Approved:________________________
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 March 11, 1996 in Room 527S-of the Capitol.

All members were present except: Representative Tom Sawyer, Representative Phill Kline, Representative Delbert Crabb, Representative Carol Dawson

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

Conferees appearing before the committee: Kathleen Sebelius, Insurance Commissioner
Tessa Johnson, Topeka Independent Living Resource Center
Newton Male, State Bank Commissioner
Chuck Stones, Kansas Bankers Association

David Hanson, Kansas Life Insurance Association, provided written testimony to Committee members addressing the problem of including life insurance in the provisions of **Sub SB 529** (Attachment 1).

Hearing on SB 441: Uninsurable health care insurance plan, rate, cap, tax credits

Commissioner Sebelius gave the history of the plan which offers health insurance to consumers who are unable to obtain coverage on the private market and the criteria for becoming one of its 786 participants (Attachment 2). Benefit schedules were included with the testimony. The bill changes the statutes governing the operations of the Kansas Health Insurance Association by providing that premiums charged to participants in the plan can be no more than 150% of premiums charged for similar coverage through private market health insurance. The bill moves up the startup date for health insurance companies and health maintenance organizations to start receiving their 80% tax credits against their premium or privilege taxes to tax year 1996. The premium tax is 1% for the domestic companies and 2% for foreign companies. Thus far $90 million has been contributed to the plan from industry taxes. ERISA plans are exempted from this tax.

Commissioner Sebelius suggested that an amendment forgiving the $2.0 million startup loan from the Pooled Money Investment Board be added to the bill. The two ways to defray this outstanding loan would be by raising the premiums or by forgiving it. There is currently a $1.35 million debit in the program.

Tessa Johnson, Topeka Independent Living Resource Center, spoke in support of the bill (Attachment 3).

Hearing on SB 666: Revising limitations on loans and borrowing in which banks are involved

Newton Male, State Bank Commissioner, explained to the Committee how the plan revision developed by a task force would allow new provisions for: increasing the lending limit to one borrower from 15 percent to 25 percent of the bank's capital; creates lending limit equity between agricultural banks and nonagricultural banks by removing he additional 10 percent allowable to a borrower whose loan was secured by livestock, seed or grain; establishes the lending limit applicable to a loan as the limit in effect on the date the loan was made; exempts from the limit those loans secured by specified types of collateral, including repurchase agreement; and allows for an additional 10 percent increase in the limit if the collateral is a first lien on real estate (Attachment 4) Mr. Male requested the addition of two amendments to the bill (see attachment). The first would allow a bank to expand the amount they can loan one borrower by an additional ten percent if certain criteria are met . The second amendment was clarifying and technical in nature.

Chuck Stones, Kansas Bankers Association, read prepared testimony by Kathy Taylor supporting the bill (Attachment 5). The bill would bring clarity to the lending limit rules and help keep Kansas banks competitive with other lenders in the market.

Representative Landwehr moved for the approval of the minutes of March 4. Motion was seconded by Representative Cox. Motion carried.

The meeting was adjourned at 5:00 p.m. The next meeting is scheduled for March 12, 1996.

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

HOUSE FINANCIAL INSTITUTIONS AND INSURANCE COMMITTEE GUEST LIST

DATE: March 11, 1996

NAME	REPRESENTING
Tom Wilder	Kansas Ins. Dept
W. Newton Male	Ks. Banking Dept.
John Holmgren	BD MEMBER Ks Health Ins Bd
Sharon L. Male	
Stan Slater	KHIA / KALU
Kirk Hunchker	Ks. Ins Dept.
[illegible] Porsch	Lt. Gov.
Melissa Wangemann	Hon Elvetta Weir
Valerie Peterson	Life Association
Bryan Miller	BCBSKC / KHIA
Don Lynn	BCBS of Ks.
Carol Dross, Tara Johnson, Susan Briggs	TILRC
Kevin Davis	Am. Family
Bill Sneed	NIAA
Danielle Noe	KCUA
Roger Franzke	FCC
David Hanson	Ks Insur Assoc

House Financial Institutions and
Insurance Committee
State Capital Building
Topeka, KS

Re: Substitute for Senate Bill 529

Chairman Bryant and Members of the Committee:

I am David Hanson appearing on behalf of the Kansas Life Insurance Association, an Association of domestic life insurance companies here in Kansas. We appreciate the opportunity to address several concerns we have with any amendment to include life insurance in the provisions of Substitute Senate Bill 529. As I indicated at the Committee hearing last week, we support the bill in its present form relating to long-term care insurance. However, we would have serious concerns with amending the bill to also apply to life insurance. We do not believe these provision will work for life insurance, nor for other types of insurance.

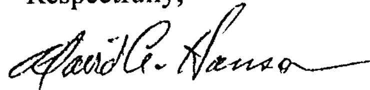
We are concerned that amending the provisions of the bill may create additional problems for life insurance companies and their insureds. Specifically, the bill provides for reinstatement of a policy if there is a default in premium payments caused by cognitive impairment or the loss of functional capacity. We are concerned this may have unintended consequences in life insurance where the insured is not always the same person as the policy owner, since it is the policy owner who may fail to pay the premiums. We are also concerned that the reference to cognitive impairment or loss of functional capacity is somewhat vague and indefinite for life insurance.

