Approved: Jan. 21, 1998
Date

MINUTES OF THE Senate Committee on Financial Institutions and Insurance.

The meeting was called to order by Chairperson Don Steffes at 9:00 a.m. on January 15, 1998 in Room 529-S of the Capitol.

All members were present except: Senator Praeger

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

Conferees appearing before the committee: Bill Caton, Consumer Credit
Brad Smoot, Blue Cross/Blue Shield
Tom Wilder, Kansas Insurance Department

Others attending: See attached list

Bill Caton, Consumer Credit Commissioner, requested changes to the Kansas Uniform Consumer Credit Code which would define origination fees as well as including in section 9 the various prepaid finance charges that are paid up front by a borrower (Attachment 1). Interest rates have been deregulated in the marketplace and the problem of used car dealers charging exorbitant rates was discussed. The ensuing result is that customers have been forced to buy older cars in order to lower their monthly payments due to the very high interest rates.

Senator Feleciano moved for the introduction of this proposal into legislation. The motion was seconded by Senator Brownlee. Motion carried.

An informational meeting on premium tax credits on medicare supplemental policies was held for the benefit of the Committee. Tom Wilder, Kansas Insurance Department, presented explanatory testimony on the proposed legislation which would provide relief for those companies complying with the Commissioner's request to provide insurance for the disabled under age 65 at the rate of 150% of the rate charged for individuals age 80. These costs have been absorbed by the companies and the proposed tax credit would allow them to recoup some of their losses (Attachment 2).

Brad Smoot spoke on behalf of Blue Cross/Blue Shield and presented the history of their involvement in providing supplemental insurance for disabled who were on medicare (Attachment 3.) Most of these disabled were or are on kidney dialysis and the costs are on-going. Persons eligible for medicare are not eligible to be placed in the high-risk pool. Bill Pitsenberger, General Counsel for BC/BS, said that medicare supplemental insurance is not income dependent. Prior to 1996 BC/BS received adequate premiums to offset the losses but since complying with the Commissioner's request and becoming "the good Samaritan" their losses have increased substantially. Their losses can only be absorbed within their medicare book of business.

The KID would be asked to approve any increase in rates and an auditor would provide proof of eligibility of any ensuing tax credits. This bill would decrease the tax premiums for BC/BS by 20% the first year. By 2000 BC/BS rates will be 1/3 of what their actual costs are. New persons will be entering the group and the loss of money will continue. Losses for BC/BS are more than $1 million per year. Johnson and Wyandottee counties are not involved as they are covered under BC/BS of Kansas City which is not required to provide medicare supplemental insurance at a lowered rate for the disabled.

The meeting adjourned at 10:00 a.m. The next meeting will be held on January 20, 1998.

SENATE FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE GUEST LIST

DATE: 1-15-98

NAME	REPRESENTING
Tom Wilder	Kansas Insurance Department
Teresa Hillenauer	HIAA
Callie Dell Denton	KS Association of Health Plans
Pat Morris	KAIA
Don Lynn	BC/BS of KS.
Brad Smoot	BC/BS of KS
Roger Prawl	Ks. Gov. Consult.
Susan Anderson	Heim + Weis
Bill Pitsenberger	Blue Cross
Mike Astle	Community Bankers Assn
David Hanson	Ks Insur. Assns
Lee Wright	Farmers Ins Group
Kathey Olsen	Ks Bankers Assn.
[illegible]	Via Christi
Matthew Goddard	HCBA

REQUESTED CHANGES
KANSAS UNIFORM CONSUMER CREDIT CODE

1. AMEND 16a-1-301(7)(b) TO READ AS FOLLOWS:

(b) reasonable expenses *not included in the origination fee or payable to an assignee* incurred by the lender in connection with the making, closing, disbursing, extending, readjusting or renewing the debt which are payable to third parties not relate to the lender, except that reasonable fees for an appraisal made by a lender or related party are permissible.

