

Approved: February 1, 1996  
Date

MINUTES OF THE HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE.

The meeting was called to order by Chairperson Bill Bryant at 3:30 p.m. on January 29, 1996 in Room 527S-of the Capitol.

All members were present except: Representative Delbert Crabb  
Representative Tom Sawyer  
Representative Phill Kline  
Representative Clyde Graeber

Committee staff present: Bill Wolff, Legislative Research Department  
Bruce Kinzie, Revisor of Statutes  
Nikki Feuerborn, Committee Secretary

Conferees appearing before the committee: Dave Hanson, Kansas Association of Property & Casualty Ins.  
Robert Woodard, Farm Bureau  
Tom Wilder, Kansas Insurance Department

Others attending: See attached list

**Hearing on HB 2713 - Property and casualty companies clearing corporations**

Dave Hanson, Kansas Association of Property and Casualty Insurers, explained that the bill is parallel in its request for revisions that were passed last year regarding investments for life insurance companies (Attachment 1). This would allow property and casualty companies to clear through and register securities with international clearing corporations rather than using only domestic clearing corporations. This request is due to the current globalization of financial markets and the increase in cross-border investment activity. This will not expand the types of securities in which property and casualty insurers are authorized to invest. Fourteen states have taken specific steps to authorize the use of international clearing corporations.

Rob Woodard, Kansas Farm Bureau Service, also emphasized the need to use international clearing corporations due to international financial markets and the increase in cross-border investment activity (Attachment 2). These clearing corporations operate in the same manner as domestic clearing corporations with the only difference being the clearing and registering of internationally traded securities issued by foreign as well as United States entities. The largest clearing system is Euroclear which uses book entry via computer operations rather than physical form (hard copy). A property /casualty insurer can invest no more than 5% of its admitted assets in obligations of foreign governments, other than obligations of Canada.

Tom Wilder, Kansas Insurance Department, voiced support of the bill as it was thoroughly explored last year when life insurance companies were granted approval to use international clearing corporations (Attachment 3)

**Action on HB 2713 - Property and casualty companies clearing corporations**

Representative Cox moved that the bill be passed out favorably. Motion was seconded by Representative Correll. Motion carried.

**Hearing on HB 2717 - Property and casualty companies investments, financial futures contracts**

Dave Hanson, Kansas Association of Property and Casualty Insurers, stated that the bill would give his clients more flexibility by providing additional types of financial instruments while at the same time creating additional safeguards (Attachment 4). Domestic property and casualty insurance companies would be allowed to invest in financial instruments which provide hedging transactions and certain income generation transactions. The insurance companies could invest in financial futures contracts which are instruments less sensitive to interest rate increases or decreases. There would be a limit the insurance companies would be allowed to invest in these types of investments. The Commissioner of Insurance would oversee the appropriateness of such investments.

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE,  
Room 527S-Statehouse, at 3:30 a.m. on January 29, 1996.

Rob Woodard, Kansas Farm Bureau Service of Manhattan, stated that this bill would be in coordination with the proposed language being drafted for the Model Investment Code by the National Association of Insurance Commissioners (Attachment 5). Specialized investment managers would be required for the implementation of such investment purchasing.

Tom Wilder, Kansas Insurance Department, reiterated the development and history of the bill (Attachment 6). He reviewed the protection built into the bill and reminded the Committee that the Insurance Department is required by this legislation to monitor these investments as part of their financial surveillance of insurance companies.

**Action on HB 2717 - Property and casualty companies**

Representative Donovan moved that the bill be passed out favorably. The motion was seconded by Representative Landwehr. Motion carried.

Representative Ruby Gilbert moved for the approval of the minutes of January 24, 1996. Representative Samuelson seconded the motion. Motion carried.

The meeting was adjourned at 4:02 p.m. The next meeting is scheduled for January 30, 1996.

# HOUSE FINANCIAL INSTITUTIONS AND INSURANCE COMMITTEE GUEST LIST

DATE: 1/29/96

NAME	REPRESENTING
David Hanson	Ks Assoc P & C Cos
Rob Woodard	Ks Farm Bureau
Whitney Danner	KS Bar Assn.
Bill Sneed	State Farm
Lee WRIGHT	Farmers Ins. Group
Tom Wilby	Kansas Insurance Dept
Lori Callahan	Kammco

Testimony to the House Committee on Financial Institutions and Insurance

January 29, 1996

Subject: HB #2713

Mr. Chairman, Members of the Committee: My name is David Hanson and I am appearing on behalf of the Kansas Association of Property and Casualty Insurers. The Association is made up of Kansas domestic insurers who's business primarily focuses on property and casualty type coverages, such as homeowners' and automobile policies.

The Association expresses its full support of HB 2713. These bills parallel revisions the legislature made last session regarding investments by life insurance companies.