We are also concerned that the notification provisions set forth in sections 2(d) and 4 will be extremely difficult to comply with since the required notice applies to certain policies issued to residents of this state even if they subsequently move to other states, thus creating a serious tracking problem. Also, life insurance would have an extremely difficult problem in trying to notify a designated additional person for a lapsed or terminated policy, since our systems programming is not equipped to do this and this additional notice would require a major revision to the systems of all life insurance companies, foreign and domestic, to try to comply with this unique requirement in Kansas. Attached is a copy of the statement submitted by the American Council of Life Insurance with over 400 members licensed in Kansas addressing some of these same concerns to the original version of Senate Bill 529. As indicated, there would also be some concern with the potential for abuse connected with life insurance where there could be substantially more to gain from trying to reinstate a policy, especially after adverse conditions may have developed.

We believe the protections of Substitute for Senate Bill 529 are specifically suited to long-term care insurance, but not other types of insurance.

We appreciate your consideration of these concerns and urge your favorable consideration of Substitute for Senate Bill 529 in its present form without any amendment to include life insurance.

Respectfully,



DAVID A. HANSON

DAH:kls

sec'y/robin/letters/bill529.311

House FI&I
Attachment 1
March 11, 1996

Received: 2/ 8/96; 8:37AM; 2026242319 => GLENN, CORNISH, HANO; #2
FEB-08-1996 10:40 FROM AM COUNCIL OF LIFE INS TO 919132320005 P.02

American Council of Life Insurance

STATEMENT
OF
THE AMERICAN COUNCIL OF LIFE INSURANCE

SENATE BILL 529

Chairman Bond and Members of the Committee:

Thank you for the opportunity to comment on Senate Bill 529.

The American Council of Life Insurance is a trade association whose nearly 600 member companies hold 90% of the life insurance in force in America today. We have over 400 member companies licensed in Kansas.

Senate Bill 529 is troublesome from a public policy standpoint in that it singles out a particular class of person and grants them favorable treatment over others. The bill would require life and long-term care insurers to reinstate policies that have lapsed for non-payment of premiums for up to a year after the lapse if the insured could show that the failure to pay premiums was due to his or her "mental incapacity" at the time of the failure to pay.

It is, of course, unfortunate that a person would suffer from mental incapacity and as a result fail to pay their life or long-term care insurance premiums. It is not unreasonable to suggest, however, that the same mental incapacity might also cause them to fail to pay other financial obligations. Indeed, there are a variety of medical or financial circumstances that befall individuals which result in their failure to make payments on all kinds of contracts. Despite this, Senate Bill 529 would single out for special treatment only those individuals who fail to make payments as a result of mental incapacity and only the payments they fail to make on life insurance and long-term care contracts. While we have great sympathy for individuals who suffer a mental incapacity we believe singling them out for special treatment in this particular circumstance is not constructive public policy.

We further believe that there is great potential for fraudulent abuse of the protections proposed by the bill. An individual, with an entire year to act, could let his policy lapse for a variety of reasons, discover during that year the need for the policy's protection and with only a note from an accommodating physician gain reinstatement. The increased anti-selection risk posed to insurers by the bill is significant. A person not otherwise entitled to reinstatement would only need claim "mental incapacity" and the insurer would be obligated to reinstate.

Most life insurance policies (many of which include a provision for acceleration of benefits for long-term care) include a provision which allows the policy owner to reinstate a lapsed policy,

1001 PENNSYLVANIA AVENUE, N.W.
WASHINGTON, D.C. 20004-2599
202/624-2000
FACSIMILE 202/624-2319

generally within three years from the policy lapse. Because of the potential for anti-selection, the policy owner must provide satisfactory evidence of insurability, as well as pay any past due premiums or loans. This is an especially important protection for the life insurer whose policy death benefits can create incentive for fraud. Mandating reinstatement without any evidence of insurability, after a year has passed, opens both life and long-term care insurers to a significantly greater fraud and anti-selection risk.

Having expressed our policy concerns over Senate Bill 529 generally, we also have specific comments regarding the language and terms used in the bill:

Page 1, lines 15 and 16:

The requirements would apply to "...policies issued to residents of this state...". We would suggest that it is immaterial whether the person in question was a resident of the state when the policy was issued. The issue is whether they are a resident of the state when the policy lapses. Under the current language, a Kansas resident who buys a policy then moves out of state and lapses would be covered by the bill. On the other hand, a policy issued to a non- resident of the state who then moves to Kansas would not be covered. Some language to make the bill apply to Kansas residents whose covered policies lapse should be considered.

Page 1, line 31:

The mental incapacity of the "insured" is not the issue. It would be the mental incapacity of the policy owner that would likely cause the lapse in payments. While in many instances the policy owner and the insured might be the same person, in other circumstances they are different individuals. In cases where they are not the same person, it is the policy owner who pays the premiums. Focusing on the mental incapacity of the policy owner, not the insured, is the correct procedure. We would therefore suggest deleting the word "insured" and inserting the term "policy owner" in line 31. We would also submit this line of reasoning applies to subsequent references to the "insured" and would therefore suggest "insured" be replaced with the term "policy owner" where appropriate.

