the utilization of optical disk storage of records, 9-1130(f) expressly provides "...any bank or trust company may cause any, or all, of its records ... to be photographed or otherwise reproduced to permanent form." This language is interpreted to mean that maintenance of bank records by use of electronic means is acceptable so long as the technology is of the "read-only" variety. (Read-only, as used in this memo, means that once a record is placed on the system the information is static and the image can not be altered.)

A related question involves the courtroom admissibility of records stored and document images retrieved from an electronic storage system. While K.S.A. 9-1121 provides for the admissibility of "microphotographed" reproductions, the department has taken the position that the specific reference to a particular method of recordation would infer the non-admissibility of records stored by alternative means. This conclusion has been weakened by amendment last session of K.S.A. 60-469 to provide for the admissibility of copies of certain business records retrieved from "read-only" optical systems. (1994 Session Laws, ch. 60, section 1.)

An important consideration which must be reviewed is the fact that the new admissibility provision relating to optical disk recordation contained in 60-469 is a general civil procedure provision while the more restrictive provision of 9-1121 is found in the Kansas Banking Code and relates specifically to records maintained by banks, trust companies, and savings and loans. The general rule of statutory construction in Kansas relating to the interaction between general and specific statutes is that general and specific statutes should be read together and harmonized whenever possible, but to the extent conflict exists, the specific statute will control unless it appears the legislature intended to make the general statute controlling. State v. Edwards 252 Kan. 860 (1993).

Because of the apparent conflict between the statutes and the lack of any review by a court on the effect of the new general civil procedure provision on the existing specific banking code language, every institution should consult with bank counsel prior to destroying any records it intends to maintain by electronic means, to assess the need for retention of the items in a form suitable for use during possible litigation.

Finally, paper files and information, or hard copies of the files produced by the electronic storage technology, must be available on an expedient basis for review by this department's examination staff. While CRT's or other electronic technology may occasionally be utilized by the examiners, the majority of the file reviews will continue to be accomplished by reference to paper copies. The availability of terminals or readers alone will not be sufficient to meet this requirement at this time.

2-2

The Kansas Bankers Association

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2-14-95

TO: Senate Financial Institutions and Insurance Committee

FROM: Chuck Stones, Director of Research

RE: HB 2082

Mr. Chairman and Members of the Committee:

The Kansas Bankers Association appreciates the opportunity to appear before you in support of HB 2082.

It is not always easy to determine whether a small business is a partnership or a sole-proprietorship. For many years, the banking industry didn't worry much about this distinction. It never seemed to matter how an account or loan was documented for this purpose. But current laws and regulations now require a bank to determine whether a customer is doing business as a partnership of a sole proprietorship.

The KBA formed a taskforce to study this problem over the summer. The taskforce identified many areas of banking where this situation might potentially be problem. Most of these situations had solutions that were administrative in nature. It did recommend that we seek a legislative remedy to the problem addressed in HB 2082.

HB 2082 addresses the filing of UCC-1 forms or financing statements with the Secretary of State. UCC-1 forms are filed to establish the creditors rights to collateral used in obtaining a loan. A lender is said to be "perfected" if the UCC-1 is filed correctly. If a business is a partnership, the UCC-1 must be filed in the name of the partnership and the partnership's Employee Identification Number. But if the business is a sole proprietorship, the UCC-1 must be filed in the name of the sole proprietor and his or her Social Security Number. A bank must rely on the borrower(s) to make a determination as to the nature of the business. The banker is not to be expected to sort through a couple's business affairs to make this determination. Once the borrower(s) has decided upon a appropriate business structure, the banker can accept their decision as appropriate and document the loan accordingly.

This is where the potential problem arises. Under Kansas law, a partnership is statutorily defined as an association of two or more persons to carry on as co-owners of a business for profit. Under this definition, a legal partnership may exist even though formal partnership papers do not exist. Our concern is that the potential exists for a bank to have filed a UCC-1 for a business loan as a sole proprietorship based on their customers determination. Later, in a court of law, the business could be found to meet the legal definition of a partnership. This would cause the bank to be found to be "not perfected" on its loan. In this situation, even though the bank did everything right, based on information given it by its customer, it could lose its right to the collateral it used to make the loan.

HB 2082 merely says that "where married debtors are jointly engaged in business and it is unclear whether a partnership exists, the financing statement may be filed in the names of the individual debtors. This change only affects the filing of the financing statement. It does NOT change the legal definition of a partnership.

Thank you for your consideration and I urge your favorable action.

Senate FI&I
2/14/95
Attachment #3

Bill Graves
Secretary of State

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STATE OF KANSAS

TESTIMONY -- HB 2082
Financial Institutions and Insurance
Office of the Secretary of State
February 14, 1995

My name is Janet Chubb, Assistant Secretary of State. With me today is Carol Beard, Deputy Assistant Secretary of State, Uniform Commercial Code Division. Carol has supervised the day-to-day activities of the division for 20 years, and she is prepared to provide further detail to the committee if it would be helpful.

The proposed amendment does not affect the Secretary of State's office. It would not require procedural changes or increase costs.

HB 2082 amends K.S.A. 84-9-402 by clarifying the requirements of partnerships and sole proprietors. The Secretary of State's office cross-indexes debtor names on all financing statements, except officers of corporations. However, debtor names are not entered by status -- e.g. sole proprietor, partnership, corporation or individual. When it is unknown whether a partnership exists, the individual's name may be entered as the debtor on a financing statement. With this amendment, if the debtor files as a sole proprietor and provides an SSN, the interest of the creditor (bank) would be perfected in the event of a subsequent bankruptcy and a legal determination that a partnership exists.

The second part of the amendment to HB 2082 (Sec. 1, (9)), merely rewords the present statute. The amendment requires no procedural change for our office.

The Secretary of State supports HB 2082. Thank you.

Senate 7141
2/14/95
Attachment #4