Briefly, HB 2713 amends K.S.A. 40-2a20 and K.S.A. 84-8-108 to allow property and casualty companies to clear through and register securities with international clearing corporations. Under current Kansas law, insurers, other than life companies, can only use certain domestic clearing corporations. International clearing corporations are not authorized. As this matter was discussed last session, it is our understanding the reason international clearing corporations were not included was simply a result of not being contemplated, rather than a determination of being risky or unsafe. Due to the current globalization of financial markets and the increase in cross-border investment activity, authorization to use international clearing corporations is crucial.

Traditionally, when an investor purchased a security, the investor received a physical certificate evidencing ownership. Today's, securities are often not held in this physical certificate form. Trades are effected by way of book entry. That is, a security is registered in an owner's name in the records of the clearing corporation. If sold, upon receipt of the purchase price, the clearing corporation re-registers the security in the purchaser's name. International clearing corporations operate in the same manner as domestic clearing corporations. The difference is that international clearing corporations are used to clear and register internationally traded securities issued by foreign and United States entities.

The number of entities that issue securities through international clearing corporations continue to increase. The reason being, the international market offers an opportunity to maximize the number of potential investors and to maximize yield. For example, a United States corporation may choose to issue debt securities in the global market because foreign investors

*David Hanson*  
*Attachment 1*

*1-29-96*

may be willing to receive a lower rate of interest in exchange for payments made in US currency.

Let me point out, HB 2713 relates only to the registration and clearing of securities. It does not expand the types of securities in which property and casualty insurers are authorized to invest. The existing limitations on investments in foreign securities remain unchanged.

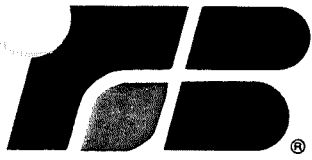
As of last year, fourteen (14) states had taken specific steps to authorize the use of international clearing corporations. We hope that the Kansas Legislature this session will extend the same opportunity to property and casualty insurers it did for life insurance companies last session. As I mentioned earlier, the language used in HB 2713 is parallel to the revisions made last session to K.S.A. 40-2b20 involving life insurers.

Again , we appreciate the Committee giving us the opportunity to present testimony as proponents of HB 2713. We feel that the proposal provides domestic property casualty insurers more opportunities and greater flexibility in making investment decisions. This added flexibility ultimately provides better security by allowing companies to more easily adjust to an ever changing financial climate. Thank you again and we respectfully request your favorable treatment of HB 2713.

Respectfully,

DAVID A. HANSON

DWM/MISCDOCS/LEG96PC.TMY



**Farm Bureau Mutual Insurance Company, Inc.**  
**KFB Insurance Company, Inc.**

January 29, 1996

RE: House Bill 2713 - International Clearing Corporations

Dear Chairman and Committee Members:

My name is Rob Woodard and I work in the investment department for Kansas Farm Bureau Services, an affiliate of The Kansas Farm Bureau. The Kansas Farm Bureau is a diversified agricultural organization offering life and property/casualty insurance through its affiliates and subsidiaries. We support House Bill 2713.

House Bill 2713 is identical in content to a bill introduced and passed as amended last year on behalf of life insurance companies. That bill (HB No. 2212) allowed, under restriction, life insurance companies in Kansas to clear through and register securities with international clearing corporations. We seek today to have the comparable property casualty statute amended.

Under current law, property casualty insurers in Kansas can use certain domestic clearing corporations. International clearing corporations are not authorized. We are not aware of a determination being made that international clearing corporations are unsafe or risky. We believe that international clearing corporations simply were not contemplated. Due to the globalization of financial markets and the increase in cross-border investment activity, authorization to use international clearing corporations is crucial.

Traditionally, when an investor purchased a security, the investor received a physical certificate evidencing ownership. Now, securities are seldom held in physical form. Trades are effected through book entry. A security is registered in an owner's name in the records of a clearing corporation. If it is sold, upon receipt of the purchase price, the clearing corporation re-registers the security in the purchaser's name.

International clearing corporations operate in the same manner as domestic clearing corporations. The difference is that international clearing corporations

*David F. D.*  
*Attachment 2*  
*1-29-96*

are used to clear and register internationally traded securities issued by foreign and United States entities.

The world's largest international clearing system is Euroclear. Euroclear is used by approximately 3,000 banks, brokers and other securities institutions that are active in the international market. Euroclear is used for settlement of over 54,000 debt and equity securities, including securities of foreign and United States entities.

Euroclear is a safe and reliable system. Book entry settlement is much safer than physical form because it eliminates the risk of physical loss or damage. However, since trades are effected by computer entry, computer system security safeguards and disaster relief programs have been implemented. Likewise, procedures for validation of trade instructions have been developed.