Page 1, line 32:

The one year time period is far too long. The National Association of Insurance Commissioners (NAIC) Long-Term Care Model Regulation sets a reinstatement period of five months. No time requirement is imposed on life insurance policies other than those covered by the Model LTC Regulation because they provide long-term care through acceleration of benefits. We strongly urge a shorter time period (certainly no greater than five months). If insurers are to be forced to reinstate a policy without being provided any evidence of insurability, a year's time is far large a

window and places insurers at considerable risk. Indeed, insurers are expected to minimize risk by adhering to prudent underwriting practices based on sound actuarial principles. Senate Bill 529's requirement of reinstatement, without evidence of insurability, for up to a year seriously affects an insurer's ability to protect its other policy holders by increasing the insurer's risk.

Page 1, lines 36 - 40:

The definition of "mental incapacity" appears open to wide interpretation depending on a number of factors including the physician and individual involved. We submit this definition is overly broad and quite general. Further, Kansas already has statutory definitions at K.S.A. 59-2902 regarding persons who are mentally ill and lacking in capacity. Making judgements regarding an individual's mental condition can be an inexact science. Adding an additional level of definition for mental incapacity blurs the area further.

In addition, since under the bill the an individual would have up to a year from lapse to assert that at the time of the lapse they were suffering from a "mental incapacity" which caused the lapse, it would be possible that both the physician involved and the insurer would be dealing with a condition which occurred up to a year in the past but which was no longer present. Those in the present are asked to rely on representations regarding an individual's mental state at a specific time in the past. Again, the opportunity for fraud against an insurer is significant. Given the span of time involved and the definition offered, we believe the definition of "mental incapacity" to be inadequate.

Page 1, lines 41-42:

The current language requiring the diagnosis be rendered by a "...physician licensed in this state and qualified to make the diagnosis" requires tightening. We submit that the only physician qualified to make a "clinical diagnosis" regarding a person's mental capacity or condition, particularly if the diagnosis is being rendered about a condition which may have occurred up to a year in the past, is a board certified psychiatrist licensed in Kansas. We suggest the requirement be changed accordingly.

We further request that the insurer have be allowed to require the individual submitting a claim of mental incapacity submit to an independent medical (specifically, psychiatric) examination to protect the insurer against fraud.

Page 2, lines 2-5:

The term "insured" should be replaced with "policy owner" for the reasons described above.

Page 2, lines 10-11:

As stated above, reinstatement under these conditions with no requirement of evidence of insurability poses too great a risk to insurers. The requirement for reinstatement under these circumstances should not be enacted. But if it is to be made law, evidence of insurability should be provided to the insurer. The term "without" should be replaced with the word "with." In the alternative, as stated above, the insurer should at a minimum be allowed to require the person asserting mental incapacity to submit to examination by an independent board certified psychiatrist to protect against fraud.

Page 2, lines 23-25:

Allowing the insurer to decline reinstatement if the mental incapacity occurred after applicable grace periods offers no protection to the insurer. Under the terms of this bill a person is seeking to show incapacity prior to the expiration of the grace period. Most insurers send notice of lapse during the grace periods mentioned. They do this to try to conserve the business and keep the policy in force. Once the grace period has expired, the condition of the insured/policy owner becomes immaterial. This provision of the bill states the obvious. The issue created by Senate bill 529 involves determining, up to a year after the fact, the mental state of the insured/policy owner prior to the expiration of the grace period.

Page 2, lines 26-36:

The disclosure provisions of the bill add additional and impractical requirements. Kansas would be only the second state in the country to pass such a law and impose such requirements. This means insurers would be required to "flag" all Kansas policies subject to the law and create a separate system for handling them when a lapse occurs. As stated above, most insurers send notice of lapse to policyholders in an attempt to conserve the business. The policy provisions regarding reinstatement and grace periods are already covered by K.S.A. 40-2203. Requiring an additional disclosure within 90 days of lapse on all existing policies covered by the bill would pose tremendous compliance difficulties for any insurer with a significant number of policies in force in the state.

Page 2, lines 41-42:

If the bill already spells out who is to receive the disclosure (lines 26-36), how many days the insurer has to send the disclosure (lines 26-36) and what type of notice constitutes compliance with the act (lines 37-39), it would seem there is little left for the insurance commissioner to decide regarding "the form and manner" of disclosure. We suggest relieving the insurance commissioner of this additional duty and deleting lines 41-42.

Kathleen Sebelius
Commissioner of Insurance
Kansas Insurance Department

MEMORANDUM

To: House Financial Institutions
and Insurance Committee

From: Kathleen Sebelius, Commissioner
of Insurance

Re: S.B. 441 (Kansas Uninsurable Health Insurance Plan)

Date: March 11, 1996

The Kansas Department of Insurance supports Senate Bill 441 which amends the provisions of the Kansas Uninsurable Health Insurance Plan Act. The legislation was introduced by the Health Care Reform Legislative Oversight Committee at the request of the Kansas Insurance Department. This law was established by the Kansas Legislature in 1992 to provide health insurance options to consumers who are unable to obtain coverage on the private market. The Kansas Health Insurance Association ("KHIA") first started providing health insurance in May, 1993 and 786 Kansans are currently insured through the plan. The KHIA is similar to health plans offered in twenty-eight states.

In order to be eligible for participation in the plan, an applicant must have resided in Kansas for six months and either have been involuntarily terminated by a health insurer for any reason other than the failure to pay premiums or have been refused coverage by two insurance companies due to health conditions. The KHIA offers a "High Option" and "Low Option" coverage plan. The High Option plan provides greater benefits to the policyholder. A chart which shows the benefit schedule for the two plans is attached to my testimony along with information on the current premium structure for the two plans. It is important to note that these plans offer only very basic health insurance coverage and have high deductible amounts together with a lifetime cap on benefits.