2. DEFINE "ORIGINATION FEE" AS SUGGESTED BY THE ATTORNEY GENERAL (new 16a-1-301 (28))

"origination fee" means a fee associated with the making, closing or disbursing of a consumer credit transaction by a lender or assignee of the lender which is intended to compensate lender or assignee of the lender for all cost incurred in making, closing of disbursing a consumer credit transaction, exclusive of closing costs defined in 16a-1-301(7), interest rate reduction charges paid by the consumer at closing or broker fees paid to third parties not related to the lender or assignee of the lender.

3. DELETION OF 16a-2-309(b) (1) and (2) WHICH REFERS TO MAKING LOANS IN THE SAME PLACE GOODS ARE SOLD OR LEASED.

This provision is no longer necessary since interest rates on retail sales contracts has been "de-regulated" and do not have rate ceilings less than consumer loan contracts.

Senate F D & D
Attachment 1
1/15/98

State of Kansas
Office of the Attorney General
301 S.W. 10TH AVENUE, TOPEKA 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

JUN 17

June 16, 1997

MAIN PHONE: (913) 296-2215
CONSUMER PROTECTION: 296-3751
FAX: 296-6296

Memo

To: Bill Caton
From: Mary Feighny

Subject: Mortgage broker fees

You inquire concerning whether K.S.A. 16a-2-401(9)(a) [hereinafter referred to as section 9] restricts mortgage broker fees to 3% of the amount financed. Section 9(a) provides as follows:

> "In addition to the applicable finance charge...prescribed by law, a supervised lender may contract for and receive a nonrefundable ***origination fee*** not to exceed 3% of the amount financed on any consumer loan secured by an interest in land, which fee shall be a nonrefundable, prepaid finance charge." (Emphasis added.)

As you point out, an origination fee is not defined in the UCCC [Code] so the issue is whether a mortgage broker fee which is paid up front by a borrower to a supervised lender is an "orgination fee". If so, then the fee is limited to 3% of the amount financed.

I reviewed the legislative history of section 9 which was placed into the Code in 1986. Evidently, prior to 1986 the Code prohibited the charging of "points" or prepaid finance charges on fixed rate real estate loans but allowed a charge of unlimited points on variable rate loans. (Statement of Assistant Consumer Credit Commissioner Mel Battin, *Minutes of the House Committee on Commercial and Financial Institutions*, March 6, 1986) The then Commissioner filed a lawsuit against a supervised lender who was charging 15 points on variable rate loans on the basis that such a charge was unconscionable. The lawsuit settled with the lender agreeing not to charge more than 3 points and the Commissioner issued Administrative Interpretation No. 107 permitting all supervised lenders to charge no more than 3 points on variable rate transactions. This administrative interpretation was codified by the legislature in 1986 and was extended to apply to fixed rate loans as well as variable rate loans.

Stan Lind, counsel for the Kansas Association of Financial Services, testified that without the ability to charge points a lender could not afford to make fixed term second mortgage loans and, therefore, borrowers who desired fixed rate loans were unable to get them. (Minutes, *House Committee on Commercial and Financial Institutions*, February 20, 21,25 1986.) The justification for the origination

fee was that lenders who sold their second mortgage real estate loans to the secondary market had to pay a 1% origination fee plus a 1-1.5% private mortgage insurance premium. This cost was then passed on to the borrower.

Section 9 was amended in 1988 to reflect that the origination fee is a finance charge that is paid up front and is in addition to the finance charge. Moreover, the legislature extended the origination fee to all consumer loans. Jim Maag of the Kansas Bankers Association testified that many banks were relunctant to make small loans because the finance charge was insufficient to cover the cost of processing the loan and that the availability of a nonrefundable fee would be a "strong incentive" for creditors to consider making small loans. (Minutes, *Senate Committee on Financial Institutions and Insurance*, February 17, 1988)

From the legislative history, it appears that an origination fee is an expense associated with the cost of processing a loan, sometimes referred to as "points" which is passed along to the borrower. The next question is whether a mortgage broker fee can be characterized as an orgination fee.