The Euroclear system is operated by Morgan Guaranty Trust Company of New York, Brussels office. Morgan Guaranty Trust is fully regulated by the U.S. Federal Reserve Board and State of New York Banking Department. Finally, if Euroclear were declared insolvent, securities registered with Euroclear would not become a part of the Morgan Guaranty Trust's estate.

Euroclear has been in operation for over 25 years. Daily securities and cash transactions average \$66 billion. In 1993, \$17 trillion dollars of securities cleared through Euroclear. On average, Euroclear processes 40,000 transactions every day. Recent statistics reveal securities valuing approximately \$1.5 trillion were held by Euroclear.

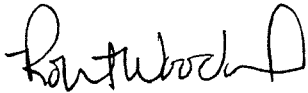
The number of entities that issue securities through international clearing corporations continues to increase. Issuers of securities choose the international market to maximize the number of potential investors and to maximize yield. For example, a United States corporation may choose to issue debt securities in the global market because foreign investors may be willing to receive a lower rate of interest in exchange for payments made in United States dollars.

This bill relates to the registration and clearing of securities only. It does not expand the type of securities in which property/casualty issuers are authorized to invest. The existing limitations on investments in foreign securities remain unchanged. A property/casualty insurer can invest no more than 5% of its admitted assets in obligations of foreign governments, other than obligations of Canada. Investments in obligations of foreign companies are not specifically authorized. However, such investments may be made under the "leeway clause," and consequently cannot in the aggregate exceed 10% of an insurer's admitted assets.

Other states have reacted to the continued trend towards globalization of financial markets. Our research indicates that fourteen states have taken specific steps to authorize the use of international clearing corporations. We hope that Kansas will join these states by adopting House Bill 2713.

Thank you for your time and consideration. I would be happy to address any questions you have.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Robert Woodard". The signature is fluid and cursive, with a large initial "R" and "W".

Robert Woodard, CFA  
Portfolio Manager  
Farm Bureau Mutual Insurance Co., Inc.





Kathleen Sebelius  
Commissioner of Insurance  
**Kansas Insurance Department**

**MEMORANDUM**

To: House Financial Institutions and  
Insurance Committee

From: Tom Wilder, Director of Government  
and Public Affairs

Re: H.B. 2713 (Clearing Corporations)

Date: January 29, 1996

House Bill 2713 allows property and casualty insurance companies to hold securities in "clearing corporations" which are located outside of the United States. A clearing corporation is an organization which holds and trades securities for other companies. The current statute allows these insurers to hold securities in United States clearing corporations which are regulated by the Federal Reserve System or the state banking commissioner.

As you are aware, the Kansas Legislature approved amendments to K.S.A. 40-2b20 to allow life insurance companies to use foreign clearing corporations. It is appropriate to extend this investment authority to other types of insurers. The clearing corporations would have to be operated or owned by a bank, trust company or other business entity that is subject to regulation by the United States Comptroller of the Currency, Federal Reserve Board or Securities and Exchange Commission.

The Kansas Department of Insurance supports the changes outlined in H.B. 2713 and requests the Committee recommend the legislation favorably for passage.

*House F&I  
Attachment 3  
1-29-96*

Testimony to the House Committee on Financial Institutions and Insurance

January 29, 1996

Subject: HB # 2717

Mr. Chairman, Members of the Committee: My name is David Hanson and I am appearing on behalf of the Kansas Association of Property and Casualty Insurers. The Association is made up of Kansas domestic insurers who's business primarily focuses on property and casualty type coverages, such as homeowners' and automobile policies.

The Association expresses its full support of HB 2717. The language of HB 2717 is parallel to the revisions made last session to K.S.A. 40-2b25 relating to life insurance companies. It is our understanding that the language used in the revised K.S.A. 40-2b25, with the exception of some added safeguards suggested by the Kansas Insurance Department, came from language developed by the National Association of Insurance Commissioners ("NAIC") Model Investment Code on the particular subject.

HB 2717 gives domestic property and casualty insurers greater investment flexibility by providing additional types of financial instruments, while at the same time creating additional safeguards. K.S.A. 40-2a24 currently allows insurance companies to invest in financial futures contracts as part of a hedging transaction ties to a specific asset or group assets. HB 2717 would permit property and casualty insurance companies to invest in additional types of financial futures contracts. This bill will allow domestic property and casualty insurance companies to invest, subject to review by the Kansas Insurance Department and statutory restrictions, in financial instruments which provide hedging transactions and certain income generation transactions. In essence, this bill allows an insurance company to invest in financial futures contracts which provide somewhat of a shield from interest rate volatility. That is, financial instruments which are less sensitive to interest rate increases or decreases. Because of the highly technical nature these types of securities, the bill requires that the insurance company be able to demonstrate to the Commissioner of Insurance the intended characteristics of the financial instrument, along with the ongoing effectiveness of the investment. Additionally, the bill limits the amount a domestic insurance company may invest of its portfolio in these types of investments. As I noted earlier, under last years revisions, life insurance companies currently have access to these types of financial instruments and the provisions seem to be working well.