House FI&I
Attachment 2
March 11, 1996

420 SW 9th Street
Topeka, Kansas 66612-1678

913 296-3071
Fax 913 296-2283

Consumer Assistance Hotline
1 800 432-2484 (Toll Free)

Printed on Recycled Paper

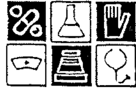
There are three sources of funding for the Kansas Health Insurance Association. In order to provide start-up funding for the KHIA, the Kansas Legislature approved a $2.0 million loan to the plan from the Pooled Money Investment Board. These funds are a non-interest bearing loan which must be repaid by the KHIA within 10 years. The fund also receives premium income from the plan participants. In 1995 the plan took in $1.1 million in premiums from its members. Finally, the KHIA is authorized to assess the health insurance companies and health maintenance organizations which do business in Kansas in order to make up any shortfall between the anticipated losses of the plan and premium income. In 1995 the Governing Board of the KHIA approved an assessment of $500,000 from health insurers and health maintenance organizations.

Senate Bill 441 makes two changes to the statutes governing the operations of the Kansas Health Insurance Association. The bill provides that premiums charged to participants in the plan can be no more than 150% of premiums charged for similar coverage through private market health insurance. The bill also makes a change in the tax credit given to health insurance companies and health maintenance organizations which are assessed by the KHIA. Under the current statute, the companies are allowed a 80% credit against their premium or privilege taxes, however, this credit is not authorized for assessments made during the first four years of operation of the plan. Senate Bill 411 states the 80% tax credit will be available for assessments made during tax years after December 31, 1995. In effect, the start date of the tax credits is moved up one year from tax year 1997 to tax year 1996.

The Kansas Insurance Department suggests one additional change should be made to the Kansas Uninsurable Health Insurance Plan Act. The KHIA was initially funded by a $2.0 million loan from the Pooled Money Investment Board. As noted, this loan must be paid back by the KHIA prior to 2003. The loan is carried by the plan as a liability which impacts the financial viability of the Kansas Health Insurance Association. This Committee should consider an amendment to K.S.A. 40-2125 which would forgive the loan made to the KHIA.

The Kansas Health Insurance Association has provided valuable assistance to those Kansas consumers who otherwise would not be able to afford health insurance. I

believe the Kansas Legislature should seriously consider how the fiscal integrity of the KHIA can be maintained in the future in a manner which assures the participants in the association will continue to have health insurance coverage at a price which is within their reach. I urge this Committee to approve S.B. 441. I also ask the Committee to amend the bill to forgive the $2.0 million start-up loan made to the Kansas Health Insurance Association by the Pooled Money Investment Board.



LaHood & Associates, Inc.

Integrated Health Care Administration

Dear Kansas Resident:

Enclosed you will find information about health care coverage available through the Kansas Health Insurance Association (KHIA) Plan. The KHIA Plan is designed for Kansans who:

- have had health insurance involuntarily terminated for reasons other than non-payment of premium.
- have been rejected for health care coverage by at least two insurance carriers.
- are being charged more than 150 percent of this plan's standard premiums for health care coverage.
- have been accepted for health insurance coverage but are subject to a permanent exclusion of a pre-existing condition or disease.

If you are in a situation described above, please take a close look at the enclosed plan brochure and enrollment materials. There are two plans available: a High Option Plan and a Low Option Plan. Both plans cover hospital care, outpatient care, physician care and other medical services. The plans encourage you to receive care from providers in two networks – Preferred Care and CAP – by paying higher benefits when network providers are used.

KHIA Plan rates for individuals

AGE	0-18	19-29	30-39	40-49	50-59	60-64	65+
HIGH OPTION	$120.50	$161.44	$172.29	$183.64	$217.51	$259.92	$311.90
LOW OPTION	$ 71.27	$ 95.48	$101.91	$108.65	$128.65	$153.73	$184.48

The KHIA Plan is designed for individual membership only. Each family member interested in this coverage must apply for his or her own coverage.

If you wish to apply for the KHIA Plan, follow the "How to Apply" instructions in the brochure. Attach all pertinent documentation as requested, and include the application, health statement and affirmation form. The affirmation form requires a witness signature in addition to your own. Be sure sure to sign and date the forms.

6717 Shawnee Mission Parkway · P.O.Box 12170 · Overland Park, Kansas 66282-2170
Kansas City Area: 1-913-362-0040 · Toll Free: 1-800-255-6065 · FAX: 1-913-362-0041

Do not send any payment at this time. You will receive notification of your acceptance or rejection within approximately 30 days of receipt of your application. Upon acceptance, you will received premium notice, policy, ID card and other information about the Plan.

The KHIA Plan is administered by LaHood & Associates. If you have any questions about the plan or the enclosed materials, please call me at (913) 362-0040 or at 1-800-255-6065.

Sincerely,

Maureen Coveney
LaHood & Associates, Inc.