A mortgage broker finds loans for borrowers. A mortgage broker is the middleman between a borrower and a lender in a situation akin to an insurance broker who finds the best insurance deal for a customer. A broker makes money by charging the borrower fees and points in a variety of different manners. *Note, The Mortgage Contingency Clause*, 17 Cardozo Law Review, 299, 303 (December, 1995)

> "The mortgage broker also receives commission rebates from the lender in the form of a discounted mortgage rate (sometimes amounting to two or more points). Generally, the costs to the borrower of obtaining a mortgage are the same whether the borrower gets the mortgage from a mortgage broker or an institutional lender. In consideration of the lender's discount, the mortgage broker undertakes some of the costly and time consuming tasks normally performed by the lender. These tasks include collecting financial documentation and arranging appraisals of the property. In addition, a mortgage broker may run credit reports and compile required documentation." *Note* at P. 303.

Stacey Brigdon (sp?) who sits on the board of the Kansas Mortgage Brokers Association explained to me the variety of mortgage broker fee arrangements that are employed between a lender and a broker and between a broker and a borrower. The arrangements are varied but it appears that a mortgage broker fee is not the kind of origination fee that the legislature had in mind when it enacted section 9.

You may want to consider legislation that defines "origination fee" or, in the alternative, broadens the scope of section 9 by including all the various prepaid finance charges that are paid up front by a borrower.

KANSAS

OFFICE OF CONSUMER CREDIT COMMISSIONER

Bill Graves
Governor

Wm. F. Caton
Commissioner

May 28, 1997

Ms. Mary Feighny
Office of the Attorney General
2nd Floor, Kansas Judicial Center
Topeka, Kansas 66612

Dear Mary:

This office has taken a position on prepaid finance charges which is coming under challenge from the industry. My request is for you to review our opinion to help me determine if it is reasonable and within the scope of the Kansas Uniform Consumer Credit Code (UCCC).

K.S.A. 16a-2-401 (9)(a) states, "In addition to the applicable finance charge or rate of interest prescribed by law, a supervised lender may contract for and receive a nonrefundable origination fee not to exceed 3% of the amount financed on any consumer loan secured by an interest in land, which fee shall be a nonrefundable, prepaid finance charge." You will note that the fee referred to in this section is an "origination fee" which is not a defined term anywhere in the UCCC. It is our position that regardless of what the fee is called, it was the original legislative intent that <u>all</u> prepaid finance charges are limited to a maximum of 3%.

Since September 30, 1996, Truth-in-Lending Regulation Z requires all mortgage broker fees to be included in the finance charge. I believe mortgage broker fees have always been the finance charge and Reg. Z finally recognized that and required it to be disclosed as a finance charge. It is our position that if this fee is paid up front, it falls under the 3% limitation of prepaid finance charges. Lenders are contending that a mortgage broker fee is not a loan origination fee (whatever that is!) and that it is not limited to 3% as stated in the UCCC. Many mortgage broker fees are 5% and upward of the loan amount which is a very substantial charge.

If a brokers fee is charged, it is our position that it has to be earned by the lender on an actuarial basis over the life of the loan, which is a very unpopular stand with the industry. If the lender pays a $5,000 broker fee and the borrower pays the loan off early, the lender cannot recoup a portion of the brokers fee.

1-4

JAYHAWK TOWER, 700 S.W. JACKSON, SUITE 1001 / TOPEKA, KANSAS 66603 / (913) 296-3151 / FAX: (913) 296-6810

I am anticipating that our position will be challenged, possibly in court, because of the significant dollar amounts involved. Please review this situation and report whether you concur or not with our position. I have enclosed a copy of information regarding the Truth-in-Lending treatment of mortgage broker fees. If you need any additional information, please do not hesitate to contact me. Your earliest response will be appreciated.

Sincerely,

Wm. F. Caton
Commissioner

WFC:dr

Enclosures

The new rule on debt cancellation fees will also become effective on October 21. The rule imposes no additional disclosure requirements. Creditors must continue to treat debt cancellation fees as finance charges; when the new rule becomes effective creditors will have the option of excluding voluntary debt cancellation fees from the finance charge if they meet the specified requirements.