*David Hanson*  
*Attachment 4*

*1-29-96*

The property and casualty companies are merely requesting similar access.

Again , we appreciate the Committee giving us the opportunity to present testimony as proponents of HB 2717. We feel that the proposal provides domestic property casualty insurers more opportunities and greater flexibility in making investment decisions. This added flexibility ultimately provides better security by allowing companies to more easily adjust to an ever changing financial climate. Thank you again and we respectfully request your favorable treatment of HB 2717.

Respectfully,

DAVID A. HANSON

DWM/MISCDOCS/LEG96PC2.TMY



**Farm Bureau Mutual Insurance Company, Inc.**

**KFB Insurance Company, Inc.**

January 29, 1996

RE: House Bill 2717 - Financial Hedging Transactions

Dear Chairman and Committee Members:

My name is Rob Woodard and I work in the investment department for Kansas Farm Bureau Services, an affiliate of The Kansas Farm Bureau. The Kansas Farm Bureau is a diversified agricultural organization offering life and property/casualty insurance through its affiliates and subsidiaries. We support House Bill 2717.

House Bill 2717 is identical in content to a Senate Bill introduced and passed (as amended) last year on behalf of life insurance companies. That bill (SB 345) replaced the existing statute regarding the use of financial instruments to engage in hedging transactions and certain income generation transactions. We seek today to have the comparable property casualty statute amended.

H.B. 2717 would amend K.S.A. 40-2a24 concerning the authorized investments of "other than life" insurance companies. The bill would strike all the existing language and incorporate language developed by the National Association of Insurance Commissioners and agreed to but not yet formally presented as part of a redraft of its Model Investment Code.

Any Kansas Insurance company (other than life) would be allowed to use designated financial instruments to engage in hedging transactions and certain income generation transactions. To do so, the company must be able to demonstrate to the Insurance Commissioner the intended hedging characteristics and the effectiveness of the financial instrument transaction or combination of transactions through cash flow testing or other appropriate analysis.

"Financial instrument" would be defined as an agreement, option, instrument, or any series or combination thereof; to make or take delivery of, or assume or relinquish, a specified amount of one or more underlying interests, or to make a

*Rob Woodard*  
*Attachment 5*  
*1-29-96*

cash settlement in lieu thereof; or which has a price, performance, value or cash flow based primarily upon the actual or expected price, level, performance, value or cash flow of one or more underlying interests. "Underlying interest" would be defined as the assets, other interests, or a combination underlying a financial instrument, such as any one or more securities, currencies, rates, indices, commodities, or financial instruments.

"Financial instruments" would be further defined to include options, warrants, caps, floors, collars, swaps, forwards, future, and any other substantially similar agreements, options, or instruments, or any series or combination of instruments. (Most of the instruments listed are defined individually in the bill.)

Investing in these types of securities takes a specialized investment manager. To that end, the statute requires that the insurance company must be able to demonstrate to the Commissioner of Insurance the intended characteristics of the financial instrument, along with the ongoing effectiveness of the investment. Additionally, subsection (c) of the bill limits the amount of the portfolio that a domestic insurance company may invest in these types of investments. Thus, you will have an ongoing review by the Insurance Department of these investments prior to and during the course of holding the investments, along with the overall cap as provided.

Thank you for your time and consideration. I would be happy to address any questions you have.

Respectfully submitted,



Robert Woodard, CFA  
Portfolio Manager  
Farm Bureau Mutual Insurance Co., Inc.



Kathleen Sebelius  
Commissioner of Insurance  
**Kansas Insurance Department**

**MEMORANDUM**

To: House Financial Institutions and  
Insurance Committee

From: Tom Wilder, Director of Government  
and Public Affairs

Re: H.B. 2717 (Investments in Financial Futures)

Date: January 29, 1996

The Kansas Insurance Department supports House Bill 2717 which amends K.S.A. 40-2a24 to give property and casualty insurers additional authority to invest in financial futures contracts. The amendments to the statute are taken from the National Association of Insurance Commissioners Model Investment Code. Although the NAIC is still in the process of developing the model act, the provisions pertaining to futures contracts have been approved. The Kansas Legislature gave similar authority to life insurance companies last year in 1995 S.B. 345. It is appropriate to also provide this investment flexibility to other insurers.

Financial futures contracts are investments which require intelligent financial management by the insurance company. There are limits placed on the investment in such instruments under Subsection (14) of the statute. In addition, the Insurance Department is required to monitor these investments as part of our financial surveillance of insurance companies.

The Insurance Department asks the Committee to approve H.B. 2717.

*James F. D. D.*  
*Attachment 6*

*1-29-96*