MC:jd

KANSAS HEALTH INSURANCE ASSOCIATION PLAN

SCHEDULE OF BENEFITS

	LOW OPTION PLAN		HIGH OPTION PLAN	
BENEFIT CATEGORY	THE PLAN PAYS	YOU PAY	THE PLAN PAYS	YOU PAY
Overall Deductible	None of the first $5,000	The first $5,000 of eligible expenses	None of the first $1,000	The first $1,000 of eligible expenses
Coinsurance Percentage* * see note below	70% of the next $5,000 of eligible expenses: 90% thereafter	30% of the next $5,000 of eligible expenses; 10% thereafter	70% of the next $5,000 of eligible expenses; 90% thereafter	30% of the next $5,000 of eligible expenses; 10% thereafter
Out-of-Pocket Expense Amount *see note below	For eligible expenses over $10,000, the Plan pays 90%	$6,500 +10% of eligible expenses over $10,000	For eligible expenses over $6,000, the Plan pays 90%	$2,500 +10% of eligible expenses over $6,000
Annual Benefit Maximum	$50,000 for the first calendar year; $75,000 for the second calendar year; and $100,000 for each calendar year thereafter.	All eligible expenses once KHIA has paid the Annual Benefit Maximum to you in the year	$50,000 for the first calendar year; $75,000 for the second calendar year; and $100,000 for each calendar year thereafter.	All eligible expenses once KHIA has paid the Annual Benefit Maximum to you in the year
Lifetime Benefit Maximum	$500,000	All eligible expenses once KHIA has paid $500,000 in benefits to you in your lifetime	$500,000	All eligible expenses once KHIA has paid $500,000 in benefits to you in your lifetime

BENEFIT CATEGORY	SPECIAL BENEFIT LIMITS OR RESTRICTIONS	Does the deductible apply before this benefit is payable?	Does the regular coinsurance apply to this benefit?	Do your copayments help satisfy the Out of Pocket Expense Amount?
Outpatient Prescription Drugs	All prescriptions paid at 50%	Yes	No	No
Maternity Coverage (includes pre-natal and well baby care)	Same as other conditions	Yes	Yes	Yes
Mental disorders – inpatient	48 hours emergency inpatient care. Additional days of hospitalization.	Yes Yes	Yes Yes	No Copayments Yes
Substance Abuse – Inpatient	Maximum of 5 days/admission up to 15 days per lifetime.	Yes	Yes	Yes
All inpatient benefits for mental disorders and substance abuse are subject to an annual maximum benefit of the lesser of 30 inpatient days or $5,000 in benefits ($10,000 for High option). One inpatient day may be exchanged for two partial hospitalization days.				
Mental Health & Substance Abuse – Outpatient	First visit paid in full $25 copayment for visits 2-20; Maximum of 20 visits per year	Low option - No High option - Yes	No	No
Nonsurgical Spinal Treatment	Maximum of 20 visits per year Benefit limited to $20 per visit	Yes	No	No
Preventive Care Services – medically accepted Immunizations, pap smears and mammograms. (See age criteria in policy)	Low option - Not covered High option - $25 copayment per visit, maximum benefit of $250 per year			

ALL SURGERY AND HOSPITAL SERVICES (EXCEPT EMERGENCIES) NEED TO BE PRE-CERTIFIED FOR BENEFITS

***Benefits are payable at the 70% and 90% levels outside the state of Kansas only for:**

(1) Services provided by network providers.
(2) Emergency services

Other services and care from non-network providers are payable at 50% and do not contribute toward reaching the 90% benefit level.

Benefits are payable at the 70% and 90% levels within the state of Kansas as follows:

(1) For services performed in counties with no network providers.
(2) For services performed in counties with network providers only if provided by network providers.

Services performed by non-network providers in the network area are payable at 50% and do not contribute toward reaching the 90% benefit level.

KHIA BOARD OF DIRECTORS
1995

(CHAIRPERSON)
Jerry W. Cole
Cole Conultants
323 N. Market
Wichita KS 67202-2009
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ADMINISTRATOR
(NOT A BOARD MEMBER)

Maureen Coveney
LaHood and Associates
6717 W.Shawnee Mission Pkwy
Overland Park KS 66212
PHONE: 1-800-255-6065 (x-332)
FAX: 913-362-0041

Offices located in
the Historic Crawford Building

Topeka Independent Living Resource Center

(913) 233-4572 V/TDD • Fax 913-233-1561 • Toll Free 1-800-443-2207
501 SW Jackson Street • Suite 100 • Topeka, KS 66603-3300

Testimony Regarding SB 441
Tessa Johnson

My name is Tessa Johnson. I work for the Topeka Independent Living Resource Center (TILRC), a services and advocacy organization for people with all types of disabilities.

The mission of our agency is to increase consumer choice, to empower people with disabilities to run their own lives to the maximum extent feasible, and to increase the capacity of our community to integrate people with disabilities into all aspects of life including work, recreation, transportation and public accommodations.

The Topeka Independent Living Resource Center supports Senate Bill No.441. This bill will increase the capacity of the private insurance industry to meet the health care needs of people with disabilities in a more affordable manner.

Senate Bill No. 441 demonstrates a positive effort in working on health care reform for the citizens of Kansas.

Thank you.

Sincerely,

Tessa Johnson

Tessa Johnson

House FI&I
Attachment 3
March 11, 1996

STATE OF KANSAS
BILL GRAVES
GOVERNOR

W. Newton Male
Bank Commissioner

Judi M. Stork
Deputy Commissioner

Kevin C. Glendening
Assistant Deputy Commissioner

William D. Grant, Jr.
General Counsel

Ruth E. Glover
Administrative Officer

OFFICE OF THE
STATE BANK COMMISSIONER

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS AND INSURANCE

MARCH 11, 1996

Mr. Chairman and Members of the Committee:

I am W. Newton Male, Bank Commissioner, and I am here to testify in favor of Senate Bill 666. The following is a review on a section by section basis. Please stop me at any time as we go through this if you have any questions.