III. Section-by-Section Analysis

Subpart A -- General

Section 226.2 -- Definitions and Rules of Construction

2(a) Definitions

2(a)(6)

Paragraph 2(a)(6) is adopted as proposed. For purposes of the Board's rules implementing the Home Ownership and Equity Protection Act of 1994 in Subpart E of Regulation Z, the "business day" definition for rescission applies. The Board has also updated the list of legal public holidays to include the Birthday of Martin Luther King, Jr.

Section 226.4 -- Finance Charge

4(a)(1) Charges by third parties

Paragraph 4(a)(1) reflects the general rule for third party charges currently contained in comment 4(a)-3 of the Official Staff Commentary. A slight modification has been made for clarity. In general, amounts charged by third parties are included in the finance charge if the creditor requires the use of the third party or retains any portion of the charge (in which case the portion retained is included as a finance charge).

4(a)(2) Special rule: closing agent charges

Paragraph 4(a)(2) incorporates the substance of section 2(a) of the 1995 Amendments, and is consistent with the existing interpretation in comment 4(a)-4 of the Official Staff Commentary. Under the rule, a fee charged by a third-party closing agent is included in the finance charge only if the creditor requires the imposition of the charge or the provision of the service, or retains any portion of the charge. Accordingly, a courier fee charged by a third-party closing agent is only a finance charge if the creditor requires the use of the courier (or to the extent the creditor retains a portion of the charge). The rule only applies to the third-party serving as the closing agent with respect to that loan. The final rule has also been modified slightly to clarify the term "closing agent."

4(a)(3) Special rule: mortgage broker fees

Paragraph 4(a)(3) contains a new rule regarding the treatment of mortgage broker fees, to implement section 106(a)(6) of the TILA (15 U.S.C. § 1605(a)(6)), which becomes effective on September 30, 1996. The rule requires that all fees charged by a mortgage broker and paid directly by the consumer be included in the finance charge, whether the fee

is paid to the broker or to the lender for delivery to the broker. A fee charged by a mortgage broker will be excluded from the finance charge only if it is the type of fee that would also be excluded when it is charged by the creditor. In the case of application fees charged by a mortgage broker, such fees may be excluded from the finance charge if the mortgage broker charges the fee to all applicants for credit, whether or not credit is actually extended.

Several commenters questioned the basis for requiring creditors to disclose, as finance charges, fees that the creditor neither imposes nor requires. They also expressed concern about creditors' duty for including brokers' fees in Truth in Lending disclosures when the existence or amount of such fees may not be known to the creditor.

The new rule is mandated by the 1995 Amendments. Under the Real Estate Settlement Procedures Act (RESPA)(12 U.S.C. § 2601 et. seq.), amounts paid by a consumer directly to a mortgage broker or through the lender for delivery to the mortgage broker are already required to be disclosed to the borrower at the loan closing on the HUD-1 or HUD-1A. See 24 C.F.R Part 3500 Appendix A, Appendix B ¶ 12. The Board believes that the new TILA disclosure requirement should not pose a significant additional burden, and that it is reasonable to require creditors to use the information from the HUD forms in calculating the finance charge. Accordingly, the Board expects that creditors will adopt practices and procedures consistent with their affirmative obligation to obtain the relevant information from the parties involved.

In the May proposal, the Board noted that fees paid by the funding party to a broker as a "yield spread premium," and already included in the finance charge as interest or as points should not be double counted. Several commenters sought further clarification, noting that brokers may be compensated by the lender under various arrangements. The proposal's reference to "yield spread premiums" was only intended to be one example of lender-paid compensation that must be separately disclosed on the HUD-1 under the current RESPA rules, but should not be double counted because it is already included as part of the finance charge.

4(b) Example of finance charge
4(b)(10) Debt cancellation fees

Debt cancellation agreements serve a purpose similar to credit insurance, even though the products are not identical in all respects. Paragraph 4(b)(10) clarifies that fees charged by creditors for debt cancellation coverage that is written in connection with a credit transaction are considered finance charges. Conditions under which voluntary debt cancellation fees may be excluded from the finance charge are set forth in paragraph 4(d)(3).

Comments by some insurance providers noted that the term "debt cancellation agreement" is not commonly used in reference to GAP agreements. For purposes of Regulation Z, however, the term "debt cancellation agreement" is used generically to refer to a contract between a debtor and creditor providing for satisfaction of all or part of the debt

John J. McManus & Associates, P.C.
Attorneys and Counselors at Law

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May 19, 1997

Mr. William Caton, Commissioner
State of Kansas
700 Southwest Jackson Street
Suite 1001A 94520
Topeka, KS 66603

Via fax 913-296-6810 and Regular Mail

Re: KSA Section 16a-2-401(9)(a)

Dear Mr. Caton:

This letter follows our several phone conversations to your office over the past several weeks on behalf of a mortgage lending client we represent in Georgia. The issue that we are struggling with involves the payment of Brokers Fees in Kansas and there relationship to the 3% "cap" on the amount financed in mortgage lending transactions. Please note the following:

1. Since October, 1996, the fees paid to mortgage brokers have been placed in the amount financed in order to determine the APR that the respective borrower(s) pay in connection with the subject mortgage loan transaction.

2. The above-referenced section of the Kansas law apparently states, among other matters, that the amount financed that is placed in the APR is "capped" at 3.0%.

If the above is accurate, it appears to the writer, and at least one of your employees, that the brokers fees paid in connection with the origination of a mortgage loan must fit into that 3% cap. However, if the brokers fees are somehow not considered in that "amount financed" calculation, as is the opinion of at least one of your employees, then the brokers fees are either unregulated or otherwise "capped".

Therefore, the purpose of this letter is to obtain clarification of exactly how Brokers Fees are considered in the State of Kansas in order that we might properly advise our client accordingly. Thank you in advance for your prompt response to this inquiry. Please advise any questions or comments engendered hereby.

Sincerely,
John J. McManus & Associates, P.C.

John J. McManus, Esq.

State of Kansas
Office of the Attorney General
301 S.W. 10TH AVENUE, TOPEKA 66612-1597

CARLA J. STOVALL
ATTORNEY GENERAL

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September 16, 1997

Memo

To: Bill Caton
From: Mary Feighny

Subject: Are buydown points subject to the 2% ceiling pursuant to K.S.A. 16a-2-401(9)(b)?

My memo to you dated June 16, 1997 discussed the concept of the origination fee as applied to consumer loans secured by real property. In that memo, I concluded that the intent behind this type of fee was to allow financial institutions to recoup the cost of processing a loan. In 1988 this same fee was extended to all consumer loans and codified at K.S.A. 16a-2-401(9)(b). Jim Maag testified on behalf of the Kansas Bankers Association that extending the origination fee to all consumer loans would be a positive move because banks were relunctant to make small loans because the finance charge alone was insufficient to cover the costs of processing the loan. He indicated that an origination fee would be a strong incentive for creditors to consider making smaller loans to a wider range of customers. (*Minutes,* Senate Committee on Financial Institutions, February 18, 1988, Attachment V).

The letter from GreenTree defines a "buydown point" as a fee paid by a customer who purchases a specific interest rate. The customer pays an upfront fee and in return gets a loan with a lower interest rate. Given the legislative intent behind the origination fee, it doesn't appear that this kind of fee is a charge for processing the loan. Rather, it's a *quid pro quo* for getting a lower interest rate. In short, it's my opinion that this type of fee does not fall within the parameters of K.S.A. 16a-2-401(9)(b).

If you think that lendors need to be reined in, consider seeking an amendment to the Code which puts a ceiling on mortgage brokers fees, buydown points and any other devices used by lendors that are detrimental to Kansas consumers.

KANSAS

OFFICE OF CONSUMER CREDIT COMMISSIONER

Bill Graves
Governor

Wm. F. Caton
Commissioner

September 12, 1997

Ms. Mary Feighny
Office of the Attorney General
301 SW Tenth Ave.
Topeka, Kansas 66612

Dear Mary:

Enclosed is a copy of a response from Green Tree Financial Corporation regarding our examination of their operation. As you can see from their response, they are disagreeing with our position regarding "buydown points" are included in the 3% origination fee in K.S.A. 16a-2-104 (9)(b).