K.S.A. 9-1104 is commonly referred to as the lending limit statute. It establishes the amount of funds that a bank can loan to one borrower. It provides for exceptions, exemptions, and various rules. Because it is so widely used and, in the current form, so very difficult to understand, I established a task force of bankers to review the statute and recommend changes. The task force met with various members of my agency's staff and arrived at the language found in the bill before you today. We also have solicited comments from the state chartered banks we regulate and the response has been very positive, with most bankers indicating the new language is much easier to follow and understand.

Section (a), beginning on page four, line 16, sets out the definitions used throughout the statute. It defines who is included in the term"borrower", what is included in capital for calculating the limit, and what constitutes a loan.

Section (b), beginning on page four, line 38, sets forth the general lending limit rule. It says that a bank can loan up to 25% of their capital to one borrower. This section represents a change from the old law where a maximum limit of 15% to one borrower was allowed. This change is a result of requests by various banks to increase the limitation. It allows for smaller banks to compete for larger business and farm loans in the community. It also levels the playing field between ag banks and non-ag banks. In the past, agricultural banks could exceed their 15% limit by an additional 10% (up to 25%) if they had collateral of livestock, seeds or grains pledged to the loan. This additional 10% was in fact a bias against a non-ag bank. There currently is no similar exemption for non-ag collateral.

As a point of comparison, the base limitations for surrounding states are as follows:

Nebraska	25%	
Colorado	15%	
Oklahoma	20%	
Missouri	15%	in towns with population 100,000 or over
	20%	in towns with population less than 100,000 and over 7,000
	25%	in towns with population 7,000 or less

House F I & I
Attachment 4
1996

Section (c), found on page four, line 41, describes when the lending limit shall be calculated. It is determined on the date a loan or written commitment is first made to the borrower. Additionally, if the bank's capital increases, the bank can advance additional funds to the borrower and remain in compliance. If the bank's capital falls, and a commitment to loan money has already been made, the decline in capital will not prohibit the bank from honoring their commitment. This represents no material change to the way lending limits have been calculated in the past; it is merely a clarification of how the department allowed banks to calculate their lending limits.

Section (d), which begins on page five, line nine, details which loans are exempt from the application of the lending limits. Exempt from the lending limitation is that portion of the loan which is secured on a one to one basis by the following types of collateral:

Government guaranties
Time deposit accounts in the lending bank
Bonded warehouse receipts
US Government bonds
GO bonds of any state
Kansas municipality GO bonds
Repurchase agreements with the lending bank

These are the same exemptions that are in the current statute with the addition of repurchase agreements. Some obsolete or unclear exemptions, such as "produce in transit" or "the discount of commercial or business paper actually owned by the person negotiating the discount", have been deleted.

Section (e), page five, line 32, reviews the special rules. The first rule allows a bank to exceed the 25% limitation previously imposed by up to an additional 10% if the collateral securing the loan is a first lien real estate mortgage. Other requirements regarding the amount of the lien and the appraised value of the property are also spelled out in this section.

The second rule says that if an individual guarantees or endorses an obligation to the bank, the loan they guaranteed will not be added to their personal debt to determine if they are in compliance with the lending limit, as long as the guaranteed debt is not greater than ten days past due. If it is past due greater than ten days, it will be added to their personal obligations when checking compliance with the lending limit.

The third rule requires loans which are made to active bank officers to receive prior approval of the bank's board of directors, if the officer's debt will exceed $50,000.

The fourth rule allows a bank to purchase a time deposit from another bank, without that "purchase" being considered a loan to the other financial institution and therefore subject to the lending limit of the purchasing bank, to the extent the deposit is insured by the FDIC.

The fifth rule relates to the purchase of third party paper. An example would best clarify this rule. The bank has as a customer an auto dealer, ABC Auto World, and they loan this customer $200,000. Additionally, ABC Auto World sells cars, completes a loan to the customer for the purchase of the car, and sells the loan to the bank. The loan is sold to the bank without any recourse to ABC Auto World for the payment of that loan, unless the loan goes into default. These types of loans are commonly known as "dealer paper". This rule says that ABC Auto World's direct loan will not be added to the dealer paper loans, unless and until the individual who purchased the car and signed the "dealer paper" loan defaults. In that case you would add the $200,000 debt of ABC Auto World to Jim Smith's loan of $10,000 for the purchase of his car because Jim Smith is in default. You would want to check to ensure the $210,000 amount is in compliance with the 25% lending limit of the bank.

On page six, line 13, **section (f)**, you will find the combination rules. These rules set out various circumstances as to when the loans of one borrower should be combined with the loans of another borrower for determining compliance with the lending limit. In general, debt of one borrower will be combined with another borrower when proceeds of the loan are used for the direct benefit of the other borrower, or when a common enterprise exists. A common enterprise exists when 1)the repayment source on both the loans is the same, 2)when the borrowers are related through control and one borrower is dependent on the other borrower for more than 50% of their revenue, or 3)when separate individuals borrow from a bank to purchase a business in which their combined ownership will be more than 50% of the voting shares. These rules are new to the Kansas statutes but are a codification of the current policies and practices of the Office of the State Bank Commissioner. They are also very similar to the regulations of the Office of the Comptroller of the Currency.