Their definition of buydown points found in the second paragraph of page two accurately defines this fee but it is our position that this is an origination fee (which is not defined in the code) as it is paid to the seller for his cost of lowering the interest rate. Buydown points significantly increase interest rates if loans are paid off early and are widely viewed as a deterrent to prepayment of loans.

Please review this situation and respond to this office at your earliest convenience. I am not requesting an official attorney general's opinion but am seeking your position on this matter.

Sincerely,

Bill

Wm. F. Caton
Commissioner

WFC:dr
Enclosure

1-10

KANSAS COMMENT

Under this section, all closed-end supervised installment loans of $1,000 or less must be repayable in substantially equal installments at equal periodic intervals (normally one month), except where irregularities are appropriate to meet the debtor's needs with respect to seasonal or irregular income. In addition, limits are imposed on the aggregate term of such loans depending upon the amount financed. Compare the limits on balloon payments under K.S.A. 16a-3-308.

16a-2-309. (UCCC) Conduct of business; other than making loans. (a) A licensee may conduct the business of making loans under K.S.A. 16a-1-101 through 16a-9-102 within any office, room or place of business in which any other business is solicited or engaged in, or in association or conjunction therewith, unless the commissioner shall find, after a hearing, that the other business is of such nature that such conduct tends to conceal evasion of such portion of this act or of the rules and regulations made thereunder and shall order such licensee in writing to desist from such conduct.

(b) (1) Except as provided in subsection (2), no licensee authorized to make supervised loans pursuant to section 16a-2-301 may engage in the business of selling or leasing of goods, at a location where supervised loans are made. In this section, "location" means the entire space in which supervised loans are made and must be separated from any space where goods are sold, leased, or displayed by walls which may be broken only by a passageway to which the public is not admitted.

(2) This section does not apply to

(a) sales or leases of goods or services pursuant to a lender credit card made at a place of business other than that of a licensee;

(b) occasional sales of property used in the ordinary course of business of the licensee;

(c) sales of items of collateral of which the licensee has taken possession; or

(d) sales of items by a licensee who is also authorized by law to operate as a pawnbroker.

History: L. 1973, ch. 85, § 26; Jan. 1, 1974.

KANSAS COMMENT

1. Subsection (a) allows a licensed lender to make supervised loans through a separate office located in a retail store unless the administrator finds that the arrangement would tend to conceal evasion of the U3C. An example of an operation which might be shut down by the administrator under this section is a loan office in a dealer's place of business to which credit buyers are referred in order to insulate the lender from defenses of the consumer. See K.S.A. 16a-3-405.

2. Subsection (b) prohibits a licensee from making supervised loans from the same location at which the licensee sells or leases goods. This rule is based on the assumption that any dual lender-seller operation will almost automatically lead to circumvention of the U3C. Tie-in sales of goods or services in connection with loans are flagrant violations of the U3C because they are carried on to evade rate ceilings. Exceptions are made for lender credit cards honored at a separate merchant's place of business, occasional sales of a licensee's business property, foreclosure sales, and sales by a lender licensed both under the U3C and the Kansas pawnbroker's law (K.S.A. 16-706 et seq.).

Part 4

CONSUMER LOANS; MAXIMUM FINANCE CHARGES

16a-2-401. (UCCC) Finance charge for consumer loans; exempting loans served by an interest in land; nonrefundable origination fee. (1) With respect to a consumer loan, including a loan pursuant to open end credit, a lender may contract for and receive a finance charge, calculated according to the actuarial method, not exceeding 18% per year on the unpaid balance of the amount financed not exceeding $1,000 and 14.45% per year on that portion of the unpaid balance in excess of $1,000.

(2) As an alternative to the rates set forth in subsection (1), with respect to a supervised loan made under a license issued by the administrator, including a loan pursuant to open end credit, a supervised lender may contract for and receive a finance charge, calculated according to the actuarial method, not exceeding the equivalent of the greater of either of the following: The total of: (a) Thirty-six percent per year on that part of the unpaid balance of the amount financed which is $300 or less; and

(b) twenty-one percent per year on that part of the unpaid balance of the amount financed which is more than $300, but does not exceed $1,000; and

(c) fourteen and forty-five hundredths percent per year on that portion of the unpaid balance of the amount financed which is more than $1,000; or

(d) eighteen percent per year on the unpaid balance of the amount financed.

(3) This section does not limit or restrict the manner of calculating the finance charge, whether by way of add-on, discount, or otherwise, so long as the rate of the finance charge does not exceed that permitted by this section. The finance charge may be contracted for and

Kathleen Sebelius
Commissioner of Insurance
Kansas Insurance Department

MEMORANDUM

To: Senate Financial Institutions
and Insurance Committee

From: Tom Wilder

Re: Premium Taxes (Medicare Supplement Policies)

Date: January 14, 1998

I am appearing today to ask for your support for legislation which will provide a premium tax credit for health insurance companies which are selling Medicare Supplement policies to individuals with a disability. A copy of the bill draft is attached to my testimony.

Prior to April 28, 1996, health insurers which sold Medicare Supplement policies to disabled applicants were permitted to medically underwrite the policies and could turn down individuals for coverage. In 1996, the Insurance Department issued regulations which required such policies to be guaranteed issued to all disabled applicants who applied for coverage after April 28, 1996. In addition, the Department required that the rate charged for policies issued prior to that date could not exceed 150% of the rate charged for individuals age 80. Once a disabled individual reaches age 65, they are charged the same rate as anyone else who is Medicare eligible by reason of age.

The cost of claims for disabled individuals is generally higher than for people who qualify for Medicaid Supplement coverage due to age. The legislation is designed to accomplish two things - to reduce the rates charged disabled individuals who enrolled in a Medicare Supplement policy prior to April 28, 1996 and to give insurance carriers a tax credit for any losses on that block of business. It is estimated that the cost to the state of

Senate FI&I
Attachment 2
Jan 15, 1998

420 SW 9th Street
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☎ Consumer Assistance Hotline
1 800 432-2484 (Toll Free)

Kansas for this legislation will be approximately $1.0 million annually, although this amount will decrease over time as the individuals in the block of business reach age 65.

This legislation primarily impacts Blue Cross and Blue Shield of Kansas and most of the premium tax credit would go to that carrier. However, Blue Cross voluntarily provided Medicaid Supplement coverage to disabled individuals on a guaranteed issue basis prior to April 28, 1996. This decision to guarantee issue coverage and the regulations from the Insurance Department which required Blue Cross to rate those policies no higher than 150% of age 80 rates, resulted in losses to Blue Cross which would be recouped through the tax credit. The Department believes it is good public policy for the state to help subsidize those losses rather than placing the burden on Blue Cross policyholders.

I would ask that the Committee favorably support this legislation.

DRAFT (Premium Tax/Medicare Supplement Policies) - 1/13/98

_____ Bill No. _____

AN ACT concerning insurance premium taxes; providing for tax credits for policies sold to individuals who purchased Medicare supplement policies prior to April 28, 1996 who were eligible to purchase such insurance because of a disability.

Be it enacted by the Legislature of the State of Kansas:

Section 1. (a) On and after January 1, 2000, the premiums which an issuer of a Medicare supplement policy as defined in K.S.A. 40-2221 and amendments thereto, may charge for a Medicare supplement policy issued to a person eligible for Medicare by reason of disability prior to April 28, 1996 shall not exceed the premium charged by such issuer for a policy containing the same benefits issued to a person age 65 who is eligible for Medicare by reason of age.

(b) On or before July 1, 1998, issuers of Medicare supplement coverage to persons eligible for Medicare by reason of disability having policyholders who acquired such coverage prior to April 28, 1996 shall submit to the commissioner of insurance a plan by which such issuer shall so adjust its rates that the rates charged as of January 1, 2000, shall comply with the provisions of subsection (a). Such plan shall provide for a reduction of such rates in an amount no less than one-half of the amount needed to bring such rates into compliance with subsection (a) in 1999. The commissioner shall approve or disapprove such plan based upon meeting the standards set forth herein. In the event of disapproval by the commissioner of such rates, the issuer shall be entitled to notice and hearing pursuant to the provisions of the administrative procedures act as applied to actions of the commissioner of insurance.