There are also special rules relating to a corporate group. This is a new rule to the Kansas statutes and is also a new policy of the Office of the State Bank Commissioner. It places a maximum lending limit to a corporation and any subsidiaries of that corporation. ("Subsidiary" is defined as any corporation which is owned more than 50% by the other corporation.) It caps the lending to the entire corporate group at 50% of the bank's capital.

The last special rule dicusses what portion of a partnership's debt is aggregated with an individual's debt for determining compliance with the lending limit. The basic rules require a general partner's full partnership debt to be aggregated with their individual liability. In a limited partnership, only the portion the partnership is liable for would be aggregated with their individual debt for determining compliance. If the loan agreement sets liability for the partnership debt in a different manner than the partnership agreement, the loan contract will control for determining compliance with the lending limit.

The final section of the bill, **section (g)**, found on page eight, line eight, grants me, the commissioner, the power to order the correction of any violation of this law. If a bank fails to comply, as commissioner, I can proceed with the removal of a bank officer or director. The language found in this section of the bill was changed to make it easier to read but the power is the same as that which exists in the current law.

We are asking for two amendments to the bill. A copy of those amendments is attached to my testimony. First, on page five of the bill, under Special Rules, line 32, if a bank wishes to expand the amount they can loan one borrower by an additional ten percent they can do so if they have as collateral on the loan a first lien on real estate. Certain requirements must be met, however, before the bank can utilize the expanded limit. One such requirement is found beginning on line 38. It requires the first lien mortgage to be filed for twice the amount of the excess liability; that amount above the 25% limitation. It also requires the appraised value to equal twice the amount of the excess. We received several comments expressing concern with the requirement that the mortgage must be filed for twice the excess liability. Their concern can best be shared through an example.

The ABC Bank has a 25% lending limit of $500,000. Their expanded limit, using the additional 10%, would equal $700,000. The amount of the "excess liability" in this case is $200,000. The bill language currently says the first lien mortgage would have to be filed for twice the excess liability, or $400,000 in this case. The concern voiced to us by bankers and the reason for the requested amendment is that filing the mortgage for $400,000 gives the bank no additional protection on the $200,000 excess loan. That mortgage ONLY has to be tied to the excess portion, the $200,000. The first $500,000 can be secured by other collateral. By making the bank file their lien for twice the excess liability, the banker receives no additional benefit but passes on a sizeable filing fee to the borrower for recording the mortgage. We see this additional fee as unnecessary and burdensome to the consumer. We do want the appraised value to remain twice the amount of the excess liability to ensure there is margin in the collateral.

The second amendment is small and can be found on page seven of the bill. We are adding a "(D)" in front of the sentence beginning on line nine. Adding the "(D)" will clarify that this sentence is not part of (C) and should be read in conjunction with the rest of (f) (3) and the rules that apply to common enterprises.

I will be happy to answer any questions regarding my testimony or the proposed amendments. I ask for favorable consideration of both the bill and the amendments.

1 limit calculation date unless new funds are advanced.
2 (2) If the bank's lending limit increases subsequent to the origination
3 date, a bank may use the current lending limit to determine compliance
4 when advancing funds. An advance of funds includes the lending of money
5 or the repurchase of any portion of a participation.
6 (3) If the bank's lending limit decreases subsequent to the origination
7 date, a bank is not prohibited from advancing on a prior commitment
8 that was legal on the date the commitment was made.
9 (d) Exemptions. That portion of a loan which is continuously secured
10 on a dollar for dollar basis by any of the following will be exempt from
11 any lending limit:
12 (1) A guaranty, commitment or agreement to take over or to purchase,
13 made by any federal reserve bank or by any department, bureau, board,
14 commission, agency or establishment of the United States of America,
15 including any corporation wholly owned, directly or indirectly by the
16 United States;
17 (2) a perfected interest in a time deposit account in the lending bank.
18 In the case of a time deposit which may be withdrawn in whole or in part
19 prior to maturity, the bank shall establish written internal procedures to
20 prevent the release of the deposit;
21 (3) a bonded warehouse receipt issued to the borrower by some other
22 person;
23 (4) treasury bills, certificates of indebtedness, or bonds or notes of the
24 United States of America or instrumentalities or agencies thereof, or those
25 fully guaranteed by them;
26 (5) general obligation bonds or notes of the state of Kansas or any
27 other state in the United States of America;
28 (6) general obligation bonds or notes of any Kansas municipality or
29 quasi-municipality; or
30 (7) a perfected interest in a repurchase agreement of United States
31 government securities with the lending bank.
32 (e) Special Rules. (1) The total liability of any borrower may exceed
33 the general 25% limit by up to an additional 10% of the bank's capital.
34 To qualify for this expanded limit:
35 (A) The bank shall have as collateral a first lien or liens on real estate
36 securing a portion of the liability equal to at least the amount by which
37 the total liability exceeds the 25% limit;
38 (B) the amount of the recorded lien or liens ~~and the appraised value~~
39 ~~of the real estate~~ shall ~~each~~ equal at least ~~twice~~ the amount of the [illegible]ss
40 liability; ~~and~~

(C) the appraised value of the real estate shall equal at least twice the amount of the excess liability; and

41 ~~(C)~~ (D) a portion of the loan equal to at least the excess liability sha[illegible]
42 installment payments sufficient to amortize that portion within 20 years
43 (2) That portion of any loan endorsed or guaranteed by a borrower

will not be added to that borrower's liability until the endorsed or guaranteed loan is past due 10 days.

(3) If the total liability of any active bank officer will exceed $50,000, prior approval from the bank's board of directors shall be noted in the minutes.

(4) To the extent they are insured by the federal deposit insurance corporation, time deposits purchased by a bank from another financial institution shall not be considered a loan to that financial institution and shall not be subject to the bank's lending limit.

(5) Third-party paper purchased by the bank will not be considered a loan to the seller unless and until the bank has the right under the agreement to require the seller to repurchase the paper.

(f) Combination Rules.

(1) General Rule. Loans to one borrower will be attributed to another borrower and their total liability will be combined:

(A) When proceeds of a loan are to be used for the direct benefit of the other borrower, to the extent of the proceeds so used; or

(B) when a common enterprise is deemed to exist between the borrowers.

(2) Direct Benefit. The proceeds of a loan to a borrower will be deemed to be used for the direct benefit of another person and will be attributed to the other person when the proceeds, or assets purchased with the proceeds, are transferred to another person, other than in a bona fide arm's length transaction where the proceeds are used to acquire property, goods or services.

(3) Common Enterprise. A common enterprise will be deemed to exist and loans to separate borrowers will be aggregated:

(A) When the expected source of repayment for each loan or extension of credit is the same for each borrower and neither borrower has another source of income from which the loan, together with the borrower's other obligations, may be fully repaid;

(B) when both of the following circumstances are present:

(i) Loans are made to borrowers who are related directly or indirectly through common control, including where one borrower is directly or indirectly controlled by another borrower. Common control means to own, control or have the power to vote 25% or more of any class of voting securities or voting interests or to control, in any manner, the election of a majority of the directors, or to have the power to exercise a controlling influence over the management or policies of another person; and

(ii) substantial financial interdependence exists between or among the borrowers. Substantial financial interdependence is deemed to exist when 50 percent or more of one borrower's gross receipts or gross expenditures (on an annual basis) are derived from transactions with the other bor-

rower. Gross receipts and expenditures include gross revenues, expenses, intercompany loans, dividends, capital contributions and similar receipts or payments; or

(C) when separate persons borrow from a bank to acquire a business enterprise of which those borrowers will own more than 50% of the voting securities or voting interests, in which case a common enterprise is deemed to exist between the borrowers for purposes of combining the acquisition loan.

(D) *An employer will not be treated as a source of repayment for purposes of determining a common enterprise because of wages and salaries paid to an employee.*

(4) Special Rules for Loans to a Corporate Group. (A) Loans by a bank to a borrower and the borrower's subsidiaries shall not, in the aggregate, exceed 50% of the bank's capital. At no time shall loans to any one borrower or to any one subsidiary exceed the general lending limit of 25%, except as allowed by other provisions of this section. For purposes of this paragraph, a corporation or a limited liability company is a subsidiary of a borrower if the borrower owns or beneficially owns directly or indirectly more than 50 percent of the voting securities or voting interests of the corporation or company.

(B) Loans to a borrower and a borrower's subsidiaries that do not meet the test contained in subsection (f)(4)(A) will not be combined unless either the direct benefit or the common enterprise test is met.

(5) Special Rules for Loans to Partnerships, Joint Ventures and Associations. (A) As used in this subpart (5), the term "partnership" shall include a partnership, joint venture or association. The term partner shall include a partner in a partnership or a member in a joint venture or association.

(B) General Partner. Loans to a partnership are considered to be loans to a partner, if by the terms of the partnership agreement that partner is held generally liable for debts or actions of the partnership.

(C) Limited Partner. If the liability of a partner is limited by the terms of the partnership agreement, the amount of the partnership debt attributable to the partner is in direct proportion to that partner's limited partnership interest.

(D) Notwithstanding the provisions of subsections (f)(5)(B) and (f)(5)(C), if by the terms of the loan agreement the liability of any partner is different than delineated in the partnership agreement, for the purpose of attributing debt to the partner the loan agreement shall control.

(E) Loans to a partner are not attributed to the partnersh[illegible]es either the direct benefit or the common enterprise test is met.

(F) Loans to one partner are not attributed to other partners unless either the direct benefit or common enterprise test is met.

4-7

The KANSAS BANKERS ASSOCIATION
A Full Service Banking Association

March 11, 1996

To: House Financial Institutions and Insurance Committee

From: Kathy Taylor, Kansas Bankers Association

Re: **SB 666**

Mr. Chairman and Members of the Committee:

Thank you for the opportunity to appear today in support of **SB 666**. This bill amends KSA 9-1104 by making meaningful changes in the state banks' lending limit law.

As you know, this statute provides a limitation on the amount of outstanding debt one "borrower" may have at a bank. Over the years, as with many laws, this statute was amended many times to account for changes needed. As the statute has been amended piecemeal, it has become difficult to read and understand. We support the changes made by **SB 666** first of all, because they bring clarity to the lending limit rules.

We also support the policy changes made in **SB 666**. We believe the change in the general lending limit will help keep Kansas banks competitive with other lenders in the market. There are so many competitors which do not have the same restrictions placed on their lending practices, and while we understand the reason for the limitation in banking, we believe the change will give a bank a few more opportunities in the market place.

SB 666 is a positive step for borrowers, bankers and the agency that regulates the industry. We respectively ask for your favorable consideration of **SB 666**.

House FI&I
Attachment 5
March 11, 1996

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