Section 2. An issuer of Medicare supplement policies which issued such policies without underwriting to persons eligible for Medicare by reason of disability prior to April 28, 1996, shall be entitled to a credit against premium taxes otherwise owing under K.S.A. 40-252 and amendments thereto to the extent of the difference between the actual claims and administrative expense incurred by such issuer for such coverage and the rates actually charged by such issuer. In order to claim such credit, the issuer shall provide with its

annual premium tax return an actuarial statement prepared by an independent consulting actuary setting forth the method of derivation of such difference. The issuer shall be entitled to such credit for premiums charged commencing April 28, 1996. Such issuer may claim the premium tax credit in the amount of such differences for 1996, 1997 and 1998 starting with premium taxes due for 1998, and may claim such premium tax credits for premiums charged in years subsequent to 1998 in the premium tax return for the year for which such premium tax is due.

Section 3. This act shall take effect and be in force from and after its publication in the Kansas Register.

BRAD SMOOT
ATTORNEY AT LAW

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**STATEMENT OF BRAD SMOOT, LEGISLATIVE COUNSEL
BLUE CROSS BLUE SHIELD OF KANSAS
SENATE FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE
REGARDING 1998 SENATE BILL NO. _____
JANUARY 15, 1998**

MR. CHAIRMAN AND MEMBERS:

Blue Cross Blue Shield of Kansas is a not for profit mutual life insurance company providing insurance benefits to more than 700,000 Kansans in 103 counties. BCBS employs nearly 2000 Kansans, mostly here in Topeka, and provides Medicare administration services in other states by contract with the federal government and Medicaid financial services by contract with the State of Kansas. On behalf of more than 160,000 Medicare policyholders we urge your support of SB _____. To understand the need for this legislation, you will want just a bit of history about Medicare Supplement policies and the regulatory changes made by the Kansas Insurance Department in 1996.

There are many insurance carriers which issue Medicare Supplement policies to the elderly. It is a very competitive environment. On the other hand, very few carriers have been willing to issue Medicare Supplement policies to the disabled. Blue Cross Blue Shield of Kansas has provided such coverage to the state's disabled population for more than 30 years. Indeed, some health care specialists encourage their disabled patients to apply for our coverage and assist them in finding funds to pay the premiums. These Medicare policies have been expensive, reflecting the higher than average health costs and risks associated with a disabled population. Prior to 1996, insurance companies were permitted to charge premiums sufficient to cover losses without a subsidy from their other insureds.

Senate FD&D
Attachment 3
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In 1995 Commissioner Sebelius ask all Med Supp carriers doing business in Kansas to voluntarily make available Med Supp coverage to disabled Medicare eligibles on the same basis as older Kansans. BCBS responded to the Commissioner's request. Few, if any, other carriers volunteered. In 1996, the Kansas Insurance Department issued an administrative regulation requiring all carriers marketing Medicare Supplement policies to also issue policies to the disabled and ordered rates for the disabled reduced to the age 65 Medicare rate. This change in public policy was intended to encourage a greater spreading of this high risk business while providing disabled Kansans with greater choice at more affordable rates.

In the future, this policy may improve access to health care coverage for the disabled and spread the business to more carriers. In the interim, however, those few companies which issued policies to the disabled before 1996 are not permitted to collect premium adequate to cover losses for this high cost/high risk population. Without the premium tax credit provided by this legislation, it will be the 160,000 elderly BCBS Med Supp policyholders who will bear the cost of the Department's 1996 change in policy.

With the state having made the decision to provide disabled Kansans with affordable health insurance, it would be unfortunate to put the entire burden of this laudable social policy on the backs of only a few older Kansans who may be least able to bear it. For these reasons, we would urge the Committee to recommend SB _____ favorably for passage.